B.20 SOI (2007)

GOVERNMENT
SUPERANNUATION FUND
AUTHORITY

GSFA

Statement of Intent

for the year commencing 1 July 2007

Introduction

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

The Authority's mandate is set out in the Act and the Crown Entities Act.

The Crown Entities Act requires the Authority to prepare a Statement of Intent (**SOI**) each year. In addition, Section 15N of the Act requires the Authority to include in its SOI specific comments on the expected performance of the Fund over the next financial year, as well as the risks to that performance and steps being taken to manage those risks.

The Authority's SOI for the year commencing 1 July 2007, is prepared pursuant to Part 4 of the Crown Entities Act.

Basil Logan, Chairman

David May, Deputy Chairman
19 June 2007

From the Chairman

On behalf of the Government Superannuation Fund Authority Board (**the Board**), I am pleased to present the Statement of Intent (**SOI**) of the Authority for the year commencing 1 July 2007.

The Authority's mission is to use best practice to manage the Fund and administer the GSF Schemes with the prime objectives of enabling -

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

The Authority seeks to achieve its mission through:

- having an Investment Strategy for the Fund that will deliver returns significantly in excess of the after tax returns from New Zealand Government stock; and
- ensuring sustainable, cost effective management of the GSF Schemes to enable accurate assessment, payment and reporting of members' entitlements.

From the establishment of the Authority in 2001 to the end of April 2007, the Investment Strategy has delivered an after tax return of 6.51% per annum, a margin of 2.61% over New Zealand Government stock (after tax). This return is above the Investment Performance Measure.

A key challenge for the Authority, in preparing for the three years ahead has been to assess the impact of the new taxation environment for investment income and develop an appropriate response. Last year I advised readers that the Investment Performance Measure set for the Fund would no longer be achievable due to proposed legislative changes that would have increased the tax payable by the Fund on investing activities. Now that the new tax environment has been confirmed, the Authority has responded by revising its Investment Strategy and accepting a higher risk profile to enable the current Investment Performance Measure to be maintained. We believe that the revised Investment Strategy is appropriate for the Fund in the current circumstances and will meet our mission. Implementation of the revised Investment Strategy will be a major focus for the year ahead.

The statutory five yearly independent review, of how effectively and efficiently the Authority is performing its functions under the Act, was completed in August 2006. The reviewer summarised its overall findings in the comment. "Our opinion is that GSFA (the Authority) is operating under best practice governance taking into account the nature of the Authority". The Authority has fully evaluated the findings of the review and a number of recommendations have been adopted. These include a review of the custodial management of the Fund's assets and incorporating a health check into the annual review of the Statement of Investment, Policies, Standards and Procedures.

The Authority has become a signatory to the United Nations Principles for Responsible Investment (UNPRI). These aspirational principles will form the framework for integrating governance, social and environmental issues into our investment process, where this is supported by a robust investment case.

Key tasks for the Authority over the three years, that will contribute towards our mission and objectives, include:

- implementing the revised Investment Strategy approved in May 2007, that takes account of the impact of a new taxation environment, and regularly reviewing this strategy;
- continuing to investigate alternative asset classes and active management strategies that, when combined with existing asset classes and strategies, contribute towards increasing returns or reducing risk for the Fund;
- reviewing the custodial management of the Fund's assets to ensure the arrangements reflect best practice and are value for money;
- ensuring investment managers' ongoing competency through robust selection, monitoring and assessment;
- developing strategