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REPORTS OF THE

GOVERNMENT SUPERANNUATION FUND AUTHORITY

FOR THE YEAR ENDED 30 JUNE 2009

2009

GOVERNMENT SUPERANNUATION FUND
Te Pūtea Penihana Kāwanatanga

FOR THE YEAR ENDED 30 JUNE 2009

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Reports presented to the House of Representatives pursuant to Section 150(3) of the Crown Entities Act 2004.

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 2009.

A separate annual report has been prepared by the Authority on the Government Superannuation Fund (**GSF** or **the Fund**), beginning on page 23.

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

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

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

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

Features of the 2009 Year

- Investment performance was severely impacted by the global financial crisis.
- Added value from active management of international and New Zealand equities.
- Exclusion of direct investment in companies involved in the manufacture of cluster munitions and nuclear weapons, in terms of the Authority's Responsible Investment Policies.
- Tender undertaken to identify an organisation to undertake the development of a new and more sustainable system to be used in the administration of the GSF Schemes.

Investments

The investment performance of the Fund during the year was severely impacted by the global financial crisis which started in 2007, but deteriorated sharply in 2008. The flow-on effects from the United States sub-prime mortgage crisis dominated the year and led to the worst downturn in investment markets since the Great Depression.

The crisis resulted in the biggest fiscal and monetary policy intervention since World War II. Government actions were taken to avert a generalised banking collapse, ensure sufficient liquidity to support economic activity, and underwrite toxic assets.

This situation was extremely difficult to predict at the start of the financial year. The international credit crisis had yet to gather pace and Lehman Brothers was still a respected name on Wall Street. In holding the Official Cash Rate at 8.25 percent in June 2008, the Reserve Bank had projected little GDP growth over 2008, and a modest recovery thereafter. In the 2008 Budget, Treasury had forecast reasonable economic growth for New Zealand of over 2% for the year to March 2009. As we now know, by the end of the financial year New Zealand was firmly in the grip of a recession, General Motors was about to be 60% owned by the US Government and Lehman Brothers had disappeared along with several other large banks.

The downturn impacted on all investment funds invested in growth assets such as equities and property. The Fund was no exception. Notwithstanding its recent diversification into global private equity, absolute return strategies, commodities and global tactical asset allocation, the Fund was severely impacted by the downturn because of its widespread effect on markets. Fortunately, there has been some recovery in markets and the global economy through 2009.

The Board continues to focus on the long-term by making sure its strategy remains appropriate for a Fund that is expected to pay pensions for the next 60 years. This is achieved by broadly diversifying the Fund's exposures to risky assets, and by maintaining a set of high quality investment managers capable of adding value. The Board is constantly seeking to enhance the management of the Fund to meet the statutory requirements of best practice portfolio management and maximising return without undue risk to the Fund as a whole. Current initiatives include a detailed investigation of the potential benefits of more dynamic asset allocation and the assessment of new asset classes.

During the year the move from passive to active management of the international equities portfolio was completed with a number of new managers being appointed. Active management added value (when compared to benchmarks) for both New Zealand equities (+1.9%) and international equities (+2.8% before hedging costs), although total returns from both asset classes were negative. Active fixed interest management suffered from investing too early in credit securities, but has partially recovered in the second half of the financial year. The Fund benefited overall from the diversification into a global multi-asset class fund, which includes exposure to private equity and hedge funds, and global tactical asset allocation, but total returns were impacted by the cost of hedging foreign exchange in a volatile market.

The Board is confident that the investment strategy remains appropriate. Although recent events have little precedent, the Fund must maintain a significant exposure to growth assets in order to meet long term investment targets and this requires acceptance of periodic shocks to some degree.

Investing in a wide range of assets globally is prudent and the Board remains committed to that approach. Diversification of risk exposures and active management of investments, where appropriate, should enhance investment performance over time.

The Fund's deficit after tax for the year of $583.3 million represents a return of -16.8% (2008 : -6.7%) on average net assets. The table on the next page compares the Fund's investment returns against the Investment Performance Measure (**IPM**) (see page 4) over 1, 3 and 5 year periods ended 30 June 2009.

	1 year %	**3 years Annualised %**	**5 years Annualised %**
Fund	-16.8	-5.2	0.7
IPM	9.3	7.2	7.1

The Risk Parameter set for the Fund (see page 4) is to have no more than 1 in 10 chance in any one year of a loss greater than 6.0% of the total Fund (after tax). As the Fund is now into its ninth year of a diversified investment strategy, a deficit greater than the Risk Parameter is not unexpected. However, a deficit greater than 6% in successive years is an extreme event.

Full details of the Fund's Investment Strategy, Strategic Asset Allocation and investment returns can be found in the Investment Commentary on page 4.

Schemes

During the year a tender was undertaken to identify an organisation to undertake the development of a new and more sustainable system to be used in the administration of the GSF Schemes. The Board is reviewing the outcome of the tender, particularly the resources, experience and capability of the tenderers to undertake the work, the timetable and whether to undertake the project in stages, and the software language and development approach to be used in the project. Final decisions are likely to be made before the end of 2009.

Further comment on GSF Schemes' activity can be found on page 12 of this report.

Website

The Authority's website – *www.gsfa.govt.nz* – continues to be an important part of our communications strategy and contains comprehensive information on both the Authority and the Fund. It explains how the Authority operates and gives all members and interested parties immediate access to our latest quarterly investment results, as well as any changes the Authority makes to its policies, Investment Strategy and personnel.

Conclusion

The Board thanks the Minister of Finance and government officials for their support, and the management team and staff for their high level of work and commitment to meeting the Authority's objectives.

I also thank my fellow Board members for their expertise and commitment during the year.

Tim McGuinness
Chairman
Government Superannuation Fund Authority Board

GOVERNMENT SUPERANNUATION FUND AUTHORITY
INVESTMENT COMMENTARY

Investment Strategy

The Authority is required to invest the Fund on a prudent commercial basis. In so doing, 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.

Key features of the Investment Strategy set for the Fund are the Investment Objective, Investment Performance Measure and Risk Parameter, as set out below:

Investment Objective

To minimise the Crown's contribution to GSF by maximising the return on the assets of the Fund over the long term, without undue risk, and within a best practice framework.

Investment Performance Measure (IPM)

The performance of the Fund will be assessed by comparing the after tax return with the NZX New Zealand Government Stock Gross Index return (after tax) plus 2.5% per annum measured over rolling 10 year periods.

Risk Parameter

Having no more than 1 in 10 chance in any one year of a loss greater than 6.0% of the total Fund (after tax).

The IPM and Risk Parameter are reviewed at least annually, taking into account the investment and tax environment in which the Authority operates. No change was made to the IPM and Risk Parameter following the last annual review.

Strategic Asset Allocation

The Authority regularly reviews the Strategic Asset Allocation (**SAA**) of the Fund to ensure it remains appropriate and consistent with legislative requirements and best practice.

During the year the Authority refined the SAA, reallocating the economic exposures held indirectly through its multi-asset class investments to the other asset classes held by the Fund. The revised presentation provides a better indication of the underlying exposures of the Fund to the main asset classes.

Table 1, below, sets out the SAA which applied as at 30 June 2009 and 30 June 2008. Table 2 sets out the actual assets managed by the investment managers for each asset class.

Table 1

Asset Class	Strategic Asset Allocation at 30 June 2009 %	Strategic Asset Allocation at 30 June 2008 %	Actual Economic Exposures at 30 June 2009 %
Fixed interest	24.0	23.0	21.5
New Zealand equities	10.0	10.0	9.9
International equities	49.5	47.0	50.0
Real estate	8.0	7.0	7.1
Commodity futures	3.0	3.0	2.9
Multi-asset*	–	7.0	–
Global tactical asset allocation (now Absolute return)	5.5	3.0	8.6
TOTAL	**100.0**	**100.0**	**100.0**

*Multi-asset class is a diversified portfolio comprising listed equities, private equity, real estate and hedge funds.

All asset classes were within their rebalancing tolerances at 30 June 2009 and were maintained within the rebalancing tolerances during the year. Assets held in the absolute return asset class are subject to initial "lock up" provisions, which prohibit withdrawals until 2010 and 2011.

Table 2 below compares the actual asset allocation, as at 30 June 2009, and 30 June 2008.

Table 2

Asset Class	Investment Assets Actual at 30 June 2009		Investment Assets Actual at 30 June 2008	
	$000	**%**	**$000**	**%**
Fixed interest	515,386	19.4	812,653	23.0
New Zealand equities	262,071	9.9	334,304	9.5
International equities	1,248,203	47.1	1,641,913	46.5
Real estate	166,092	6.3	232,190	6.6
Commodity futures	64,378	2.4	140,944	4.0
Multi-asset	230,014	8.7	250,660	7.1
Global tactical asset allocation	163,106	6.2	116,661	3.3
TOTAL	**2,649,250**	**100.0**	**3,529,325**	**100.0**

The numbers in the table are based on the assets managed by the investment managers for each asset class. They differ from the investments numbers set out in the Statement of Net Assets for the Fund (see page 30) because of differing disclosure requirements for financial reporting purposes.

Asset Management

During the year the move from passive to active management of the international equities portfolio was completed with a number of new managers being appointed. The Authority believes it has retained managers capable of adding value over time and that the cost of active management will be more than offset by higher returns. The managers appointed by the Authority are listed in the Directory on page 75.

Active management added value (when compared to benchmarks) for both New Zealand equities (1.9%) and international equities (2.8% before hedging costs) although returns from asset classes were negative. The Fund also benefited from the diversification into a global multi-asset class fund and global tactical asset allocation. These were offset by underperformance from fixed interest, which suffered from investing too early in credit securities, and the global tactical asset allocation which did not achieve a high performance target. The New Zealand dollar returns from international equities and real estate were also impacted by the high cost of hedging foreign exchange exposures in a volatile market. Overall, the Fund underperformed its benchmark by 0.5%.

Investment Returns

The Fund's after- tax deficit for the year represents a -16.76% return on average net assets. The pre-tax deficit represents a -19.9% return on average net assets.

Investment returns were ahead of the IPM on an annualised basis for the period from 2 October 2001, when the Authority took over responsibility for the management of the Fund, to 30 June 2007. The negative investment returns, in the last two financial years, mean returns are now below the IPM and the Fund is outside the Risk Parameter for the second time in nine years.

Table 3 below compares the Fund's investment returns against the IPM over 1, 3 and 5 years ended 30 June 2009.

Table 3

	1 year %	3 years Annualised %	5 years Annualised %
Fund Return	-16.8	-5.2	0.7
IPM	9.3	7.2	7.1

The new offshore tax regime was another factor that had an adverse impact on the results for the year. This came into force for the Fund in October 2007. Even though the Fund made a loss on its international equities portfolio, tax was still payable on deemed income of 5% pa of the opening market value each month. Under the previous regime, tax was payable only on dividends. Now, tax is paid even if there are no dividends and the share price falls. Also, under the new tax rules, losses on Australasian equities and listed New Zealand property securities are no longer deductible for tax. In a rising market the new tax regime should be beneficial to the Fund.

It is important to take a long term view of investment returns, as the Fund is expected to pay pensions for another 60 years. To earn an average 2.5% after tax, over and above the after-tax returns from Government stock over the long term, means there is a risk of occasional loss and the Risk Parameter recognises this. Any losses are expected to be more than offset over time by years of high returns. The losses experienced this year and last year and the cumulative returns since the inception of the diversified Investment Strategy in 2001 are a reflection of the severity of the global financial crisis. Despite this unusually volatile period the Board remains confident that its investment strategy remains appropriate. The current environment has created good opportunities for long term investors.

Returns by Asset Class

The Fund's negative return in 2009 reflects the dramatic decline in New Zealand and international equities, including listed real estate. New Zealand equities returned -9.2% and international equities -31.4%. Real estate returned -40.6% and collateralised commodity futures -50.9%, largely offsetting the excellent return earned by this asset class in 2008. The only asset classes to generate positive returns were fixed interest at 10.2% and global tactical asset allocation at 9.1%.

Table 4 below compares the pre-tax investment returns by asset class and for the total Fund for the financial years ended 30 June 2008 and 2009.

Table 4 - Pre Tax Investment Returns for each Asset Class, and for the Fund, for 2009 and 2008

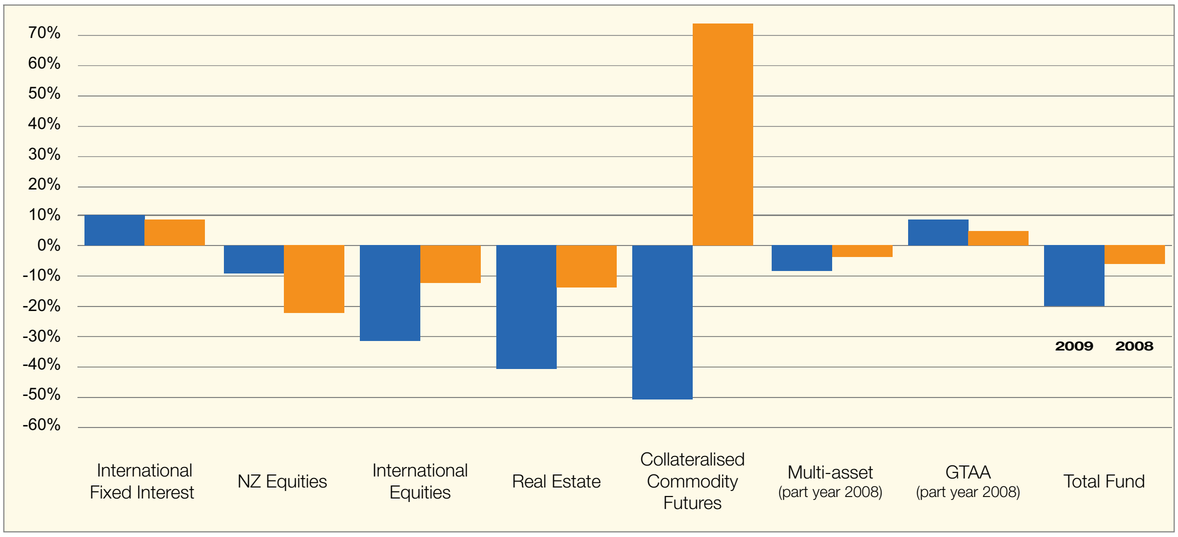
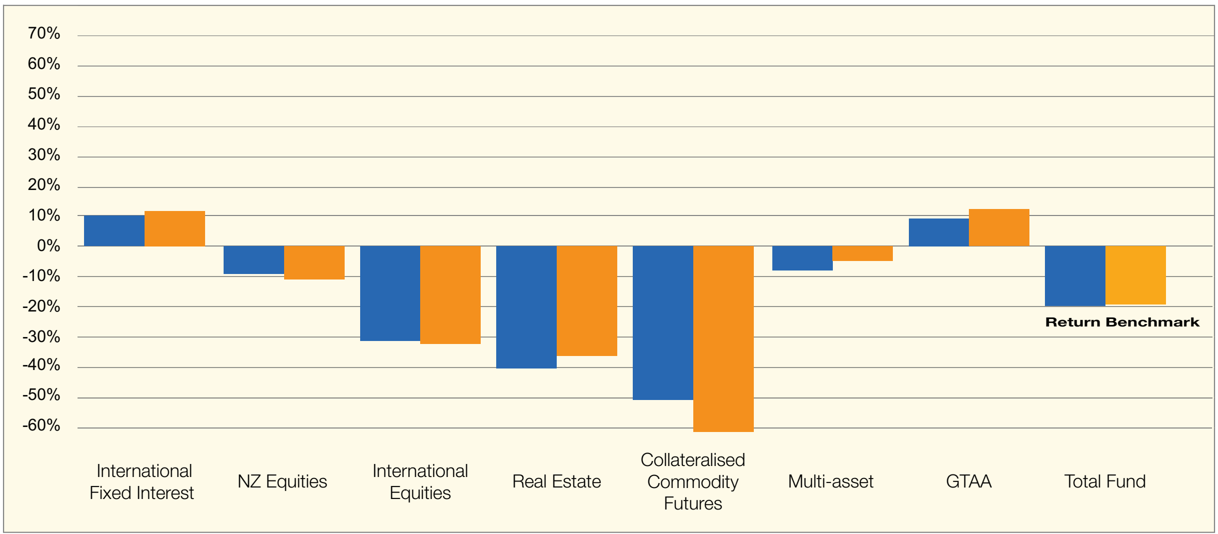


Table 5 below compares the pre tax investment returns for each asset class with its benchmark index.

Table 5 - Pre Tax Investment Returns v Benchmark, year ended 30 June 2009



Active management added value in New Zealand and international equities but detracted value in fixed interest and real estate.

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.

This is clearly shown in the following analysis of the return from each asset class against its benchmark index for the year.

International fixed interest 10.17%

Barclays Capital Global Aggregate Index, hedged to New Zealand dollars 11.63%

Returns from fixed interest investments (such as Government stock and corporate bonds) are a combination of interest income and capital gains or losses as market yields fall (generating gains) or rise (generating losses).

In the key US market, the 10 year government bond yield fell 44 bps to 3.53% while the equivalent rates for the United Kingdom and Germany fell by 144 bps and 124 bps to 3.69% and 3.39% respectively. The Japanese 10 year yield also declined 24 bps to 1.36%. The downward trend in yields globally reflected a sharp rise in risk aversion with the deepening credit crunch and threat of systemic financial meltdown. The aggressive cuts in interest rates to record lows by the central banks around the globe supported the general decline in bond yields.

Over the first half of 2009, however, the fall in government bond yields reversed as recovering equity markets and improving risk appetite led bond yields sharply higher. Surging government debt issuance also weighed heavily on bond markets. Higher long-term yields, despite record low official interest rates, led the yield curve to steepen significantly over the last six months.

It was a different story for investors in non-government fixed interest securities. In 2008, the global credit crisis hurt returns for securities exposed to credit risks as companies were not able to access money so easily, the cost of borrowing soared and credit spreads blew out. Returns improved in the first half of 2009 for these investors, as credit markets reopened and corporates were better able to issue debt, albeit at discounted prices.

In this volatile environment and difficult market conditions, investment managers with credit exposures under-performed.

New Zealand equities -9.22%

NZX50 Gross Index including imputation credits -11.11%

New Zealand equities posted a negative return over the period. The market outperformed global shares because of its low exposure to financial and resource companies.
New Zealand equities rebounded strongly in 2009, however, being up 8% in the six months to June.

International equities -31.40%

MSCI All Countries World Index 72% hedged (after tax) to New Zealand dollars -32.32%

International sharemarkets fell heavily, reflecting the global financial crisis and a recessionary earnings environment. The MSCI World Gross Index ended the year down -26% in local currency terms, with all major markets posting negative returns. The Chinese sharemarket was one of few regions with a positive return (13%). As with New Zealand shares, global shares have rebounded strongly from their lows in early March, posting the best quarterly returns in the three months to June 2009 since the March quarter of 1987. Hedging of foreign exchange exposures detracted value.

Real Estate -40.55%

UBS Warburg Global Real Estate Investors Index, hedged to New Zealand dollars -36.46%

The slowing economy and negative sentiment towards riskier investments also weighed on the property market over the period. Global listed property securities (as measured by the UBS Warburg Global Real Estate Investors Index) posted a loss of 38.4% in local currency terms. Transactions were low and capitalisation rates continued to rise. Moreover, the tighter lending standards and increased funding costs meant that property was particularly hard hit. Price volatility was extreme as leverage increased due to falling asset values. Though they ended the period well down, global property securities staged a very strong rebound in the June quarter and were one of the strongest performing markets with the UBS Warburg Global Real Estate Investors Index returning 24.1% in the June quarter in local currency terms.

Collateralised Commodity Futures -50.85%

Goldman Sachs Commodities Index Total Return Swap in New Zealand dollars -61.47%

The Fund had 3% invested in a collateralised commodity futures index swap, earning a return of -50.9% over the year versus the index of -61.5%. The difference reflects the benefit of the returns on New Zealand dollar cash balances held to collateralise the swap position. Futures returns fell as the collapse in the global economy reduced demand for oil, agricultural products and precious metals. As with other growth assets, commodities rallied in the June quarter.

Multi-asset class -7.98%

Composite made up of 70% of the MSCI All Countries World Index and 30% of the Lehman Brothers Global Aggregate Index -4.76%

7% of the Fund is invested in a United States endowment fund strategy managed by Makena. In addition to public equity and bond market investments the fund invests in private equity, real estate, natural resources and hedge funds. The multi-asset class aims to earn equity-like returns over the long term with about half the volatility of equities. Returns in 2009 were disappointing despite diversified exposure to hedge funds and private markets.

Global tactical asset allocation 9.12%

USD 3 month LIBOR plus 6% p.a. hedged into New Zealand dollars 12.16%

The Fund is invested in a global tactical asset allocation strategy. The manager invests tactically in a range of liquid public market securities including developed and emerging market equities, bonds, currencies and commodities and is measured by the Authority against an aggressive target of 6% per annum above cash, hedged into New Zealand dollars. In 2009 the manager achieved half the outperformance target and made a significant positive contribution to total portfolio return.

Responsible Investing

The GSF Act requires the Authority to manage and administer the Fund in a manner consistent with (among other requirements) avoiding prejudice to New Zealand's reputation as a responsible member of the world community. The Authority's Statement of Investment Policies, Standards and Procedures (**SIPSP**) is required to cover ethical investment, including policies, standards and procedures for avoiding prejudice.

In addition to the references to these matters in the SIPSP, the Authority has developed Responsible Investment Policies, Standards and Procedures (**RI Policies**), which cover:

- Ethical investment, including avoiding prejudice to New Zealand's reputation as a responsible member of the world community.
- Environmental, social and governance considerations.
- The retention, exercise or delegation of voting policies.

The RI Policies can be viewed on the Authority's website. In terms of the RI Policies last year the Authority resolved to exclude direct investment in securities issued by a number of companies understood to be involved in the manufacture of tobacco and anti-personnel mines.This year the Authority has resolved to exclude direct investment in securities issued by a number of companies understood to be involved in the manufacture of cluster munitions and nuclear weapons. The decisions were made on the basis that the companies' activities are inconsistent with the Authority's RI Policies and with international conventions to which New Zealand is a party.

Background on the decisions and the list of the companies excluded from direct investment can be viewed on the Authority's website.

The Authority also invests in a number of collective investment vehicles (**CIVs**), which are a practical and cost effective way of achieving exposure to some markets and managers. The Authority has little or no influence or control over the structure of the CIVs, the corporate securities held or individual voting decisions. In such cases, the managers of the CIVs have been made aware of the Authority's RI Policies and its decisions with respect to its RI Policies, and encouraged to consider whether these are appropriate for the CIVs.

The Authority has signed a collaborative agreement with the Guardians of New Zealand Superannuation (**GNZS**), the Earthquake Commission and the Accident Compensation Commission to share the research of the GNZS Responsible Investing Unit to assist the Authority in meeting its RI Policies and to minimise duplication of time and cost. The Authority and the other three parties have similar obligations in relation to RI and all are signatories to the United Nations Principles for Responsible Investment (**UNPRI**).

GOVERNMENT SUPERANNUATION FUND AUTHORITY
SCHEMES COMMENTARY

During the year a tender was undertaken to identify an organisation to undertake the development of a new and more sustainable system to be used in the administration of the GSF Schemes. The GSF Business System is more than 15 years old and incorporates technology that is no longer in common use in New Zealand. People with relevant technology skills are becoming increasingly scarce. The Board is reviewing the outcome of the tender, particularly the resources, experience and capability of the tenderers to undertake the work, the timetable and whether to undertake the project in stages, and the software language and development approach to be used in the project. Final decisions are likely to be made before the end of 2009. If the development proceeds, it is anticipated the project will take around 18 months to complete.

Datacom's performance has improved over the year after some slippage in 2008. The performance standards for schemes administration were reviewed during the year and new performance standards apply from 1 July 2009. The new performance standards reflect current best practice in schemes administration and are more specific in terms of required turn around times. Datacom adopted and was meeting the new performance standards before year end.

In April the Authority and Datacom implemented the decision made in Budget 2008, and subsequently confirmed by an amendment to the GSF Act, that from April 2009 the minimum cost of living adjustment applied to GSF annuities would be increased from 90% of the increase in the Consumer Price Index (**CPI**) to 100%. The lower than 100% increase in the CPI received by some annuitants continues to apply before April 2009.

GOVERNMENT SUPERANNUATION FUND AUTHORITY
STATEMENT OF GOVERNANCE AND ACCOUNTABILITY

The Authority was established as a Crown entity by section 15A of the GSF Act and became an autonomous Crown entity under the Crown Entities Act. The business of the Authority is to manage the assets, and administer the schemes of the Fund in accordance with the GSF Act.

Section 15G of the GSF Act specifies that the Board is responsible for the business of the Authority.

Government Superannuation Fund Authority Board - as at 3 September 2009

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

Tim McGuinness. Chairman. Appointed as a Board member in 2001, reappointed 2004 and 2007. Appointed as Chairman in 2008. Mr McGuinness is a trustee of the Police Superannuation Scheme, NZ Fire Service Scheme, Globus NZ Pension Plan and the NZ Qualifications Authority Superannuation Scheme, Chairman of Trustees of the Dairy Industry Superannuation Scheme and the Fonterra Superannuation Scheme, and a director of Whai Rawa Fund Limited. He previously held senior investment management positions at Royal & Sun Alliance and Norwich Union Investment Management.

David May. Deputy Chairman. Appointed in 2001, reappointed 2004, 2007 and 2009. Mr May 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.

Helen Bowie. Appointed in 2001, reappointed 2003, 2006 and 2008. Ms Bowie is a partner of Chapman Tripp.

Steve Napier. Appointed in 2008. Mr Napier is principal of Whakatane sharebrokers, Steve Napier Ltd. He previously held senior investment management positions with Colonial First State Investments.

Ralph Stockdill ONZM. Appointed in 2002, reappointed 2005 and 2008. Mr Stockdill 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.

Susie Weaver. Appointed in 2001, reappointed 2002, 2005 and 2007. Ms Weaver is a principal of Weaver Consulting Ltd, Chair of Shamrock Superannuation Ltd and Trustee of The Anglican Trust for Women and Children.

Keith Taylor. Appointed in 2008. Mr Taylor is Deputy Chair of the Earthquake Commission and a Board member of Takeovers Panel and New Zealand Qualifications Authority. He is a Director of the Reserve Bank of New Zealand, Gough, Gough and Hamer Limited and Butlands Management Services Limited. He was previously Group Managing Director and Chief Executive Officer of Tower Limited and, prior to that, held a number of senior management roles in Tower and its predecessor, Government Life.

Remuneration of Board Members

Remuneration of 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 three committees with specific responsibilities for Audit and Risk Review, Investments and Responsible Investing. The Chairman is an ex officio member of all committees.

As required by the GSF 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 scheme administration managers, investment managers, other service providers, and custodians.

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

Auditor

The Auditor-General is the auditor of the Authority. The Auditor-General has appointed Ian Marshall 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 scheme 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 Provisions, Policies and Procedures of the Government Superannuation Fund, 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
- Paul Bevin — General Manager, Investments
- Nicky Rumsey — Manager, Investments
- Peter McCaffrey — Manager, Special Projects
- Janet Shirley — Manager, Schemes

Indemnity

In 2006, the Authority:

- provided indemnities to each Board member under Deeds of Indemnity whereby the Authority agreed to indemnify each Board member (subject to certain exceptions) for certain costs and liabilities in respect of certain 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, and
- entered into Deeds of Indemnity with members of the Management team, who exercise delegations on behalf of the Board in terms of the MSA, whereby it agreed to indemnify the members of the Management team (subject to certain exceptions) for certain costs and liabilities in respect of certain 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. In 2009 the Authority and Annuitas varied the MSA to include the Manager, Schemes as an additional member of the Management team who exercise delegations on behalf of the Board. At the same time the Authority entered into a Deed of Indemnity with the current holder of the position of Manager, Schemes.

The indemnities provided by the Authority to Board members and the members of the Management team do not protect the Board member, or the member of the Management team, against any liability, claim or proceeding of any kind for any dishonesty or fraud or anything else that either:

- as a matter of public policy cannot be indemnified at law, or
- which 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 indemnities. Broadly speaking, strict liability offences are those for which no intent needs to be established.

Insurance

During the financial year, the Authority continued Directors and Officers insurance cover for Board members and members of the Management team (including the Manager, Schemes) in respect of potential liabilities and costs incurred through acts and omissions made in the performance, or intended performance, of the functions of the Authority. Insurance is not provided for an act or omission that is in bad faith.

The Authority also continued Company Reimbursement insurance cover in respect of any claims made by Board members, or members of the Management team, under the indemnities described above.

The scope of the Directors and Officers insurance cover and the Company Reimbursement insurance cover is consistent with the limitations imposed by the Crown Entities Act.

STATEMENT OF SERVICE PERFORMANCE

Output Class O1 – Management of the Government Superannuation Fund

This output class provides investment and scheme management for the Fund.

Outputs in this class are:

- management of the GSF assets (the Fund),
- management of the GSF Schemes, including the agreement between the Authority and the scheme administrator, and
- interpretation of the provisions of the GSF Act and exercising discretionary powers (as set out in the GSF Act).

The performance targets are set out in the Authority's Statement of Intent for the year commencing 1 July 2008.

INVESTMENT MANAGEMENT	
PERFORMANCE STANDARD	**PERFORMANCE ACHIEVEMENT**
Maximise fund income without undue risk, by:	
Keeping under review the Fund's Investment Strategy and the key investment and taxation assumptions, to ensure the strategy remains efficient and consistent with the Investment Objective.	The Fund's Investment Strategy and key investment and taxation assumptions were reviewed as part of the annual review of the SIPSP in September 2008. No changes were seen to be required following the review and the strategy was considered to remain efficient and consistent within the Investment Objective. Each quarter, Management presented to the Board a comprehensive report that covered Fund performance, both before and after tax compared to the Investment Performance Measure, and Fund volatility compared to the Risk Parameter.
Continuing to assess diversification opportunities to broad classes of market risk.	Research into alternative strategies such as hedge funds, life settlements, catastrophe bonds and infrastructure investments were on-going projects at year end. Dynamic asset allocation and the use of derivative strategies were being considered to more efficiently manage asset class exposures.

INVESTMENT MANAGEMENT	
PERFORMANCE STANDARD	**PERFORMANCE ACHIEVEMENT**
Identifying potential sources of additional return through active management strategies and, if appropriate, implementing these to improve the Fund's performance.	New Zealand private equity investment and active management of the commodities exposure were introduced to the portfolio during the year. To improve the Fund's performance active managers were appointed to manage emerging markets equities and small cap equities, and allocations to enhanced index global equities managers were eliminated.
Manage the investment processes in accordance with best practice portfolio management by:	
Developing and maintaining effective processes and tools to allocate Fund assets, allow for tax effects and monitor investment risks.	Risk modelling of the equities allocation (which consumes the significant portion of the Fund risk budget) was undertaken quarterly and reported to the Board. Allocations to equity managers were made on the basis of their contribution to portfolio risk. The quarterly report to the Board included attribution analysis to identify sources of return and Management commentary on sources of return and risk. Dynamic asset allocation is being evaluated.
Ensuring investment managers'ongoing suitability through careful selection, monitoring and assessment.	Management held quarterly performance and portfolio strategy calls with current investment managers. Insights gained from the risk analysis (above) were discussed with managers. Manager reviews from external consultants were part of this process. One manager was terminated as a result of this process. Other terminations of managers were the result of changes to asset mixes. Managers not in the portfolio were also researched and monitored for comparison purposes with incumbent managers and for potential inclusion in the portfolio. Full records are maintained of the processes followed to appoint new managers.

INVESTMENT MANAGEMENT	
PERFORMANCE STANDARD	**PERFORMANCE ACHIEVEMENT**
Monitoring investment managers against their performance requirements, risk limits and compliance criteria, as specified in investment management agreements.	Each month Management reviewed the performance of the investment managers against the performance requirements, risk limits and compliance criteria set out in investment management agreements. Monthly compliance certificates were received from investment managers and reviewed by Management. A comprehensive quarterly report to the Board included analysis of each manager's historical returns, risk, major exposures and Management's views.
Maintaining the safe custody of the Fund's assets, and monitoring the custodian's performance to ensure that the quality of service and the accuracy and timeliness of reports on the Fund are maintained.	The Custodian has: • settled all transactions and maintained the safe custody of GSF assets; • prepared monthly accounting reports in compliance with New Zealand International Financial Reporting Standards, by the 7th business day following the end of the month; • prepared investment manager reconciliation reports by the 8th business day following the end of the month; and • prepared independent investment performance reports, by the 14th business day following the end of the month.
Adhering to the Authority's SIPSP, and recording all amendments to its policies, standards and procedures in this document.	The Authority adhered to its SIPSP over the year and recorded all amendments to its policies, standards and procedures in the document. The SIPSP is formally reviewed annually and more frequent changes may be made as the Investment Strategy moves into previously unconsidered areas, for example, private equity investments. Compliance with the SIPSP is an integral part of the due diligence for the appointment of new managers.

INVESTMENT MANAGEMENT	
PERFORMANCE STANDARD	**PERFORMANCE ACHIEVEMENT**
Avoiding prejudice to New Zealand's reputation as a responsible member of the world community by:	
Implementing the Authority's RI Policies.	The Authority's investments were reviewed against the provisions of the RI Policies. Managers were required to report on compliance with the Authority's RI Polices. Direct investment in companies understood to be involved in the manufacture of anti-personnel mines, nuclear weapons, cluster munitions and tobacco have been excluded from the Fund.
Developing and implementing strategies that will contribute to meeting the aspirational principles of the UNPRI in a cost effective way and where supported by a robust investment case.	The Authority has joined with other Crown Financial Institutions (**CFIs**) to implement an integrated and cost effective approach to the principles of the UNPRI. A formal agreement with CFIs addresses responsible investment issues in policy statements and mandates, and allows for participation in and support for platforms to share research and pool resources.

SCHEMES ADMINISTRATION	
PERFORMANCE STANDARD	**PERFORMANCE ACHIEVEMENT**
Providing sufficient funding to Datacom to ensure all entitlement payments are able to be made as they become due.	Sufficient funding was provided to Datacom every four weeks to enable all authorised payments to be accepted and processed through the Schemes' bank account without the bank account being overdrawn.
Responding to member correspondence within five working days.	All member correspondence received at least an initial reply within five working days of receipt. In some cases a more comprehensive reply was required to finally resolve the issues raised by the member. On occasions final resolution took longer than five working days.
Responding to appeals by members, against decisions made by or on behalf of the Authority, in accordance with the Act; ensuring the Authority's reports to the Appeals Board are provided at least 14 days before each scheduled hearing date.	One appeal was made against a decision made by, or on behalf of, the Authority during the year ended 30 June 2009. The appeal was reported to the Appeals Board at least 14 days before the scheduled hearing date. The appeal was declined by the Appeals Board.
Maintaining a Business Continuity Plan (**BCP**) for scheme administration that is in accordance with best industry practice.	The scheme administrator maintains a comprehensive BCP that is in accordance with best practice. The BCP is tested periodically and reviewed annually.
Maintaining the Policies and, subject to consultation with interested parties, amending to record any policy changes made by the Authority.	The Policies were maintained during the year under review. No changes were made to the Policies.
Providing actuarial data, required for the valuation of the liabilities of the Fund, for inclusion in the Crown financial statements, in accordance with the timetable agreed with Treasury.	Complete actuarial data was provided to the Government Actuary to enable completion of the valuations of the liabilities of the Fund, for inclusion in the Crown financial statements, in accordance with the timetable agreed with Treasury.
Communicating annually with contributors, annuitants, and employers regarding the activities of the Authority and the performance of the Fund.	A message from the Chairman was sent to all contributors, annuitants, and employers in September 2008, reporting on the activities of the Authority and the performance of the Fund.

STATEMENT OF SERVICE PERFORMANCE (CONTINUED)

SCHEMES ADMINISTRATION	
PERFORMANCE STANDARD	**PERFORMANCE ACHIEVEMENT**
Monitoring the scheme administrator's performance including sustainability of service, service levels to contributors, annuitants, and employers and other key service standards, within an overall framework of seeking continual improvement.	Management monitored the scheme administrators' performance on a regular basis during the year and provided comprehensive monthly reports to the Board. After some slippage in 2008, there was a significant improvement in the scheme administrator's performance against the standards set out in the schemes' administration contract. The performance standards cover sustainability of service and service levels to contributors, annuitants and employers. New performance standards applied from 1 July 2009, which are at a higher level than the original standards. Datacom was largely meeting the new standards by year end, resulting in a continual improvement in service to members.

GOVERNMENT SUPERANNUATION FUND

Authority's Report

On behalf of the Government Superannuation Fund Authority (**the Authority**), I have pleasure in presenting this report on the Government Superannuation Fund (**GSF** or **the Fund**) for the year ending 30 June 2009. The report is made in accordance with section 93B of the Government Superannuation Fund Act 1956 (**the GSF 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, who are not funded directly by the Government, pay contributions as set by the Government Actuary, at 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 Authority was established to manage the Fund's assets and administer the GSF Schemes.

This annual report includes information on membership, and other matters required by the GSF Act. Commentary on the investment performance of the Fund starts on page 4 of the Authority's Annual Report.

Information on the Authority can be found commencing on page 1.

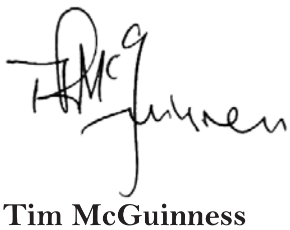
Membership

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.

Details of the membership of the GSF Schemes is set out on page 25.

Mortgage Finance

No new mortgages are being granted. The GSF mortgage portfolio, as at 30 June 2009, consisted of two mortgages totalling $8,000 (30 June 2008: two mortgages totalling $14,000), with an average earning rate of 8.00% for the year (30 June 2008: 8.00 %).



Tim McGuinness
Chairman
Government Superannuation Fund Authority Board

GOVERNMENT SUPERANNUATION FUND
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 2009:

(a) All contributions required to be made to the Fund, under the GSF Act, have been made or accrued.

(b) All benefits required to be paid from the Fund under the GSF Act have been paid.

(c) Due to the partially funded nature of the GSF Schemes, the market value of assets did not match the accrued benefit liability of the Fund by $9,298 million (2008: $8,380 million). The deficiency is covered by Section 95 of the GSF Act, which requires the Minister of Finance to appropriate funds from public money to meet the annual deficiency in payments from the Fund.

(d) All employer contributions paid were in accordance with the most recent recommendations of the Government Actuary.

Tim McGuinness
Chairman
Government Superannuation Fund Authority Board

20 August 2009

GOVERNMENT SUPERANNUATION FUND
MEMBERSHIP COMMENTARY

The movement in contributors during the past five years was:

Year ended 30 June	*Total*	*Change*	*% Change Contributors*
2005	22,241	(1,478)	(6.23)
2006	20,240	(2,001)	(9.00)
2007	18,718	(1,522)	(7.52)
2008	17,031	(1,687)	(9.00)
2009	15,683	(1,348)	(7.91)

Contributors by scheme were:

GSF Scheme	***Number 2009***	*% of Total*	*Number 2008*
General Scheme	**14,465**	92.23	15,370
Armed Forces	**607**	3.87	808
Police	**469**	2.99	682
Prisons Service	**109**	0.90	127
Judges and Solicitor-General	**24**	0.13	20
Parliamentary	**13**	0.08	20
Total contributors at end of year	**15,683**	100.00	17,031

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

	Number 2009	*Number 2008*
Contributors at beginning of year	**17,031**	18,718
Retirements	**(1,023)**	(1,196)
Withdrawals	**(8)**	(6)
Death before retirement	**(24)**	(16)
Cessation of employment before retirement	**(79)**	(83)
Transfer to other schemes	**(214)**	(386)
Total contributors at end of year	**15,683**	17,031

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

Year ended 30 June	*Total Annuitants*	*Change*	*% Change*
2005	47,587	(108)	(0.23)
2006	47,523	(64)	(0.13)
2007	47,237	(286)	(0.60)
2008	47,158	(79)	(0.17)
2009	46,963	(195)	(0.41)

The movement in number of annuitants during the year was:

	Number 2009	*Number 2008*
Annuitants at beginning of year	**47,158**	47,237
New retiring allowances	**1,034**	1,196
New allowances to spouses	**785**	758
Allowances deferred	**16**	(46)
Discontinued allowances	**(2,030)**	(1,987)
Total annuitants at end of year	**46,963**	47,158

There were 6,052 deferred pensions at 30 June 2009 (2008: 6,068)

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

Year ended 30 June	*Total Contributors*	*Total Annuitants*	*Total Deferred Pensions*	*Total Members*	*Decrease During Year*
2005	22,241	47,587	5,895	75,723	(1,469)
2006	20,240	47,523	6,019	73,782	(1,941)
2007	18,718	47,237	6,025	71,980	(1,802)
2008	17,031	47,158	6,068	70,257	(1,723)
2009	15,683	46,963	6,052	68,698	(1,559)

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

	2009	*%*	*2008*	*%*
Contributors	**15,683**	25	17,031	26
Annuitants	**46,963**	75	47,158	74
	62,646	100	64,189	100

Granting a charge over contributions

In the year to 30 June 2009, 31 charges (2008: 70) were registered by the Fund in favour of chargeholders as security over individual contributor's contributions.

FINANCIAL STATEMENTS

GOVERNMENT SUPERANNUATION FUND
STATEMENT OF RESPONSIBILITY

The Financial Statements of the Fund for the year ended 30 June 2009 have been prepared in accordance with Section 93 of the GSF Act.

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, and
- the investment policies, standards, and procedures for the Fund, commencing on page 77, have been complied with.

In our opinion, the attached Financial Statements and reports fairly reflect the net assets, as at 30 June 2009, and the changes in net assets and the cash flows of the Fund, for the year ended 30 June 2009.

Tim McGuinness
Chairman
Government Superannuation Fund Authority Board

Alan Langford
Chief Executive

20 August 2009

GOVERNMENT SUPERANNUATION FUND
STATEMENT OF CHANGES IN NET ASSETS

FOR THE YEAR ENDED 30 JUNE 2009

	Note	2009 $000 Actual	2008 $000 Actual	2009 $000 Forecast
Change in assets from:				
Investing activities				
Investment revenue				
Interest, dividend and other income	1	**116,002**	105,972	96,156
(Decrease)/increase in fair values of investment assets	2	**(788,742)**	(316,096)	210,648
		(672,740)	(210,124)	306,804
Operating activities				
Operating revenue	3			
Government		**19,181**	15,591	27,127
Other employers		**4,499**	4,169	6,363
		23,680	19,760	33,490
Operating expenses	3			
Funding for the Authority		**(23,680)**	(19,760)	(33,490)
(Deficit) before tax and membership activities		**(672,740)**	(210,124)	306,804
Income tax benefit/(expense)	4	**89,429**	(50,818)	(51,719)
(Deficit)/surplus after tax and before membership activities		**(583,311)**	(260,942)	255,085
Membership activities				
Contributions				
Government	5	**618,286**	691,057	577,291
Members		**63,902**	68,405	55,825
Other employers		**12,704**	14,559	14,465
		694,892	774,021	647,581
Benefits paid	6	**(881,650)**	(947,333)	(825,964)
Net benefits paid		**(186,758)**	(173,312)	(178,383)
Net (decrease)/increase in net assets		**(770,069)**	(434,254)	76,702
Opening net assets available to pay benefits		**3,574,152**	4,008,406	3,706,255
Net assets available to pay benefits		**2,804,083**	3,574,152	3,782,957

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 2009

	Note	2009 $000 Actual	2008 $000 Actual	2009 $000 Forecast
Current assets				
Cash and cash equivalents		**317,008**	289,834	433,125
Trade and other receivables	7	**83,232**	228,708	167,135
Income tax receivables		**36,319**	32,601	–
Total current assets		**436,559**	551,143	600,260
Non-current assets				
Investments				
Fixed interest - New Zealand	8	**–**	61,744	20,585
Fixed interest - International		**510,270**	730,977	501,822
Equities - New Zealand		**252,902**	319,122	340,175
Equities - International		**955,094**	1,518,575	1,866,117
Real estate		**161,186**	228,930	224,564
Commodity futures		**44,033**	140,987	2,280
Multi-asset and Global Tactical Asset Allocation		**380,503**	369,246	607,768
Mortgages	9	**8**	14	10
Derivative assets held for trading		**148,163**	134,055	170,831
Short term investments		**600**	8,030	–
Total investments		**2,452,759**	3,511,680	3,734,152
Non-current tax receivables				
Deferred tax asset	4	**87,536**	–	–
Total non current tax receivables		**87,536**	–	–
Total non-current assets		**2,540,295**	3,511,680	3,734,152
Total assets		**2,976,854**	4,062,823	4,334,412

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

STATEMENT OF NET ASSETS (CONTINUED)

	Note	2009 $000 Actual	2008 $000 Actual	2009 $000 Forecast
Less liabilities				
Current liabilities				
Trade and other payables	10	**132,540**	337,594	337,421
Income tax payable		**11,494**	11,942	12,247
Benefits payable		**1,456**	6,906	4,594
Derivative liabilities held for trading		**27,281**	120,287	162,118
Non-current liabilities				
Non-current tax payables	4	**–**	11,942	–
Deferred tax liability	4	**–**	–	35,075
Total liabilities		**172,771**	488,671	551,455
Net assets available to pay benefits		**2,804,083**	3,574,152	3,782,957
Promised retirement benefits				
Gross liability for promised retirement benefits	13	**12,102,000**	11,954,152	12,536,000
Deficit		**9,297,917**	8,380,000	8,753,043
Net assets available to pay benefits		**2,804,083**	3,574,152	3,782,957

The Financial Statements were approved by the Authority Board on 20 August 2009.

Tim McGuinness
Chairman
Government Superannuation Fund Authority Board

Keith Taylor
Chairman
Audit & 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
STATEMENT OF CASH FLOWS

FOR THE YEAR ENDED 30 JUNE 2009

	2009 $000 Actual	2008 $000 Actual	2009 $000 Forecast
Cash flows from operating activities			
Cash was provided from:			
Government contributions	**638,277**	724,378	601,002
Members' contributions	**64,351**	64,939	55,903
Other employers' contributions	**18,498**	18,278	20,902
Interest and dividends	**119,219**	106,826	96,836
Other	**10**	3,798	861
Cash was disbursed to:			
Benefit payments	**(886,849)**	(943,123)	(826,596)
Income tax	**(11,942)**	(132,903)	(61,471)
Operating expenses	**(22,136)**	(17,478)	(33,465)
Net cash flows from operating activities	**(80,572)**	(175,285)	(146,028)
Cash flows from investing activities			
Cash was provided from:			
Maturities and sales of investment assets	**7,929,115**	7,288,348	12,298,884
Mortgage repayments	**14**	17	12
Cash was disbursed to:			
Purchase of investment assets	**(7,821,383)**	(7,163,085)	(12,152,868)
Net cash flows from investing activities	**107,746**	125,280	146,028
Net increase/(decrease) in cash held	**27,174**	(50,005)	–
Opening cash and cash equivalents	**289,834**	339,839	433,125
Closing cash and cash equivalents	**317,008**	289,834	433,125

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

GOVERNMENT SUPERANNUATION FUND

RECONCILIATION OF NET CHANGE IN NET ASSETS TO NET OPERATING CASH FLOWS

FOR THE YEAR ENDED 30 JUNE 2009

	2009 $000	2008 $000
Net (decrease) in net assets	**(770,069)**	(434,254)
Add: Non-cash items		
(Decrease) in deferred tax liability	**–**	(39,474)
Increase in deferred tax asset	**(87,536)**	–
(Decrease)/increase in non-current tax payables	**(11,942)**	11,942
Capitalised interest	**1**	(2)
Mortgage management expense	**–**	1
	(99,477)	(27,533)
Add: Movements in working capital items		
Receivables and prepayments	**1,287**	(1,476)
Investment receivables	**143,614**	33,814
Trade and other receivables	**575**	557
Income tax receivable	**(15,660)**	(32,601)
Government contributions received in advance	**1,519**	18,704
Investment payables	**(208,404)**	(71,575)
Trade and other payables	**1,831**	(1,812)
Income tax payable	**11,494**	(18,460)
Benefits payable	**(5,449)**	2,046
	(69,193)	(70,803)
Add: Items classified as investing activities		
Decrease in accrued interest portion of bonds	**4,635**	3,448
Change in fair value of investment assets	**788,742**	316,096
(Decrease) in investment settlement receivables	**(143,614)**	(33,814)
Decrease in investment settlement payables	**208,404**	71,575
	858,167	357,305
Net cash out flows from operating activities	**(80,572)**	(175,285)

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

GOVERNMENT SUPERANNUATION FUND
JUDGES AND SOLICITOR-GENERAL SUPERANNUATION
STATEMENT OF CHANGES IN NET ASSETS

FOR THE YEAR ENDED 30 JUNE 2009

	2009 $000	2008 $000
Income from operations*		
Government contributions	**14,007**	15,469
Members contributions	**–**	109
	14,007	15,578
Expenditure*		
Benefits paid:		
Retirements	**11,062**	10,442
Allowances capitalised	**1,228**	1,629
Spouses and children	**1,717**	3,507
	14,007	15,578
Net changes in net assets	**–**	–

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

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

GOVERNMENT SUPERANNUATION FUND
PARLIAMENTARY SUPERANNUATION
STATEMENT OF CHANGES IN NET ASSETS

FOR THE YEAR ENDED 30 JUNE 2009

	2009 $000	2008 $000
Income from operations*		
Government contributions	**3,680**	3,194
Members contributions	**156**	244
	3,836	3,438
Expenditure*		
Benefits paid:		
Retirements	**3,117**	2,908
Allowances capitalised	**165**	–
Spouses and children	**554**	530
	3,836	3,438
Net changes in net assets	**–**	–

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

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 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 (**the Fund**) are prepared pursuant to section 93 of the Government Superannuation Fund Act 1956 (**GSF Act**) and incorporate the Judges and Solicitor-General Superannuation Account and the Parliamentary Superannuation Account.

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

Reporting requirements

The Financial Statements have been drawn up in accordance with NZ IAS 26: *Accounting and Reporting by Retirement Benefit Plans*, and with the provisions of relevant legislative requirements. They include the Judges and Solicitor-General Superannuation Account and the Parliamentary Superannuation Account.

The Fund is a profit-oriented entity domiciled in New Zealand.

(ii) Statement of compliance

The Financial Statements have been prepared in accordance with Generally Accepted Accounting Practice in New Zealand (**NZ GAAP**), applying the New Zealand equivalents to International Financial Reporting Standards, and its interpretations (**NZ IFRS**), as appropriate for profit-oriented entities. These Financial Statements comply with International Financial Reporting Standards (**IFRS**).

The preparation of financial statements, in conformity with NZ IFRS, requires judgements, estimates and assumptions to be made that affect the application of policies and the reported amounts of assets and liabilities, income and expenses. The estimates and associated assumptions made are based on historical experience and other factors that are believed to be reasonable under the circumstances. The results of the estimates and associated assumptions form the basis of making the judgements about the carrying value of assets and liabilities, which are not readily apparent from other sources. Actual results may differ from these estimates.

The estimates and associated assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised, if the revision affects only that period, or in the period of the revision and future periods, if the revisions affect both current and future periods.

Judgements are made in the application of NZ IFRS, that have a significant effect on the Financial Statements, and estimates with a significant risk of material adjustment in the next year are discussed in notes 11, 12, 13 and 14.

(iii) Measurement base

The measurement base adopted is that of historical cost modified by the revaluation of investment assets, which are measured at fair value.

(iv) Presentation and functional currency

The Fund is located within New Zealand, and the performance of the Fund is measured and reported in New Zealand Dollars (**NZD**), rounded to thousands (**$000**). Therefore, these Financial Statements are presented in NZD as that is the currency of the primary economic environment in which the Fund operates. NZD is the Fund's presentational and functional currency.

(v) Accounting policies

The following particular accounting policies, which materially affect the measurement of changes in net assets, financial position and cash flows have been consistently applied in the preparation of the Financial Statements.

Reporting period

The reporting period is the year ended 30 June 2009. Comparative figures are for the year ended 30 June 2008 with restatement of tax receivables and payables to be consistent with the current year disclosure.

Investment income

Interest income is recognised using the effective interest rate of the instrument. Realised and unrealised gains or losses on financial instruments are recognised in the Statement of Changes in Net Assets. Interest income on assets, designated at fair value through profit or loss, is accrued at balance date. Dividend income is recognised in the Statement of Changes in Net Assets on the ex dividend date.

Foreign currencies

Transactions in currencies, other than NZD, are recorded in NZD at the rates of exchange prevailing on the dates of the transactions. At each balance date, assets and liabilities, that are denominated in foreign currencies, are retranslated at the rates prevailing on the balance date. Gains and losses arising on retranslation are included in the Statement of Changes in Net Assets for the period.

Expenses

All expenses recognised in the Statement of Changes in Net Assets are accounted for on an accruals basis.

Tax

The tax expense represents the sum of the tax currently payable and includes deferred tax (if any). The tax payable is based on taxable profit for the year. Taxable profit differs from profit before tax, as reported in the Statement of Changes in Net Assets, because it excludes items of income or expense that are taxable or deductible in other years, and it further excludes items that are never taxable or deductible. Taxable profit also requires that the Fair Dividend Rate (**FDR**) method be applied to investments in most overseas equities, which deems taxable income to arise regardless of the increase or decline in value of the investments.

The liability for current tax is calculated using tax rates that have been enacted or substantively enacted by the balance date.

Deferred tax is the tax expected to be payable or recoverable on differences between the carrying amounts of assets and liabilities in the Financial Statements and the corresponding tax bases used in the computation of taxable profit, and is accounted for using the balance sheet liability method. Deferred tax liabilities are recognised for all taxable temporary differences, and deferred tax assets are recognised to the extent that it is probable that taxable profits will be available against which deductible temporary differences can be utilised.

The carrying amount of the deferred tax asset is reviewed at each balance date and reduced to the extent that it is no longer probable that sufficient taxable profits will be earned to allow all or part of the asset to be recovered.

Deferred tax is calculated at the tax rates that are expected to apply in the period when the liability is settled, or the asset is realised. Deferred tax is charged or credited in the Statement of Changes in Net Assets.

Financial instruments

Financial assets and financial liabilities are recognised in the Statement of Net Assets when the Fund becomes a party to the contractual provisions of the instruments. The Fund offsets financial assets and financial liabilities if the Fund has a legally enforceable right to set off the recognised amounts and interests, and intends to settle on a net basis. The Fund derecognises a financial asset when the contractual rights to the cash flows from the financial asset expire. A financial liability is derecognised when the obligation specified in the contract is discharged, cancelled, or expires.

Investments

Investments are recognised and derecognised on the trade date where a purchase or sale is under a contract, whose terms require delivery within the timeframe established by the market concerned, and are initially measured at fair value.

Investments are designated at fair value through profit or loss. Transaction costs are expensed immediately. As the Fund's business is investing in financial assets with a view to profiting from their total return in the form of interest, dividends or increases in fair value, investments are designated at fair value through profit or loss on initial recognition. Fair values are determined after taking into account accrued interest on all applicable securities.

Fair value is an estimate of the amount of consideration that would be agreed upon in an arms' length transaction between knowledgeable willing parties who are under no compulsion to act.

Financial assets, designated at fair value through profit or loss, are measured at subsequent reporting dates at fair value, which is the bid price on the exchange on which the investment is quoted without any deduction for estimated future selling costs. If a quoted market price is not available on a recognised stock exchange, the fair value of the instrument is estimated using accepted valuation techniques.

Investments in units of collective investment vehicles (**CIVs**) are valued at the closing price, or value released by the relevant investment manager.

Impairment

Financial assets, that are stated at amortised cost, are reviewed at each balance date to determine whether there is objective evidence of impairment. If any such indication exists, the asset's recoverable amount is determined and any impairment loss is the difference between the asset's carrying amount and the present value of the recoverable amount.

Trade and Other Receivables

Trade and other receivables are initially recognised at fair value and subsequently at amortised cost. Trade and other receivables may include sales of securities and investments that are unsettled at balance date and may also include dividends and interest. Dividends and distributions are accrued when the right to receive payment is established. Interest is accrued at the balance date from the time of last payment.

Trade and other payables

Trade and other payables are not interest-bearing and are intially recorded at their fair value and subsequently at amortised cost. Any outstanding trades are recorded on trade date and are normally settled within three business days. Purchases of securities and investments, that are unsettled at balance date, are included in payables.

Derivative financial instruments and hedge accounting

Derivative financial instruments are contracts whose values are derived from changes in one or more underlying financial instruments or indices. The Fund's activities expose it primarily to the financial risks of changes in foreign currency rates, commodity prices and interest rates. The Fund may use foreign exchange forward contracts, commodity swaps and interest rate swap contracts to hedge these exposures. In other words, all derivative financial instruments are entered into for hedging purposes. The Fund does not use derivative financial instruments for speculative purposes.

Derivative instruments are initially recognised at fair value through profit or loss on the date on which a derivative contract is entered into. They are subsequently re-measured each balance date by using either quoted sales prices or appropriate valuation techniques. Any gains or losses are taken to the Statement of Changes in Net Assets in the period in which they occur. Transaction costs are expensed on initial recognition and recognised in profit or loss.

The fair value of commodity futures swaps is determined using broker quotations.

Derivatives are carried as assets when their fair value is positive, and as liabilities when their fair value is negative. The Fund does not undertake any form of hedge accounting.

The use of financial derivatives is governed by a Statement of Investment Policies, Standards and Procedures (**SIPSP**), approved by the Government Superannuation Fund Board (**the Board**), which includes written policies on the use of financial derivatives.

Goods and Service Tax

The Fund is not registered for Goods and Service Tax (**GST**). All components of the Financial Statements are stated inclusive of GST where appropriate.

Statement of Cash Flows

The following are definitions of the terms used in the Statement of Cash Flows:

- *Cash and cash equivalents*

  These comprise cash balances held with banks in New Zealand and overseas. Cash equivalents are short-term, highly liquid investments that are readily convertible to known amounts of cash, are subject to insignificant risk of changes in value, and are held for the purpose of meeting short-term cash commitments. Only items that have an original maturity of three months or less are classified as cash.

- *Investing activities*

  These comprise acquisition and disposal of investments. Investments include securities not falling within the definition of cash.

- *Operating activities*

  These include any activities that are the result of normal business activities.

Standards issued but not yet effective

A number of other standards, amendments and interpretations have been issued by the New Zealand Accounting Standards Review Board (**ASRB**), and are not yet effective. These standards are not expected to have a material impact on the Fund.

(vi) Changes in accounting policies

There were no significant changes in accounting policies during the year.

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 30 JUNE 2009

1) Interest, dividends, and other income

	2009 $000	2008 $000
NZ Government Stock	**526**	1,717
NZ Government owned/guaranteed securities	**212**	897
Local Authority bonds	**123**	203
Other bonds and securities	**1,587**	1,705
Fixed interest – international	**27,282**	39,660
Short term and call deposits, including treasury bills	**1,858**	6,323
Equities – New Zealand	**11,631**	22,000
Equities – international	**46,506**	23,020
Real Estate – international listed securities	**3,455**	3,913
Real Estate – international unlisted securities	**5,228**	2,963
Mortgages to members	**1**	2
Other sources	**17,593**	3,569
Total Interest, dividends, and other income	**116,002**	105,972

2) Changes in fair values of investment assets

	2009 $000	2008 $000
NZ Government Stock	**2,076**	2,749
NZ Government owned/guaranteed securities	**359**	(36)
Local Authority bonds	**176**	(7)
Other bonds and securities	**615**	2,312
Fixed interest – international (including hedging)	**21,096**	50,298
Short term investments	**1,738**	1,616
Equities – New Zealand	**(43,324)**	(147,556)
Equities – international (including hedging)	**(574,016)**	(250,213)
Real Estate – international listed securities (including hedging)	**(68,428)**	(53,382)
Real Estate – international unlisted securities (including hedging)	**(36,480)**	6,118
Commodity futures (including hedging)	**(90,396)**	76,577
Multi-asset and Global Tactical Asset Allocation (including hedging)	**(2,158)**	(4,572)
Total Changes in fair values of investment assets	**(788,742)**	(316,096)

3) Operating revenue and expenses

In terms of section 15E (1) of the GSF Act, the administrative expenses of the Authority, including investment management and custody expenses, are reimbursed by the Fund. Both the Government and other employers reimburse the Fund under section 95 of the GSF Act for the Authority's expenses. In the reporting period, as certified by the Government Actuary, the Government contributed 81% of the Authority's administrative expenses, including investment management and custody expenses, reimbursed by the Fund. Other employers contributed the balance of 19%.

4) Income tax

	2009 $000	2008 $000
Deficit before tax and membership activities	**(672,740)**	(210,124)
Add imputation credits	**2,796**	8,676
Net taxable income/(loss)	**(669,944)**	(201,448)
Tax credit @ 30% (2008 : 33%)	**200,983**	66,478
Tax effect:		
Non-assessable/deductible investment losses	**(89,234)**	(107,376)
Fair dividend rate (**FDR**) income	**(27,009)**	(20,910)
Other	**–**	112
Prior period adjustment	**1,893**	–
Imputation credits	**2,796**	8,676
Withholding tax credits	**–**	2,202
Income tax benefit (expense)	**89,429**	(50,818)
Income tax benefit (expense) comprises:		
Current tax	**–**	(54,465)
Deferred tax	**87,536**	3,647
Prior period adjustment	**1,893**	–
Income tax benefit (expense)	**89,429**	(50,818)
Movement in deferred taxation		
Opening balance	**–**	(39,474)
Current year movement	**87,536**	3,647
PIE/FDR transition liability	**–**	
- transfer to current tax		23,885
- transfer to non current tax	**–**	11,942
Deferred tax asset	**87,536**	–

	2009 $000	2008 $000
Non current tax payables		
Opening balance	**(11,942)**	–
Deferred tax prior period adjustment	**448**	–
PIE/FDR transition liability	**–**	
- transfer from deferred taxation		(11,942)
- transfer to current tax	**11,494**	–
Closing balance	**–**	(11,942)

With effect from 1 October 2007 the Fund qualified as, and elected to be, a Portfolio Investment Entity (**PIE**) for taxation purposes. Under the PIE tax rules any gains or losses on New Zealand and certain Australian listed shares are non-taxable, whereas those gains or losses had previously been taxable or deductible to the Fund. The effective tax rate changed from 33% to 30% for periods beginning on or after 1 April 2008.

5) Government contributions

	2009 $000	2008 $000
Government service superannuation contributions	**600,599**	672,394
Judges and Solicitor-General superannuation contributions	**14,007**	15,469
Parliamentary superannuation contributions	**3,680**	3,194
Total Government contributions	**618,286**	691,057

Funding arrangements

There is no requirement on the Government 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 GSF Act for the Government to ensure that sufficient funds are available, or will be available, to pay benefits as they fall due.

Member Contribution %	GSF Scheme	Employer Contribution %
	General Scheme:	
6.5	– Non-funding employers	6
6.5	– Funding except Islands*	Between 6 and 10
6.5	– Islands	6
7.6	Armed Forces	15.4
7.5	Police	16.1
8.5	Prisons Service	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

	2009 $000	2008 $000
Pension entitlements	**621,233**	604,316
Allowances capitalised	**75,092**	94,935
Spouses and children	**100,130**	97,234
Refunds:		
Transfers to other schemes	**82,106**	139,419
Cessation of membership	**2,168**	11,103
Death	**921**	326
Total Benefits paid	**881,650**	947,333

7) Trade and other receivables

	2009 $000	2008 $000
Government contributions – operating	**4,284**	3,575
Members' contributions	**402**	807
Other employers' contributions	**3,045**	3,914
Interest and dividends	**2,702**	3,097
Investment settlements receivable	**24,605**	168,219
Prepaid benefits	**44,647**	44,974
Past service contributions	**3,292**	3,826
Pension entitlements	**255**	296
Total Trade and other receivables	**83,232**	228,708

8) Fixed Interest - New Zealand

	2009 $000	2008 $000
NZ Government Stock	**–**	15,389
NZ Government owned/guaranteed securities	**–**	10,075
Other bonds and securities	**–**	30,908
Local Authority bonds	**–**	5,372
Total Fixed Interest – New Zealand	**–**	61,744

9) Mortgages

The Housing New Zealand Corporation manages mortgages previously granted to members of the Fund. The mortgage portfolio consists of two mortgages (2008 : two mortgages) at an average earning rate of 8.00% (2008 : 8.00%).

10) Trade and other payables

	2009 $000	2008 $000
Government receipts	**197**	196
Unallocated contributions	**29**	61
Government Superannuation Fund Authority	**6,298**	4,435
Government contributions in advance - benefits	**33,373**	31,854
Investment settlements payable	**92,643**	301,048
Total Trade and other payables	**132,540**	337,594

11) Actuarial Valuations of the Fund

Statutory actuarial valuation

Section 94 of the GSF Act 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 statutory valuation was undertaken by the Government Actuary, Mr David Benison, B.Sc. (Econ), FIA, FNZSA, as at 30 June 2008, and the report, dated August 2008, was tabled in Parliament on 25 March 2009. More information on the results of the valuation is provided in note 12 below.

New Zealand International Accounting Standards (NZ IAS)-26 actuarial valuation

In addition to the statutory valuation discussed above, the Government Actuary values the Promised Retirement Benefits in accordance with NZIAS-26 for the Financial Statements of the Fund. The most recent valuation was undertaken as at 30 June 2009 – refer note 13.

12) Statutory actuarial valuation as at 30 June 2008

Significant assumptions, used in the statutory valuation, as at 30 June 2008, were:

Discount rate	6.25% per annum
Consumer Price Index	2.50% per annum
Salary increases	3.00% per annum

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

NOTES TO THE FINANCIAL STATEMENTS

12) Statutory actuarial valuation as at 30 June 2008 (CONTINUED)

The results of the 30 June 2008 statutory valuation were:

	2008 $million	2007 $million
Past Service Liabilities		
Armed Forces contributors	187	260
General Scheme contributors (excluding Islands)	2,874	3,119
General Scheme contributors (Islands only)	31	33
Police contributors	289	417
Prisons Service contributors	29	34
Judges and Solicitor-General	32	42
Parliamentary	13	13
Pensioners	7,887	7,982
Deferred pensioners	612	662
Total Past Service Liabilities	11,954	12,564
Value of Fund Assets	3,574	4,008
Unfunded Past Service Liability	8,380	8,556

The above figures are rounded and so may not appear to add exactly.

Vested benefits are calculated as the amount payable in the event that all contributors ceased membership as at the valuation date. The vested benefit values are shown in the following table, where contributors include the inactive members. The ratio of vested benefits to past service liabilities is also shown.

	As a percentage of past service liability	*2008 $million*	*2007 $million*
Vested benefits			
Contributors:			
Armed Forces	31%	59	82
General Scheme (excl Islands)	113%	3,257	3,462
Islands	109%	34	36
Police	90%	259	361
Prisons Service	104%	29	36
Judges and Solicitor-General	n/a	47	67
Parliamentary	n/a	17	17
Total Contributors	108%	3,703	4,061
Pensioners:			
Pensioners	100%	7,887	7,982
Deferred Pensioners	100%	611	664
Total Pensioners	100%	8,498	8,645
Grand total		12,202	12,706
Less net assets		3,574	4,008
Shortfall		8,628	8,698

The above figures are rounded and so may not appear to add exactly.

The Fund has been closed to new entrants since 1992. Members with 10 or more years' service are eligible to take an immediate or deferred pension on leaving the Fund. As a result, almost all members in the Fund can take either an immediate pension or a deferred pension. The total value of this pension for all members, as at the valuation date, is the vested benefits.

Members will, however, retire at date later than 30 June 2008. The pension they receive at their actual retirement date can be split into that part accrued at the valuation date and that part which will accrue after the valuation date.

The net asset value was used as the actuarial value of the assets.

The valuation revealed that the Fund was in deficit at the date of the valuation. The benefits payable from the Fund are underwritten by the Government. The Government Actuary recommended that from 30 June 2009, the Government pays 75% of each benefit paid (previously 71%).

The rate of contribution, including employer superannuation contribution tax at 33%, that is required to be paid by funding employers (employers of those contributors who are paid from money that is not public money) has been determined under a notional funding approach, and:

- for employers that are the Public Services of the Cook Islands, Niue or Tokelau, is certified as 6.0% of contributor salaries, and
- for employers other than the Public Services of the Cook Islands, Niue or Tokelau, is certified as the average rate of contributor salaries obtained by applying the percentage rates to the contributors of the employer, by reference to gender and age nearest as at 30 June 2009 given in the following table:

Age range	*Males*	*Females*
Up to age 49	3.0%	2.0%
Age 50 to age 54	9.0%	9.0%
Age 55 to age 59	10.0%	12.3%
Age 60 to age 64	13.0%	13.0%
Age 65 and over	0.0%	0.0%

For each employer, these rates are subject to a maximum average rate of 10.0% and a minimum average rate of 6.0%, and further subject to the proviso that, if application of these rates in any case give rise to a change from the average rate currently applying for an employer of less than 0.3%, then the current rate for that employer shall continue to apply.

The rate of contribution, including superannuation contribution tax at 33%, applicable to non-funding employers (the employers of those contributors who are paid from money that is public money) is recommended by reference to the notional funding approach to be set at the following levels:

- for the Armed Forces Scheme: a rate of 15.4% of contributor salaries;
- for the General Scheme: a rate of 6.0% of contributor salaries;
- for the Police Scheme: a rate of 16.1% of contributor salaries;
- for the Prisons Service Scheme: a rate of 0% of contributor salaries;
- for the Judges & Solicitor-General Scheme: an amount equal to the benefits payable;
- for the Parliamentary Scheme: an amount equal to the benefits payable.

Movement in Promised Retirement/Past Service Benefit Liability

	2008 $million	2007 $million
Opening Gross Promised Retirement/Past Service Benefit Liability	12,564	12,098
Movements in Liability		
Benefit changes	44	76
Experience gains	42	44
Change in discount rate and Consumer Price Index	(696)	346
Closing Gross Promised Retirement/Past Service Benefit Liability	11,954	12,564

13) Actuarial valuation under NZIAS-26

The Government Actuary has estimated the value of the Promised Retirement/Past Service Benefits as at 30 June 2009 for the purposes of the Fund's Financial Statements.

Significant assumptions, used in the NZ IAS-26 valuation, as at 30 June 2009, were:

Discount rate	6.00% per annum
Consumer Price Index	2.25% per annum
Salary increases	3.00% per annum

Movement in Promised Retirement/Past Service Benefit Liability

	2009 $million	2008 $million
Opening Gross Promised Retirement/Past Service Benefit Liability	11,954	12,564
Movements in Liability		
Benefit changes	54	44
Experience gains	68	42
Change in discount rate and Consumer Price Index	26	(696)
Closing Gross Promised Retirement/Past Service Benefit Liability	12,102	11,954

Vested benefits – 30 June 2009

Vested benefits are calculated as the amount payable in the event that all contributors ceased membership as at the valuation date. The vested benefit values as at 30 June 2009 are shown in the following table, where contributors include the inactive members.

Vested benefits	2009 $million	2008 $million
Contributors	3,658	3,703
Pensioners:		
Current pensioners	8,073	7,887
Deferred pensioners	619	611
Total pensioners	8,691	8,498
Total vested benefits	12,349	12,202
Less net assets	(2,804)	(3,574)
Shortfall	9,545	8,628

The above figures are rounded so may not appear to add exactly.

14) Financial instruments

a) Management of financial instruments

The investments of the Fund are managed on behalf of the Authority by specialist investment managers, which are required to invest the assets allocated for management in accordance with the terms of written investment management agreements. The Authority has determined that the appointment of these managers is appropriate for the Fund and is in accordance with the Authority's SIPSP.

JP Morgan Chase acts as master custodian on behalf of the Authority and provides services including physical custody and safekeeping of assets, settlement of trades, collection of dividends and accounting for investment transactions.

b) Significant accounting policies

Details of the significant accounting policies and methods adopted, including the criteria for recognition, the basis of measurement and the basis on which revenues and expenses are recognised in respect of each class of financial asset and financial liability, are disclosed in the Statement of Accounting Policies.

c) Capital risk management

The Strategic Asset Allocation (SAA) of the Fund is reviewed regularly by the Authority, in conjunction with its advisors. The Authority reviews, on a monthly basis, the cash requirements and funding of the GSF Schemes in the context of maintaining the SAA and redeems or invests funds as appropriate. The Fund's Investment Strategy is reviewed regularly, considering the investment requirements of the Fund.

d) Categories of financial instruments

The Fund recognises all investment financial assets and liabilities at fair value through the Statement of Changes in Net Assets, as detailed in the Statement of Accounting Policies, and other financial assets and liabilities at amortised cost.

	2009 $000	2008 $000
Financial investment assets at fair value	**2,452,759**	3,511,680
Financial investment liabilities at fair value	**27,281**	120,287
Financial assets at amortised cost	**400,240**	518,542
Financial liabilities at amortised cost	**133,996**	344,500

e) Financial risk management objectives

The Fund is exposed to a variety of financial risks as a result of its activities. These risks include market risk (including currency risk, fair value interest rate risk and price risk), credit risk, liquidity risk and cash flow interest rate risk. The Fund's risk management and investment policies, approved by the Authority, seek to minimise the potential adverse effects of these risks on the Fund's financial performance, within the context of the Risk Parameter (See page 4). These policies may include the use of certain financial derivative instruments to manage risk to within the approved limits.

The Authority outsources the investment management to specialist managers, which provide services to the Fund, co-ordinate access to New Zealand and international investment markets, and manage the financial risks relating to the operations of the Fund in accordance with investment mandates set by the Authority. The Fund invests in a diversified portfolio of stocks listed on the New Zealand Stock Exchange (**NZX**) and international stock exchanges and fixed interest securities, and it may also invest in derivative instruments such as futures and options.

The Fund does not enter into or trade derivative financial instruments for speculative purposes. The use of financial derivatives is governed by the Authority's SIPSP, which provides written policies on the use of financial derivatives. These policies permit the use of derivatives to change the Fund's exposure to particular assets. Derivatives cannot be used directly to leverage the Fund and the Fund's effective market exposure should not exceed the market value of its assets. Compliance with policies and exposure limits is reviewed by the Authority on a continuous basis.

f) Credit risk

Credit risk refers to the risk that a counterparty will default on its contractual obligations, resulting in financial loss to the Fund. The Authority has adopted the policy of only dealing with creditworthy counterparties and obtaining sufficient collateral, or other security where appropriate, as a means of mitigating the risk of financial loss from default. The Authority measures credit risk on a fair value basis. The Fund's exposure and the credit ratings of its counterparties are continuously monitored by the Authority.

Credit risk, arising on investments, is mitigated by investing in rated instruments or instruments issued by rated counterparties with credit ratings for the portfolio as a whole of at least a weighted average of A-, or better, as determined by Standard and Poor's. Credit risk associated with receivables is considered minimal. The main receivables balance is in relation to investments sold, which are settled within three days of trade date, and for which the counterparties are mainly large financial institutions. Other receivables balances are largely immaterial.

The Fund does not have any significant credit risk exposure to any single counterparty, or any group of counterparties having similar characteristics. The table below shows the maximum exposure to credit risk at the reporting date. It is the opinion of the Authority that the carrying amounts of these financial assets represent the maximum credit risk exposure at the balance sheet date.

As at 30 June 2009, the Fund held investments in the multi-asset class and global tactical asset allocation at fair value which each exceeded 5% of the net assets of the Fund (2008: multi- asset class only).

Credit Risk Exposure

	2009 $000	2008 $000
Cash and cash equivalents	**317,008**	289,834
Listed equities & unit trust investments	**1,793,718**	2,576,860
Fixed interest securities	**510,270**	792,721
Derivative assets	**148,163**	134,055
Trade and other receivables	**83,232**	228,708
Other	**608**	8,044
Total credit risk exposure	**2,852,999**	4,030,222

g) Liquidity risk

The Authority's approach to managing liquidity is to ensure that it will always have sufficient liquidity to meet its liabilities. The Fund is therefore exposed to the liquidity risk of meeting benefit payments. The Authority's listed equities and fixed interest securities are considered to be realisable over a reasonable period of time, although with a market risk.

The Fund's liquidity risk is managed in accordance with the Authority's investment strategy. The Fund has a level of net outward cash flows. The Authority manages liquidity risk by maintaining cash, cash equivalents and short term investments, and through the continuous monitoring of forecast and actual cash flows and by matching the maturity profiles of financial assets and liabilities. The Authority's overall strategy to liquidity risk remains unchanged from 2008.

All the Fund's financial liabilities are expected to be paid within the next three months. The break down of the financial liabilities is as follows:

	2009 $000	2008 $000
Unsettled purchases	**92,642**	301,047
Derivative liabilities	**27,281**	120,287
Other financial liabilities	**41,354**	43,453
Total financial liabilities	**161,277**	464,787

h) Market risk

Market risk is the risk that the fair value of future cash flows of a financial instrument will fluctuate because of changes in market prices. Market risk comprises three types of risk: market interest rates (interest rate risk), foreign exchange (currency risk) and market prices (price risk). The Authority manages market risk via outsourcing its investment management; the investment managers manage the market risk relating to the operations of the Fund in accordance with investment mandates. The Authority's strategy is to invest in a diversified portfolio of equities and fixed interest securities and it may also invest in derivative instruments such as futures and options.

The Fund's exposure to market risk has increased from 2008 with the investment in the multi-asset class and the global tactical asset allocation strategy, and commodity futures.

Interest rate risk management

The Fund's activities expose it to the financial risk of changes in interest rates. Floating rate instruments expose the Fund to cash flow risk, whereas fixed interest rate instruments expose the Fund to fair value interest rate risk. The Authority monitors the Fund's exposure to interest rate risk.

The following tables detail the Fund's exposure to interest rate risk at the balance date by the earlier of contractual maturities or re-pricing. Interest rate risk is managed by the investment managers within mandates prescribed by the Authority.

Financial assets: Variable interest rate instruments	*Weighted average interest rate %*	*Less than 12 months $000*	*1-5 years $000*	*5+ $000*	***Total $000***
2009					
Cash and cash equivalents	0.52	317,008	–	–	**317,008**
Fixed interest	4.40	9,558	162,037	260,761	**432,356**
Receivables for securities		24,605	–	–	**24,605**
Mortgages	8.00	–	8	–	**8**
Total		351,171	162,045	260,761	**773,977**
2008					
Cash and cash equivalents	8.50	289,834	–	–	**289,834**
Fixed interest – New Zealand	7.53	8,277	41,245	12,222	**61,744**
Fixed interest – international	5.70	25,676	161,301	544,000	**730,977**
Receivables for Securities		168,219	–	–	**168,219**
Mortgages	8.00	–	14	–	**14**
Total		492,006	202,560	556,222	**1,250,788**

Interest rate sensitivity

The sensitivity analysis below has been determined based on the Fund's exposure to interest rates at the reporting date, and the stipulated change taking place at the beginning of the financial year and held constant throughout the reporting period, in the case of instruments that have floating interest rates. A 1% or 100 basis point increase or decrease is used when reporting interest rate risk internally.

The following table illustrates the effect on the operating surplus and net assets from possible changes in interest rate risk, that were reasonably possible based on the risk the Fund was exposed to at reporting date:

	Changes in variable +/-	*Effect on (deficit)/surplus after tax and before membership activities*	
		2009	*2008*
		$000	*$000*
Interest rate risk	1%	**17,540**	21,626

The Funds sensitivity to interest rates has decreased during the current period mainly due to the decrease in interest rates. The methods and assumptions used to prepare the sensitivity analysis have not changed during the year.

Foreign currency risk management

Foreign currency risk is the risk that the market value of future cash flows of a financial instrument will fluctuate because of changes in foreign exchange rates.

The Fund undertakes certain transactions and holds investment assets denominated in foreign currencies, hence it is exposed to the effects of exchange rate fluctuations. Exchange rate exposures are managed within approved policy limits and parameters. The Fund enters into foreign currency contracts designed to hedge some or all of its exposure to foreign currencies. This exchange rate exposure is managed in line with the Authority's SIPSP.

The Authority's overall objective is to have an exposure to foreign currencies of 20% of the total Fund (2008:10%). To achieve that objective the Authority hedges its foreign currency exposures from the Fund's asset classes as set out as follows:

Asset Class	*Pre tax (Post tax) Strategic Hedging Ratio*	*Range (Pre tax)*
International equities	103% (72%)	93% to 113%
Real estate	143% (100%)	138% to 148%
Fixed interest	100% (100%)	90% to 110%
Commodities	143% (100%)	138% to 148%
Absolute return strategies	143% (100%)	138% to 148%

The Fund's total exposure to foreign currency exchange at the reporting date, (after hedging) was $208,006,000 (2008: $193,870,000). The Fund's foreign exchange exposure, before taking into account hedging, was $2,088,306,000 (2008: $2,812,096,000).

Foreign currency sensitivity

The Fund is mainly exposed to the United States dollar (**USD**), Australian dollar, British Pound, Japanese Yen and Euro currencies.

The fixed interest managers are responsible for managing the exposure to other currencies back to the USD, within the terms of their individual investment mandates. Another manager hedges the USD exposure to the NZD. For international equities the foreign currency exposure is hedged back to the NZD within the limits approved by the Authority.

The following table details the Fund's sensitivity to a 5 percent increase or decrease in the NZD against the USD, assuming there is no hedging. This represents the Authority's assessment of the possible change in foreign exchange rates. The sensitivity analysis includes only outstanding foreign currency denominated items and adjusts their translation at the period end for a 5 percent change in foreign currency rates.

	Changes in variable +/-	*Effect on (deficit)/surplus after tax and before membership activities*	
		2009	*2008*
		$000	*$000*
Operating surplus before finance costs allocated to members	5%	**42,643**	60,586

A positive impact results in an increase in the surplus or a reduction of the deficit, after tax and before membership activities, where the NZD weakens against other currencies. For a strengthening of the NZD against other currencies there would be an equal and opposite impact on the surplus or deficit, and the amounts above would be negative.

There have been no changes in the methods and assumptions used to prepare the foreign currency sensitivity analysis from the prior year.

Other market risk

Other market risk is the risk that the total value of investments will fluctuate as a result of changes in market prices, whether caused by factors specific to an individual investment or its issuer, or to factors affecting all instruments traded in the market. The Fund has investments in equity instruments, fixed interest instruments and derivative financial instruments, which exposes it to price risk. The investment managers manage the other market risk in accordance with the Authority's SIPSP and their mandates.

As the Fund's financial instruments are carried at fair value, with changes in fair value recognised in the Statement of Changes in Net Assets, all changes in market conditions will directly affect investment income.

The following table illustrates the effect on the operating surplus and net assets from possible changes in market price risk, that were reasonably possible based on the risk that the Fund was exposed to at reporting date:

	Changes in variable +/-	*Effect on (deficit)/surplus after tax and before membership activities*	
		2009	*2008*
		$000	*$000*
Other market risk	5%	**61,404**	72,494

The Authority does not believe there are any financial assets past due at balance date.

15) Related parties

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

The Fund had business transactions with the Government, Crown Entities, and State Owned Enterprises, together with a number of other public sector entities, on an arms' length basis:

- The Fund had invested a proportion of its assets in New Zealand Government Stock and Treasury Bills. The Fund's interests are disclosed in the notes to the Financial Statements.
- The Authority managed the Fund's assets and administered the GSF Schemes. For the year ended 30 June 2009, the Fund paid the Authority $23,680,000 (2008 : $19,760,000) for operating expenses, as detailed in the Statement of Changes in Net Assets. In turn, the Fund was reimbursed by the Government and other employers, as set out in Note 3.

16) 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 fair value of investment assets.
- Decreases for values of investments and delays in appointing investment managers resulted in lower operating expenses (including investment management and custody expenses) than the forecast set out in the Statement of Changes in Net Assets. During the year the number of investment managers have increased and resulted in a increase in fees paid as compared to previous year.
- 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, unexpected salary changes, or transfers to other superannuation schemes.

17) Subsequent Events

There have been no material events after balance date that require adjustments to, or disclosure in, the Financial Statements. (2008: Nil).

AUDIT REPORT

TO THE READERS OF THE GOVERNMENT SUPERANNUATION FUND'S FINANCIAL STATEMENTS FOR THE YEAR ENDED 30 JUNE 2009

The Auditor-General is the auditor of the Government Superannuation Fund (the "Fund"). The Auditor-General has appointed me, Ian Marshall, using the staff and resources of Deloitte, to carry out the audit of the financial statements and performance information of the Fund, for the year ended 30 June 2009.

Unqualified Opinion

In our opinion the financial statements of the Fund on pages 29 to 55:

- comply with generally accepted accounting practice in New Zealand;
- comply with International Financial Reporting Standards; and
- fairly reflect:
  - the Fund's Statement of Net Assets as at 30 June 2009; and
  - the changes in net assets and cash flows for the year ended on that date.

The audit was completed on 20 August 2009, 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 do 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 2009. 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 New Zealand Institute of Chartered Accountants.

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

Ian Marshall
On behalf of the Auditor-General

DELOITTE
WELLINGTON, NEW ZEALAND

GOVERNMENT SUPERANNUATION FUND AUTHORITY
STATEMENT OF RESPONSIBILITY

The Financial Statements of the Authority, for the year ended 30 June 2009, have been prepared in accordance with section 154 of the Crown Entities Act.

The Board is responsible for the preparation of the Financial Statements and the Statement of Service Performance, and for the judgments made in them.

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

In our opinion, the Statement of Service Performance set out on pages 16-21, and the attached Financial Statements for the financial year fairly reflect the financial position, as at 30 June 2009, and the operations of the Authority for the year ended 30 June 2009.

Tim McGuinness
Chairman
Government Superannuation Fund Authority Board

Keith Taylor
Chairman
Audit & Risk Review Committee
Government Superannuation Fund Authority Board

20 August 2009

GOVERNMENT SUPERANNUATION FUND AUTHORITY

INCOME STATEMENT

FOR THE YEAR ENDED 30 JUNE 2009

	Note	**2009 $000 Actual**	2008 $000 Actual	2009 $000 Forecast
Revenue				
Interest received		**10**	14	14
Other revenue, including rental from the Bowen space		**586**	753	404
Transfer from the Government Superannuation Fund	1	**23,680**	19,760	33,490
Total revenue		**24,276**	20,527	33,908
Expenses				
Scheme administration		**2,696**	2,301	2,756
Investment management and custody	2	**16,981**	13,891	26,155
Operating	3	**4,599**	4,335	4,997
Total expenses		**24,276**	20,527	33,908
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
BALANCE SHEET

FOR THE YEAR ENDED 30 JUNE 2009

	Note	2009 $000 Actual	2008 $000 Actual	2009 $000 Forecast
Public equity				
General fund		**–**	–	–
Total public equity		**–**	–	–
Represented by:				
Current assets				
Cash and cash equivalents		**339**	56	170
Trade & other receivables	4	**6,451**	4,506	2,870
Total current assets		**6,790**	4,562	3,040
Non – Current assets				
Trade & other receivables	4	**13**	56	–
Total non – current assets		**13**	56	–
Total assets		**6,803**	4,618	3,040
Current liabilities	5			
Trade & other payables		**6,803**	4,618	3,040
Total current liabilities		**6,803**	4,618	3,040
Net assets		**–**	–	–

The Financial Statements were approved by the Government Superannuation Fund Authority Board on 20 August 2009.

Tim McGuinness
Chairman
Government Superannuation Fund Authority Board

Keith Taylor
Chairman
Audit & 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 2009

	Note	2009 $000 Actual	2008 $000 Actual	2009 $000 Forecast
Cash flows from operating activities				
Cash was provided from:				
Government Superannuation Fund	1	**21,801**	17,430	33,465
Interest		**10**	14	14
Other		**406**	686	404
		22,217	18,130	33,883
Cash was disbursed to: Total expenses		**(21,934)**	(18,356)	(33,843)
		(21,934)	(18,356)	(33,843)
Net cash flows from operating activities		**283**	(226)	40
Net increase/(decrease) in cash held		**283**	(226)	40
Opening cash and cash equivalents		**56**	282	130
Closing cash and cash equivalents		**339**	56	170

Reconciliation of net operating result to net cash flows from operating activities

	2009 $000 Actual	2008 $000 Actual	2009 $000 Forecast
Net operating result	**–**	–	–
Movements in working capital items:			
Receivables and prepayments	**(1,902)**	(2,255)	(25)
Payables	**2,185**	2,029	65
Net cash flows from operating activities	**283**	(226)	40

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 MOVEMENT IN PUBLIC EQUITY

FOR THE YEAR ENDED 30 JUNE 2009

	2009	*2008*	*2009*
	$000 Actual	*$000 Actual*	*$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	**–**		–

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 COMMITMENTS

FOR THE YEAR ENDED 30 JUNE 2009

Section 22 of the Government Superannuation Fund Amendment Act 2001 (**the Amendment Act**) vested in the Government Superannuation Fund Authority (**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 terminated on 17 February 2009.

The Authority had entered into subleases with the Ministry of Economic Development (**MED**) and Accident Compensation Corporation (**ACC**) for the Bowen space. The MED and ACC subleases ended on 31 January 2009.

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

The Authority had an obligation under the lease contract to redecorate the Bowen space on 17 February 2009. A full and final payment of $382,500 (including GST) on 16 June 2009 settled this obligation. In terms of the lease agreement, the Authority has no further commitments to the Bowen space (2008:$485,000).

In terms of section 19(1) of the GSF Act the Authority appointed Datacom Employer Services Ltd to administer the GSF Schemes for a term of six years from 26 April 2005.

	2009 $000	*2008 $000*
Non-cancellable contractual commitments		
Scheme administration not later than one year	**2,660**	2,684
Scheme administration later than one year and not later than two years	**2,210**	2,660
Scheme administration later than two years and not later than five years	**–**	2,210
Total non-cancellable contractual commitments payable	**4,870**	7,554

The Authority has also committed $2,500,000 for ongoing expenditure on the upgrade of the GSF business system used in the administration of the GSF Schemes.

On 1 December 2007 the Authority entered into a new Management Services Agreement (**MSA**) with Annuitas Management Limited (**Annuitas**), a joint venture company formed by the Authority and the Board of Trustees of the National Provident Fund (**NPF**), to provide secretarial and executive support to the Authority and NPF.

Estimated commitments under the existing MSA are:

	2009 $000	*2008 $000*
Management services not later than one year	**1,950**	1,950
Management services later than one year and not later than two years	**2,050**	2,050
Management services later than two years and not later than five years	**6,150**	3,100
	10,150	7,100

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 CONTINGENT LIABILITIES

FOR THE YEAR ENDED 30 JUNE 2009

There were no contingent liabilities as at 30 June 2009.

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 ACCOUNTING POLICIES

The following policies have been applied in the preparation of the Financial Statements:

(i) Reporting entity, basis of preparation and statutory base

The Authority was established as a Crown entity by section 15A of the GSF Act and became an autonomous Crown entity under the Crown Entities Act. The core business of the Authority is to manage the Government Superannuation Fund (**the Fund**) and administer the GSF Schemes. The Authority is an Autonomous Crown Entity for legislative purposes and a Public Benefit Entity for financial reporting purposes.

These Financial Statements have been prepared in accordance with section 154 of the Crown Entities Act.

Separate Financial Statements have been prepared for the Fund in terms of section 93 of the GSF Act.

(ii) Statement of compliance

The Financial Statements have been prepared in accordance with Generally Accepted Accounting Practice in New Zealand (**NZ GAAP**), applying the New Zealand equivalents to International Financial Reporting Standards and its interpretations (**NZ IFRS**), as appropriate, for Public Benefit Entities. The Authority is a public benefit entity, which is domiciled in New Zealand.

The preparation of Financial Statements, in conformity with NZ IFRS, requires judgements, estimates and assumptions to be made that affect the application of policies and the reported amounts of assets and liabilities, income and expenses. The estimates and associated assumptions made are based on historical experience and other factors that are believed to be reasonable under the circumstances. The results of the estimates and associated assumptions form the basis of making the judgements about the carrying value of assets and liabilities, which are not readily apparent from other sources. Actual results may differ from these estimates.

The estimates and associated assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which an estimate is revised, if the revision affects only that period, or in the period of the revision and future periods, if the revisions affect both current and future periods.

The accounting policies set out below have been applied consistently to all periods presented in these Financial Statements.

(iii) Measurement base

The measurement base adopted is that of historical cost.

(iv) Presentational and functional currency

The Financial Statements are presented in New Zealand dollars (**NZD**), rounded to thousands (**$000**), which is also the Authority's functional currency.

(v) 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:

Forecast figures

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

The forecast figures were prepared in accordance with generally accepted accounting practice, and are consistent with the accounting policies adopted by the Board for the preparation of the Financial Statements.

Goods and services tax

The Authority makes principally exempt supplies for Goods and services tax (**GST**) purposes as it manages superannuation schemes. GST is 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 the provision of investment reports. Apart from GST on transactions relating to the lease of the Bowen space, which was recoverable as input tax, GST is included in expenditure.

Tax

As a public authority, in terms of the Income Tax Act 2004, the Authority is exempt from income tax.

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 in New Zealand, used in the day to day cash management of the activities of the Authority.
- *Operating activities*

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

  Financing activities relate to changes in equity capital structure.

Operating leases

Section 22 of the Amendment Act, vested in the Authority the Bowen space. The lease of the Bowen space was classified as an operating lease. Receipts and payments under the lease were recognised as revenue and expenses on a straight line basis over the lease term. The lease of the Bowen space was terminated on 17 February 2009.

Financial instruments

The categories of financial assets and financial liabilities comprise:

- financial assets that are classified as loans and receivables. These include various bank term deposits, receivables from related parties and other receivables.
- financial liabilities, that are not at fair value through profit or loss, are classified as other liabilities and measured at amortised cost. These include trade and other payables.

Recognition

The Authority recognises a financial asset or a financial liability on the date the Authority becomes a party to the contractual provisions of the instrument.

Measurement

Financial instruments are measured initially at fair value. Transaction costs are expensed immediately.

Financial assets, classified as receivables, and other financial liabilities are carried at amortised cost using the effective interest rate method, less impairment losses, if any.

Fair Value Measurement Principles

The fair value of financial instruments is based on the calculated value, including accrued interest for term deposits at the balance sheet date, without any deduction for estimated future selling costs.

Impairment

Financial assets, that are stated at amortised cost, are reviewed at each balance sheet date to determine whether there is objective evidence of impairment. If any such indication exists, an impairment loss is recognised in the Income Statement as the difference between the asset's carrying amount and the present value of estimated future cash flows.

Derecognition

The Authority derecognises a financial asset when the contractual rights to the cash flows from the financial asset expire, or it transfers the financial asset and the transfer qualifies for derecognition in accordance with NZ IAS 39 Financial Instruments. A financial liability is derecognised when the obligation specified in the contract is discharged, cancelled or expired.

Foreign currencies

The Authority, from time to time, pays the managers of international equities and international fixed interest for management fees in currencies other than NZD. Due to the nature of these payments there are no currency gains or losses.

Revenue

Revenue is recognised on an accrual basis. Interest income, on assets classified as receivables, is accrued at balance date using the effective interest rate of the instrument.

Expenses

All expenses recognised in the Income Statement are accounted for on an accrual basis.

Accounting for Joint Ventures

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.

Standards issued but not yet effective

A number of other standards, amendments and interpretations have been issued by the New Zealand Accounting Standards Review Board (**ASRB**), and are not yet effective. These standards are not expected to have a material impact on the Authority.

(vi) Reporting period

The reporting period is the year ended 30 June 2009. Comparative figures are for the year ended 30 June 2008.

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 30 JUNE 2009

1) Transfer from the Fund

In terms of section 15E (1) of the GSF Act, the administrative expenses of the Authority, including investment management and custody expenses, are reimbursed by the Fund. Both the Government and other employers reimburse the Fund under section 95 of the GSF Act for the Authority's expenses. In the reporting period, as certified by the Government Actuary, the Government contributed 81% of the Authority's administrative expenses, including investment management and custody expenses, reimbursed by the Fund. Other employers contributed the balance of 19%.

2) Investment management and custody

	2009 $000	2008 $000
Investment management expenses	**15,539**	12,457
Custodian expenses	**1,442**	1,434
Total Investment management and custody	**16,981**	13,891

3) Operating expenses

	2009 $000	2008 $000
Operating expenses include (but are not limited to):		
Audit	**159**	143
Other assurance fees paid to Auditor – IFRS	**–**	25
Other assurance fees paid to Auditor – Probity	**9**	4
Board fees and expenses	**220**	196
Gross rental and outgoings – Bowen space	**489**	766
Make good – Bowen space	**343**	–
Annuitas Management Limited	**1,762**	1,501

4) Trade and other receivables

	2009 $000	2008 $000
Government Superannuation Fund	**6,314**	4,435
Other receivables and prepayments	**144**	116
Annuitas Management Limited	**6**	11
Total trade and other receivables	**6,464**	4,562
Current	**6,451**	4,506
Non current	**13**	56

5) Trade and other payables

	2009 $000	2008 $000
Investment management	**6,445**	3,920
Professional services	**334**	501
Other creditors	**24**	197
Total Trade and other payables	**6,803**	4,618

6) Financial instruments

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, cash equivalents and receivables. The Authority has a minimal credit risk in its holdings of cash, cash equivalents, 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 amounts due from the Fund, which is an obligation of the Government in terms of section 15E of the Act.

The maximum amount of credit risk for each class is the carrying amount in the Balance Sheet.

Currency risk

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

The Authority has United States dollars (USD) 740,000 (2008: USD 1,073,000) and Australian dollars (AUD) 64,000 (2008: AUD Nil) management fees owing in foreign currency at balance date to two international fixed interest, and four international equity managers. This is the total exposure to currency risk.

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.

Fair values

The fair values of financial instruments are equivalent to the carrying amounts disclosed on the Balance Sheet.

7) Employee remuneration

The Authority has no employees.

Annuitas provides staff who act in management and secretarial roles for both the Authority and NPF.

During the year Annuitas employed 14 staff (including 2 part time) (2008: 13 (including 2 part time)). Total remuneration was $2,269,697 (2008: $1,982,705) and the Authority reimbursed $1,361,818 (2008: $1,130,000), or 60% (2008 : 57%) of the total.

8) Board fees

Board members were paid the following fees during the period

	2009 $000	2008 $000
Chairman		
Tim McGuinness*	**46,400**	22,883
Deputy Chairman		
David May	**29,000**	26,187
Members		
Helen Bowie	**23,200**	20,950
Ralph Stockdill	**23,200**	20,950
Susie Weaver	**23,200**	20,950
Steve Napier (appointed September 2008)	**21,267**	–
Keith Taylor (appointed September 2008)	**21,267**	–

*Appointed as Chairman 01 June 2008 therefore the comparison is for his membership (predominantly) as a Board member only

The Authority also met Board members' travel and other expenses, where applicable, to attend Board meetings, and for travel on matters directly related to the business of the Authority. Travel and other expenses totalled $12,250 in 2009 (2008: $5,849).

The Authority continued with Directors' and Officers' insurance cover for Board members and members of the Management team, and Company Reimbursement insurance in respect of any claims made by Board members, or members of the Management team, under indemnities provided by the Authority. The total cost of the insurance was $19,125 (2008: $19,125) per annum.

9) Related party information

The Authority is an autonomous Crown entity.

In terms of section 19(1) of the GSF Act the Authority has appointed Datacom Employer Services Ltd to administer the GSF Schemes for a term of six years from 26 April 2005.

The Authority has entered into various transactions with Government entities on an arm's length basis in the normal course of business. During the year the Authority entered into a resource sharing agreement with the Guardians of New Zealand Superannuation (**the Guardians**) to work jointly with the Guardians on the Authority's Responsible Investing Policies. David May (Deputy Chairman) is Chairman of the Guardians. Other Crown Financial Institutions, including the Earthquake Commission (**EC**), are also involved in this resource sharing agreement with the Guardians. Keith Taylor (Board member) is the Deputy Chair of the EC Board.

The Authority and the NPF have formed a joint venture company, Annuitas. Each organisation has entered into a management services agreement with Annuitas. The main function of Annuitas is to provide staff (**Management**) who act in management and secretarial roles on behalf of the Authority and the NPF. The Authority has appointed Board members, Tim McGuinness and David May, as directors of Annuitas. The costs of running Annuitas are shared between the Authority and the NPF on an equitable basis, as agreed between the two parties. The Authority paid fees for this service during the year amounting to $1,762,000 (2008 : $1,501,000). The amount owing by Annuitas to the Authority at year end was $6,279 (2008: $11,253).

The Authority, through Management, monitors the performance of the managers, appointed by the Authority to provide services to the Authority, and their adherence to the terms of their contracts, and co-ordinates actuarial, accounting, taxation, legal and communication services for the Authority.

There were no transactions between the Board members as individuals and the Authority, other than the payment of fees or expenses. There were no individual transactions with Management.

10) Actual versus forecast

Decreases in fair values of investments of the Fund and delays in appointing new investment managers resulted in lower investment management and custody expenses than the forecast set out in the Income Statement.

Deloitte.

AUDIT REPORT

TO THE READERS OF THE GOVERNMENT SUPERANNUATION FUND AUTHORITY'S FINANCIAL STATEMENTS AND STATEMENT OF SERVICE PERFORMANCE FOR THE YEAR ENDED 30 JUNE 2009

The Auditor-General is the auditor of the Government Superannuation Fund Authority (the "Authority"). The Auditor-General has appointed me, Ian Marshall, using the staff and resources of Deloitte, to carry out the audit of the financial statements and statement of service performance included in the annual report of the Authority for the year ended 30 June 2009.

Unqualified Opinion

In our opinion the financial statements of the Authority on pages 59 to 71:

- comply with generally accepted accounting practice in New Zealand; and
- fairly reflect:
    - the Authority's financial position as at 30 June 2009; and
    - the results of its operations and cash flows for the year ended on that date.

The statement of service performance of the Authority on pages 16 to 21:

- complies with generally accepted accounting practice in New Zealand; and
- fairly reflects for each class of outputs:
    - its standards of delivery performance achieved, as compared with the forecast standards outlined in the statement of forecast service performance adopted at the start of the financial year; and
    - its actual revenue earned and output expenses incurred, as compared with the forecast revenues and output expenses outlined in the statement of forecast service performance adopted at the start of the financial year.

The audit was completed on 20 August 2009, and is the date at which our opinion is expressed.

The basis of our opinion is explained below. In addition, we outline the responsibilities of the 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 the audit to obtain all the information and explanations we considered necessary in order to obtain reasonable assurance that the financial statements and statement of service performance 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 and the statement of service performance. If we had found material misstatements that were not corrected, we would have referred to them in our opinion.

The audit involved performing procedures to test the information presented in the financial statements and statement of service performance. 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 and statement of service performance disclosures are adequate.

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

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

Responsibilities of the Government Superannuation Fund Authority Board and the Auditor

The Board is responsible for preparing financial statements and a statement of service performance in accordance with generally accepted accounting practice in New Zealand. The financial statements must fairly reflect the financial position of the Authority as at 30 June 2009 and the results of its operations and cash flows for the year ended on that date. The statement of service performance must fairly reflect, for each class of outputs, the Authority's standards of delivery performance achieved and revenue earned and expenses incurred, as compared with the forecast standards, revenue and expenses adopted at the start of the financial year. The Board's responsibilities arise from the Crown Entities Act 2004 and the Public Finance Act 1989.

We are responsible for expressing an independent opinion on the financial statements and statement of service performance and reporting that opinion to you. This responsibility arises from section 15 of the Public Audit Act 2001 and the Crown Entities Act 2004.

Independence

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

Other than the audit, and the provision of other assurance services, we have no relationship with or interests in the Authority.

Ian Marshall
On behalf of the Auditor-General

DELOITTE
WELLINGTON, NEW ZEALAND

GOVERNMENT SUPERANNUATION FUND AUTHORITY DIRECTORY

As at 2 September 2009

Government Superannuation Fund Authority Board
Tim McGuinness (Chairman)
David May (Deputy Chairman)
Helen Bowie
Steve Napier
Ralph Stockdill
Keith Taylor
Susie Weaver

Executive office
Level 12, The Todd Building
95 Customhouse Quay
PO Box 3390
Wellington

Scheme administrator
Datacom Employer Services Limited
Level 6, New Zealand Post House
7-27 Waterloo Quay
PO Box 3614
Wellington

Custodian
JP Morgan Chase Bank NA

Investment adviser
Russell Investment Group Limited

Tax adviser
PricewaterhouseCoopers

Actuary
Government Actuary

Auditor
Ian Marshall
Deloitte
on behalf of the Auditor-General

Bankers
Bank of New Zealand (Authority)
National Bank of New Zealand Limited (Fund)

Solicitors
DLA Phillips Fox
Crown Law

Investment managers

New Zealand fixed interest
AMP Capital Investors (New Zealand) Limited (*to July 2009*)

International fixed interest
Pacific Investment Management Company LLC
Goldman Sachs Asset Management International (*to January 2009*)
Wellington Management Company LLP

New Zealand equities
AllianceBernstein New Zealand Limited
ING (NZ) Limited

International equities
Altrinsic Global Advisers, LLC
Arrowstreet Capital Limited Partnership
AXA Rosenberg Investment Management Asia Pacific Ltd (*from September 2008*)
Genesis Emerging Markets Investment Company (*from April 2009*)
Marathon Asset Management LLP
PanAgora Asset Management, Inc
Pzena Investment Management LLC (*from April 2009*)
T. Rowe Price Global Investment Services Limited

Real estate
AMP Capital Redding Investors Limited
LaSalle Investment Management (Securities) L.P.
RREEF America REIT II, Inc

Collateralised commodity futures
Commodities swap
Goldman Sachs International (*to July 2009*)
Gresham Investment Management LLC (*from July 2009*)

New Zealand Cash
AMP Capital Investors (New Zealand) Limited (*to July 2009*)

Multi-asset
Makena Capital Management (Cayman), LLC (*from January 2008*)

Global tactical asset allocation
AQR Capital Management, LLC

Currency management
International equities and real estate
State Street Global Advisors, Australia, Limited

International fixed interest
ANZ National Bank Limited

DIRECTORY (CONTINUED)

All correspondence relating to the GSF Schemes should be addressed to –
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GSF Scheme Administration
Level 6, New Zealand Post House
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PO Box 3614
Wellington

or

Chief Executive
Government Superannuation Fund Authority
PO Box 3390
Wellington

GOVERNMENT SUPERANNUATION FUND AUTHORITY
STATEMENT OF INVESTMENT POLICIES, STANDARDS AND PROCEDURES

This document is titled Statement of Investment Policies, Standards and Procedures (**SIPSP**) and is dated 05 August 2009. An electronic copy is available via website *www.gsfa.co.nz*

No liability

While the Authority has made every effort to ensure that the information provided in this document is accurate, neither the Authority nor its advisors will be liable whether in contract or in tort (including negligence), equity or any other cause of action to any persons or person who rely on the information without the prior agreement of the Authority.

Change without notice

The Authority may change the information in this document at any time and without providing any notice to any party of any changes.

CONTENTS

1 INTRODUCTION

1.1 The Authority

The Government Superannuation Fund Authority (**the Authority**) was established in 2001 to manage and administer the assets of the Government Superannuation Fund (**GSF** or **the Fund**) and the Government Superannuation Fund Schemes (**GSF Schemes**) in accordance with the Government Superannuation Fund Act 1956 and subsequent amendments (**the GSF Act**). The Authority is an autonomous Crown entity under the Crown Entities Act 2004 (**Crown Entities Act**).

1.2 Purpose

This Statement of Investment Policies, Standards and Procedures (**SIPSP**) records the arrangements set by the Authority's Board (**the Board**) for the governance and management of the investment assets held by the Fund. The Board's governance defines fiduciary roles and responsibilities, establishes the decision-making processes and the policies and procedures for management of the investment assets of the Fund.

1.3 The GSF Act

The Authority manages the assets of the Fund in accordance with the requirements of the GSF Act. Extracts from sections 15J (2), 15L and 15M of the GSF Act are set out below.

Section 15J (2) of the GSF 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 15L of the GSF 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 of the GSF Act requires that:

> *"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."*

1.4 Review

This document is dated 05 August 2009 and supersedes all previous versions. This document is subject to regular review and amendment as the Fund's investment strategy evolves. A version control document is maintained by the Board.

2 THE FUND MANAGEMENT STRUCTURE AND GOVERNANCE

Required under section 15M (f)- the Fund management structure.

2.1 Policies

The Board is the governing body of the Authority and is responsible for making all decisions relating to the Fund. The Board has all the powers necessary for managing, and for directing or supervising the management of, the business of the Authority and the Fund. The Authority's key governance document its Corporate Governance Statement, incorporating the requirements set out in the Act, the Crown Entities Act 2004, other legislation and regulation, and policies and practices developed by the Board. A copy of the Authority's Corporate Governance Statement can be found on the website *www.gsfa.govt.nz*

The Board has established an Investment Committee and Responsible Investing Committee to perform and exercise the functions and powers of the Board delegated to each committee, as applicable. Committees have written terms of reference and ensure that their activities remain consistent with the Crown Entities Act. Each committee reviews its performance annually and is also reviewed by the Board;

The Board is supported by a Management team who act in management, operational and secretarial roles on behalf of the Authority. Clear separation of the governance and operational functions is maintained. The Board retains the power of appointment of investment managers and custodians.

The Authority has outsourced the key activities of scheme administration and investment management (including custody of the Fund's assets) as well as legal, tax and investment advisory functions and communication services.

In terms of the GSF Act, the Government Actuary is the actuary for the Fund and the Auditor-General is the auditor.

2.2 Standards

(a) A global custodian is appointed 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 (undertaken by the global custodian).

All the assets of the Fund, apart from cash holdings required for operational liquidity purposes, are held under custody, unless specifically authorised by the Board.

(b) Cash required for operational liquidity purposes is managed by the Authority's Management.

(c) Third party investment managers have been engaged to invest the assets of the Fund. Details of the current investment managers can be found on the website *www.gsfa.co.nz*

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 MSA between the Authority and Annuitas contains delegations of authority to enable Management to carry out the day to day management of the Authority's investment, custody and scheme administration arrangements. In relation to investments, Management is primarily responsible for the identification and implementation of appropriate strategies for the Authority to meet its obligations under the GSF Act and its objectives. This includes the management of contracted services, including investment management, custodial and external advisers, maintaining financial accounting and performance calculations and contract and compliance monitoring.

2.3 Procedures

Selection of managers is made in accordance with the Authority's Policy on Procurement of Services.

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

- best-practice portfolio management;
- the skills and experience the manager brings to the role;
- the substance and viability of the manager;
- the costs that can be expected to be incurred;
- the potential for cost savings and other efficiency gains; and
- the existence of appropriate risk management structures.

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

Investment mandates shall include guidelines setting out 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.

3 STATEMENT OF INVESTMENT BELIEFS

3.1 Policies

The Board believes that it is essential to have a clear set of investment beliefs to communicate its values and to provide a basis for its investment actions. Accordingly the Board has adopted the following set of Investment Beliefs.

3.2 Standards

(a) **Higher returns generally require acceptance of higher risks and diversification reduces total risk**

Investors generally demand a return premium to compensate them for investing in risky assets. Total investment risk can be reduced for any given return target by investing in a diversified range of asset classes. Risk is reduced by exposure to different sources of return that are complementary or not closely related and, within an asset class, by investing across a range of industries, countries and entities. Diversification reduces risk but has a proportionately lesser effect on returns. A portfolio that is well-diversified, both across and within asset classes, will deliver more consistent returns over time than a less diversified portfolio.

(b) **Setting a strategic asset allocation appropriate to the Fund's long term objectives is the most important investment decision as it creates the majority of the Fund's risk and return**

Setting, managing and monitoring the appropriateness of the strategic asset allocation and exposures to major market risks are the key investment management functions. Although active management may be engaged to seek additional sources of return to the underlying asset class returns, the additional impact on the risk and return characteristics of the portfolio is secondary compared to the risks and returns of the underlying markets themselves.

(c) **Markets vary in their efficiency, and market inefficiencies offer skilful 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 inefficiencies. It is possible to identify skilful managers by thorough research. The higher expected returns from active management should be weighed against the higher costs and any tax implications arising from active management. Rewards from active management will be maximised by engaging skilful managers with diversified investment approaches.

(d) **Market timing is not a reliable source of return in the short term because of the unpredictability of returns over short periods, but account should be taken of unusual asset price behaviour with respect to longer term indicators of relative reward for risk**

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. Returns are affected in the short term as new information is incorporated into asset prices and by uncertainty, temporary influences and sentiment. 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.

Asset prices deviate significantly from normal relationships from time to time increasing the risk of abnormal future returns (i.e. 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. Over longer periods, the more stable components of return become more evident.

(e) **Investment opportunities should be considered net of all costs and taxes and having regard to their contribution to total fund risk and return**

Investment returns should be considered net of all costs and taxes. Costs can be incurred in the form of fees, commissions, transaction expenses, and the impact of transactions on market prices. Costs can also arise from deviations from the strategic asset allocation that increase risk, maintenance of the management structure and unduly constraining investment managers' ability to add value.

In addition to considering the characteristics of an investment opportunity in its own right it is important to take into account its contribution to the total risk and return of the fund. Investments, whose risks are less correlated with the fund as a whole, generally have a lower return threshold for inclusion in the portfolio.

(f) **Costs and principal-agent risks should be controlled carefully, especially where managers are engaged to add value through their skill**

Active management requires an investment in research and skill or experience and is therefore more expensive than passive management, such as index tracking. When active managers are engaged to add value through their skill it is important to ensure the additional fees and costs are reasonable. Most importantly, where fees are related to performance, the manager's interests must be aligned strongly with those of the fund in terms of returns, risks and investment horizon.

3.3 Procedures

The Investment Beliefs are reviewed formally as part of the annual statutory review of the SIPSP and updated at other times as determined by the Board.

4 ASSET CLASSES AND SELECTION CRITERIA

Required under section 15M (a) – The classes of investments in which the Fund is to be invested and the selection criteria for investments within those classes.

4.1 Introduction

Investments can be divided into broad asset classes that share common return and risk characteristics. Each asset class differs materially from the others in its characteristics. These differences and the interaction among asset classes, when combined in a total portfolio, provide diversification that improves the total expected return available for any given level of risk.

4.2 Policies

The asset classes in which the Fund may invest are:

(a) **Equities** comprising equity securities and securities convertible into equities and includes partly paid ordinary and preference shares. The asset class includes large, mid and small capitalisation equities, emerging market and unlisted equity investments.

(b) **Real Estate** comprising land and premises built on land and holdings in entities that invest principally in land and premises.

(c) **Fixed Interest** comprising securities issued by sovereign and non-sovereign issuers and investments in various sub-sectors such as mortgage-backed and asset-backed securities and inflation linked bonds or products. The asset class includes government guaranteed debt securities (or guaranteed by an agency thereof) and non-sovereign debt, including deposits debentures, bonds, notes, promissory notes and other securities not convertible into equity at the issuers option.

(d) **Cash and short term securities** comprising New Zealand and foreign currency cash holdings, as specifically provided for in the relevant investment management. agreements for liquidity purposes or held as collateral against derivative transactions.

(e) **Commodities** comprising tangible products, such as metals, energy and agricultural products.

The Fund may invest in these asset classes through direct ownership of the assets or through investing in collective investment vehicles that hold the assets or through derivative securities, such as futures, forward contracts and options.

The Fund's investments may be traded on recognised public exchanges (**public markets**) or may be traded on **private markets.**

Private market assets and securities are generally less liquid than their public market counterparts. They include collective investment vehicles that hold eligible assets and securities, such as unit trusts, hedge funds and fund-of-funds that engage in active strategies trading among various asset classes and securities. Private market assets are generally valued by appraisal.

The selection of individual investments within the various asset classes is delegated by the Authority to professional investment managers selected for their expertise in particular investment disciplines. Each manager is mandated contractually to invest in a defined range of eligible investments which may cover one or more of the asset classes above and is subject to defined limits of investment risk.

5 THE BALANCE BETWEEN RISK AND RETURN

Required under section 15M (e) of the GSF Act – The balance between risk and return in the overall Fund portfolio.

5.1 Policies

(a) Investment Objective

The Authority's investment objective is to minimise the Crown's contribution to GSF by maximising the return on the assets of the Fund over the long term without undue risk to the Fund as a whole, within a best practice framework.

In seeking to achieve this objective over the long term, the Authority determines a level of investment risk the Fund can accept that is consistent with an expected excess return over New Zealand Government Stock (**NZGS**). The Risk Parameter defines this level of risk and the Investment Performance Measure is the expected return.

(b) Risk Parameter

The current Risk Parameter, adopted in May 2007 and confirmed in June 2008, is to have no more than a one in ten chance in any one year of a loss after tax greater than 6% of the total Fund.

(c) Investment Performance Measure (IPM)

The Authority considers that the Risk Parameter is consistent with an expected after tax return equivalent to the NZX New Zealand Government Stock Gross Return Index (after tax), plus 2.5% per annum, measured over rolling 10 year periods.

5.2 Standards

(a) Strategic asset allocations (SAA) and rebalancing ranges

The investment performance of the Fund will be determined largely by the allocation among asset classes in which the Fund invests. The SAA is selected by the Authority to maximise the likelihood of achieving the investment objective, limited by the Risk Parameter and the IPM.

The current allocation to each asset class or strategy and the rebalancing ranges is set out in Table 1.

The ranges indicate the percentage the capital allocation is permitted to deviate from the SAA before rebalancing trades are required.

Table 1: Strategic Asset Allocation (SAA) and Rebalancing Ranges

Asset Class/Strategy	SAA (%)		Rebalancing Ranges (%)	
Global equities	49.5		42 to 57	
New Zealand equities	10		7 to 13	
Property	8		4 to 12	
Total growth assets		**67.5**		**60 to 75**[1]
Fixed interest		24		18 to 30
Commodities		3		0 to 6
Absolute return strategies		5.5		0 to 11
Total assets		**100**		
Foreign currency exposure		**20**		**16 to 24**

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

(b) **Foreign exchange exposure and hedging policies**

The Authority's overall objective is to have an exposure to foreign currencies of 20% of the total Fund. To achieve that objective the Authority hedges its foreign currency exposures from the Fund's asset classes as set out in Table 2.

Table 2: Hedging Strategies

Asset Class	Pre tax (Post tax) Strategic Hedging Ratio	Range (Pre tax)
Global equities	103% (72%)	93% to 113%
Real estate	143% (100%)	138% to 148%
Fixed Interest	100% (100%)	90% to 110%
Commodities	143% (100%)	138% to 148%
Absolute return strategies	143% (100%)	138% to 148%

5.3 Procedures

(a) **Review of Objectives and SAA**

The IPM and the Risk Parameter are reviewed at least annually, taking into account the investment and taxation environment in which the Authority operates. The trade-off between risk and return is reviewed based on analysis of the prospective risk and return characteristics of each asset class in which the Fund might invest and their combinations.

(b) **Rebalancing**

Rebalancing takes place monthly to ensure the Fund remains aligned with SAA taking into account known cash flows for the following month. The asset exposure ranges are set as a trade-off between the costs of being exactly at the SAA with variations in exposures that do not compromise the Fund's investment objectives. Rebalancing takes into account private market investments that are relatively illiquid, such as equity interests in collective investment vehicles that are not traded and have contractual restrictions on redemptions.

(c) **Implementation**

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.

6 BENCHMARKS

Required under section 15M (b) – Determination of benchmarks or standards against which the performance of the fund as a whole, classes of investment, and individual investments will be assessed.

6.1 Policies

The benchmark for the Fund as a whole (and for individual asset classes) is selected to be consistent with the risk and return assumptions that underpinned determination of the strategic asset allocation for the Fund. The Fund's performance is assessed by comparing its investment return with the IPM, Risk Parameter and individual asset class or strategy benchmarks (see sections 5.1 and 5.2).

6.2 Standards

(a) **Investment Objective**

The Authority's investment objective is to minimise the Crown's contribution to GSF by maximising the return on the assets of the Fund over the long term without undue risk to the Fund as a whole, within a best practice framework.

(b) **Investment Performance Measure (IPM)**

The IPM is an expected after tax return equivalent to the NZX New Zealand Government Stock Gross Return Index (after tax), plus 2.5% per annum, measured over rolling 10 year periods.

(c) **Risk Parameter**

The current Risk Parameter, adopted in May 2007 and confirmed in June 2008, is to have no more than a one in ten chance in any one year of a loss after tax greater than 6% of the total Fund.

(d) **Multi-asset Class**

The Fund has an investment with a multi-asset class manager who manages a diversified range of both public markets' and private markets' assets including global equities, fixed interest, property and private equity, and absolute return strategies The asset allocation for reporting and monitoring purposes is set out in Table 3 below. For the strategic asset allocation set out in Table 1 on page 89 the economic exposures of the multi-asset class are re-allocated amongst the Fund's asset classes according to the multi-asset manager's long-term asset allocation targets.

Table 3: Fund Asset Allocation with Multi-asset Manager

Asset Class/Strategy	Allocation (%)
Global equities	47
New Zealand equities	10
Property	7
Fixed Interest	23
Commodities	3
Absolute return strategies	3
Multi-asset	7
Total Assets	**100**
Foreign currency exposure[1]	20

[1]The foreign currency exposure arising from the multi-asset class manager's investments is not hedged, rather the hedge ratio for global equities is adjusted so give the required Fund foreign currency exposure.

(e) **Asset Class and Strategy Benchmarks**

For the purposes of assessing asset class or strategy performance, the benchmarks set out in Table 4 are adopted.

Table 4: Asset Class and Strategy Benchmarks

Asset Class/Strategy	Benchmark
Global equities	MSCI All Countries Index
New Zealand equities	NZX 50 gross index including imputation credits
Global listed real estate – collective portfolio	UBS Warburg Global Real Estate Total Return Investors Only Index
US unlisted real estate	NCREIF Property Index
International fixed interest	Barclays Global Aggregate Index
Commodities expressed (Collateralised Commodities Futures)	Dow Jones – AIG Commodity Index expressed in US dollars
Absolute return strategies (that are not part of the Multi-asset class manager's portfolio)	US 3 month Libor + 6%
Multi-asset Class	70% MSCI World Index and 30% Barclays Global Aggregate Index

Generally, managers within an asset class have the same benchmark as the asset class. Managers may have specific benchmarks depending on their specific mandates, for example in the case of global equities the MSCI All Country World Index, the MSCI World Index, the MSCI Emerging Markets Index and the Standard and Poors ex-Australia Developed Markets Small Cap Index are used.

6.3 Procedures

(a) Any investment returns above the return for NZGS will reduce the Crown's contribution to the Fund (NZGS is a proxy for the rate at which the Crown could otherwise borrow money to pay entitlements). Performance against the Investment Objective can be measured by comparing the after tax return of the Fund with the after tax return from investing in NZGS over the same period.

(b) The Fund's performance is assessed by comparing its investment return with the IPM over rolling 10 year periods. The Authority recognises that, from year to year, investment returns may not meet the IPM.

The Board also monitors the performance of the Fund's SAA relative to the Risk Parameter and IPM and the performance of the Fund relative to its SAA. The first measure gauges the appropriateness of the SAA while the second measure gauges the effectiveness of implementation, primarily selection of active managers or strategies.

(c) The performance against the Risk Parameter is monitored by comparing the variance of the Fund's actual return with the variance consistent with a loss of 6% occurring not more than one year in ten.

The performance of asset classes or strategies is assessed by comparing the actual performance of the investment managers with the benchmarks relevant to their respective mandates, plus any excess return target expected for active managers. Investment managers' performances are generally considered over periods not less than three years.

Investment performance is generally measured:

- Before and after the deduction of any fees due to the investment managers; and
- After transaction costs have been deducted (but before custodian costs are deducted).

Investment managers are evaluated after taking into account their investment management fees and the degree of risk incurred to achieve expected return targets. Investment managers are also compared to other managers in the same asset class or strategy.

7 STANDARDS FOR REPORTING

Required under section 15M (c) - standards for reporting the investment performance of the Fund.

7.1 Policies

A comprehensive and timely reporting framework enables the Board to analyse the performance of the Fund, asset classes and investment managers.

7.2 Standards

(a) **Reporting by the custodian to the Board**

For the Fund's investments as a whole and for each investment manager, the custodian provides the reports required by the Authority to enable monitoring and review of the Fund and managers' performance. Those reports include:

- the overdraft position of each portfolio;
- accounting matters including portfolio valuation;
- reconciliation of portfolio values and cash flows with the investment managers;
- investment performance measurement and comparisons with benchmarks;
- taxation matters; and
- reports of compliance with mandate specific restrictions on separately managed portfolios.

(b) **Reporting by investment managers**

Reports from investment managers each month may cover (where applicable):

- details of securities held;
- a review of the performance and an analysis of performance factors;
- investment philosophy and strategy;
- certification that the terms of the investment contract have been met including certification that the portfolio has not been leveraged;
- reconciliation of portfolio accounts with the custodian;
- a statement of any voting rights issues;
- annual external audit report; and
- compliance with responsible investment policies.

The Board reviews the managers' investment performance quarterly and investment managers are required to meet with Management, on behalf of the Authority, on at least an annual basis.

(c) **Reporting by Management to the Board**

Management reports investment performance quarterly to the Board including aggregate returns and returns analysed by asset class and by manager. In each case actual returns are compared to benchmarks, expected risk measures, any active return targets and, in appropriate cases, peer returns. Summary reports are provided monthly of aggregate and asset class returns. Management also reports on responsible investment developments.

Management liaises regularly with the Treasury which represents the Minster of Finance.

(d) **Public Reporting**

The Fund's investment performance is reported quarterly on the Authority's website *www.gsfa.govt.nz* and published each year in the Fund's Annual Report, which is tabled in the House of Representatives. Forecasts for investment performance are published each year in the Authority's Statement of Intent.

The Treasury also reports to the Minister quarterly, following consultation with the Authority, on the Fund's investment performance and on key operational issues.

7.3 Procedures

The investment management agreements contain reporting provisions to enable the Board to determine a manager's compliance with the agreement and mandate, and success in meeting investment targets set for the manager. Similarly, the reporting functions provided by the custodian, including standards for timeliness, are described in the custodian contract.

8 RESPONSIBLE INVESTMENT

Required under section 15M (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 15M (i) – the retention, exercise or delegation of voting rights acquired through investments.

8.1 Responsible Investment Policies, Standards and Procedures

The Authority has developed Responsible Investment Policies, Standards and Procedures (**RI Policies**) for:

(a) ethical investment, including avoiding prejudice to New Zealand's reputation as a responsible member of the world community;

(b) environmental, social, and governance considerations; and

(c) the retention, exercise, or delegation of voting rights acquired through investments.

The Authority may take other factors into account in its investment processes, provided they do not conflict with its responsibilities under the GSF Act and can be implemented in a practicable and cost effective way. The Authority takes a broad range of other factors into account in its investment processes including:

- information or advice that a corporate entity or country, on the basis of credible evidence from publicly available sources, has participated in serious infringements of relevant international standards relating to human rights, labour and employment, the environment or international security and disarmament;
- any action by the corporate entity or country which is of such a nature that the Board considers that ongoing investment may give rise to a risk of prejudice to New Zealand's reputation as a responsible member of the world community; and
- information and advice obtained by the Authority that the entity is subject to economic or other sanctions that New Zealand applies.

The Authority's RI Policies are regularly reviewed by the Board.

8.2 Procedures

The Board is accountable for, and maintains oversight of, the Authority's RI Policies. The Board has established the Responsible Investing Committee to oversee the development of the RI Policies, monitor their implementation, and make recommendations to the Board, as required.

The Authority has signed a collaborative agreement with the Guardians of New Zealand Superannuation (**GNZS**), the Accident Compensation Commission and the Earthquake Commission as all parties have similar RI obligations and all are signatories to the United Nations Principles for Responsible Investment. The purpose of the agreement is to minimise costs and duplication of research effort for all parties.

The Board has delegated the implementation of the RI Policies to the General Manager - Investments, the Chief Executive and the Board's Responsible Investing Committee depending on the level of action required.

A copy of the Authority's **RI Policies** and the delegated authorities for their implementation can be found on the website *www.gsfa.govt.nz*

9 RISK MANAGEMENT

Required under section 15M (h) – The management of credit, liquidity, operational, currency, market, and other financial risk.

9.1 Policies

The Authority has developed comprehensive risk management policies for the management of various investment, operational and financial risks. The Audit and Risk Review Committee assists the Board in fulfilling its responsibilities with respect to internal controls, accounting policies, financial statements approval and risk management. Risk management is further supported by the Corporate Governance Statement, acceptable conduct policies for Board members and Management, Board expenditure policies and procedures, defined roles and responsibilities, performance accountability processes and timely disclosure and communication.

The level of investment risk in the Fund is defined by the Risk Parameter and the Authority's risk management procedures described in section 9.3. A description of the major risk categories are set out below.

9.2 Standards

(a) **Market risk**

Market risk is the risk of adverse movements in investment markets (including asset prices, volatility, changes in the yield curve or other market related variables) that affect the value or income of the portfolio. Market risk is outside the control of the Authority. The volatility of investment markets means that the return from the Fund is inherently uncertain. Actual returns from each asset class may vary significantly each year from the mean returns assumed in determining the investment strategy appropriate to the long term.

Major structural changes to investment markets and/or taxation environment are not within the control of the Authority. However, the Authority takes into account changes in these risks in its reviews of the SAA and investment strategy.

(b) **Borrowing or leverage risk**

The Fund is not permitted to borrow money or charge any of the property of the Fund, directly or through financial instruments, without the Minister of Finance's consent. The Authority has sought and obtained the Minister's consent to enter into financial instruments, where the use of those is consistent with the Authority's SIPSP. The Authority has also obtained the Minister's consent to enter into temporary overdrafts with its banks.

Collective investment vehicles

The Fund may own equity securities or invest in collective investment vehicles that borrow or grant charges on their own assets provided that owning these equity securities does not cause undue risk to the Fund as a whole, as expressed in the Risk Parameter. Particular investments or strategies within collective investment vehicles may be leveraged or include leverage or be invested "short". (Short positions arise when securities are sold while not yet owned, in anticipation of being bought after the price falls. Short positions may be created physically by borrowing the securities and selling them or through derivative contracts.)

Derivatives held directly by the Fund

To avoid undue risk to the Fund as a whole, derivative positions held directly by the Fund are required to be collateralised. In general this means the Fund must hold sufficient cash or securities corresponding to the derivatives to be able to meet any obligations arising from closing out the derivative transaction at current market prices.

(c) **Manager risk**

The Authority retains professional managers to implement its investment strategy and, in many cases, deliver superior returns through skilled active management. Managers' returns may vary from expected levels.

(d) **Credit risk**

Credit (or counterparty risk) is the risk of default by a counterparty to a particular transaction or an issuer of a security held in the portfolio.

(e) **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.

(f) **Operational risk**

Operational risk is the risk of financial loss due to mismanagement, error, fraud or unauthorised transactions.

(g) **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.

9.3 Procedures

(a) **Market risk** is managed by:

- specifying the total risk budget of the Fund and its various major exposures consistent with the Risk Parameter and best practice assumptions in relation to exposure risks and correlations among them;
- diversifying the asset classes in which the Fund invests by adopting the SAA described in section 5 and a range of investment management techniques for the Fund;
- seeking professional advice on the investment strategy and SAA;
- carrying out peer reviews of advice, and consulting with other Crown Financial Institutions and large investment funds;
- requiring investment managers to manage their portfolios within defined market exposure limits for each asset class held; and
- setting limits to which managers are required contractually to manage their portfolios which may include:
  - limits on the expected volatility of their total portfolio or their portfolio relative to the benchmark;
  - limits on exposure to any single issuer of securities;
  - limits on particular exposures in the manager's benchmark; and exposures not represented in the benchmark.

(b) **Borrowing or leverage risk** is managed by:

- requiring any derivative transactions held directly by the Fund to be adequately collateralised with cash or corresponding securities, valued at current market prices;

- entering into commercial arrangements for any charges against the Fund in accordance with industry best practice, such as the use of agreed counterparty settlement limits and temporary overdrafts for forward currency contracts, swaps and other contracts for difference;
- requiring settlement of amounts outstanding from any deriva-tive transactions due to short term price fluctuations that exceed levels agreed in advance with counterparties;
- the Authority satisfying itself that potential managers (including managers of collective investment vehicles) have adequate policies and procedures relating to derivative counterparties and, if selected, monitoring that managers adhere to their policies; and
- using appropriate industry standard documentation.

(c) **Manager risk** is managed by:

- robust selection process for investment managers based on demonstrated ability and independent expert opinion;
- diversification among managers;
- setting mandates for active managers based on best practice portfolio management that prescribe acceptable risk limits;
- regular assessment and review of manager performance against the benchmark and peers; and
- putting in place management agreements or other satisfactory contractual terms that separate Fund assets from managers and protect against manager errors, omissions and wrongful actions.

(d) **Credit risk** is managed by requiring that managers of the Fund's credit investments:

- maintain the credit quality of their portfolios within agreed contractual guidelines and specified according to approved independent credit ratings;
- limit exposure to individual issuers to prescribed limits; and
- maintain appropriate policies and procedures relating to derivative counterparty selection and management and appropriate industry standard documentation.

(e) **Liquidity risk** is controlled by implementing the Fund's SAA and rebalancing procedures described in section 4. In addition, liquidity risk is managed by:

- requiring, except as specifically authorised by the Board, managers to invest only in securities listed on recognised exchanges;
- limiting investment in securities that are not traded on recognised markets as authorised by the Board;
- requiring managers, within the terms of their individual investment management agreements, to hold diversified portfolios; and
- limiting the credit rating of the fixed interest and cash investments to approved levels.

(f) **Operational risk** is managed by:

- engaging an independent global custodian to record transactions, report on performance and monitor compliance of investment managers with mandates;
- having in place a specific mandate for each investment manager, based on best practice portfolio management;
- clear separation of functions between investment management, custody, and overall supervision;

- ensuring the Management team has sufficient resources to conduct the oversight function as part of its overall responsibilities; and
- requiring investment managers and the custodian to:
  - provide the Authority with third party covenants or assurances against operational risk events
  - have in place insurance arrangements to cover claims in those events
  - have in place and regularly confirm the existence and efficiency of internal policies and controls to address those risks
  - provide compliance reporting, and
  - reconcile the Fund's recorded positions regularly.

(g) **Currency risk** is managed by:

- maintaining a foreign currency hedging policy for the Fund and individual asset classes;
- engaging currency managers to manage the various hedging programmes;
- specifying the bounds within which investment managers may take on currency exposures relative to their benchmark; and
- specifying the instruments that managers may use and the credit worthiness of the counterparties in the investment management agreement with each manager.

10 THE USE OF DERIVATIVES

Required under section 15M (g) – The use of options, futures and other derivative financial Instruments.

10.1 Introduction

Derivatives are financial instruments whose value and characteristics are derived from underlying assets, indices or reference rates. Derivatives cover a broad range of financial instruments and include futures contracts, forward currency contracts, swaps, forward interest rate contracts, options and credit default swaps.

There is a variety of purposes for which it may be appropriate for the Fund to use derivatives. These include risk management, value adding investment strategies and transactional efficiency.

Derivatives provide another means for an investment manager to obtain market exposures and can be more liquid than the assets from which their value is derived.

10.2 Policies

Derivatives may be entered into by the Authority or its managers and custodians on behalf of the Fund. Their use must be entered into as specified in each investment management agreement, or where consistent with the terms governing collective investment vehicles.

Section 15C of the Act requires the consent of the Minister of Finance to enter into derivative transactions. Accordingly the Authority has sought and obtained the Minister's approval to use derivatives subject to certain conditions.

The use of derivatives is permitted only where it results in market exposures appropriate to the Fund as a whole; the resulting counterparty exposures are adequately controlled and the Fund can meet any liquidity requirements arising from their use.

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.

10.3 Standards

Derivative instruments may be traded on recognised exchanges or issued by a counterparty over-the-counter. Each such counterparty must meet the Fund's general requirements in terms of credit rating and contractual arrangements.

The net exposure to foreign currencies (after taking into account hedging positions) in the relevant portfolios is to be in accordance with the Authority's hedging policy for the asset class. If required, appropriate parameters for hedging using proxy currency will be established with the currency managers as well as appropriate operational ranges.

The effective exposures to underlying securities or assets arising from any derivatives are taken into account for the purposes of determining compliance with the prescribed exposure limits of portfolios.

10.4 Procedures

All investment managers are required to provide the Authority with a copy of their policies relating to derivative securities trading and counterparty risk and to manage their derivative exposures in accordance with those policies. The Authority recognises that, where it invests in collective investment vehicles offered by investment managers, those vehicles may be investing in derivatives and takes that into account in determining the appropriate level of investment for the Fund.

The risk of derivatives is measured by their effective exposure to underlying assets as well as on a stand alone basis. The value of derivatives is measured according to generally accepted industry best practice.

Over-the-counter foreign exchange hedging derivative 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 and domiciled in New Zealand, or in countries with which New Zealand has a double tax treaty.

The currency exposure associated with international investing will be managed using forward foreign exchange contracts relating to the currencies in which the securities that comprise the portfolio are denominated, or their close proxies.

Derivative policies and practices, including foreign exchange hedging are in accordance with any selected manager's derivatives policies, set out in their offer documents, or as otherwise specified in an investment management agreement. Selected managers are required to maintain policies and procedures relating to derivative counterparty selection and management accordingly and use appropriate industry standard documentation.

11 INVESTMENT CONSTRAINTS

Required under section 15M (k) – Prohibited or restricted investments or any investment constraints or limits.

11.1 Policies

Prohibitions and constraints imposed by the Authority can be categorised as follows:

(a) asset classes or strategies which do not form part of the asset allocation;

(b) investments excluded under the Authority's RI Policies;

(c) investments outside the permitted investments of any investment mandate, or not included in the offer document of a collective investment; and

(d) exposures outside the rebalancing range for each investment class (to ensure the investment objective of the Fund is not compromised by excessive deviation from the Fund's SAA).

In addition, 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 GSF Act.

11.2 Standards

The Authority has developed constraints and limits in respect of each asset class or strategy to control risks. Each investment management agreement specifies those investments that constitute authorised investments and managers may not invest other than in those permitted investments.

Limits on the maximum holding that can be held in each issuer address section 15K of the GSF Act and rebalancing ranges for each asset class or strategy are recorded in Section 5.2

11.3 Procedures

Specific written authorisation from the Authority 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.

Procedures for rebalancing are set out in section Table 1, page 89.

12 VALUATION

Required under section 15M (j) – The method of, and basis for, valuation of investments that are not regularly traded at a public exchange.

12.1 Policies

Many of the investments of the Fund are securities regularly traded on recognised exchanges and are valued independently and reported publicly. These investments are valued at current market value by the independent custodian in accordance with accepted industry best practice.

Where investments are not traded on recognised exchanges but can be independently priced by the custodian, the Authority, in conjunction with the custodian, determines fair valuation on these investments through an objective or independent process where possible. Examples of investments that are not traded on recognised exchanges but that can be independently priced are: some collective investment vehicles, some non-sovereign bonds and over-the-counter derivative transactions.

Where a valuation discrepancy arises between an investment manager and the custodian, the Authority generally accepts the custodian's valuation.

For private market investments, that are not able to be independently priced by the custodian, the Authority relies on the valuation undertaken by the investment manager. In these cases the valuation is required to have been undertaken by a reputable, suitably qualified professional valuer who is independent of the investment manager.

12.2 Standards

In the case of listed assets, fair value is determined by reference to prices traded on recognised exchanges. For unlisted securities, where quoted market prices are not available, fair value will be determined on the basis of independent valuation. Investments in collective investment vehicles will be subject to external valuation processes and valued according to accepted market practice. In the case of over-the-counter derivatives, the mark-to-market method for determining the value is independently verified.

12.3 Procedures

Wherever possible, independent pricing measured at subsequent reporting dates will form the basis of the Board's fair value estimate, using the Standards in 12.2. In cases where an independent valuation is unable to be obtained, the Authority uses the closing price released by the relevant investment manager. Investments in collective investment vehicles, where underlying assets are not publicly traded, are subject to the Board being satisfied that there are adequate and timely independent valuations and audit procedures to validate underlying valuations.

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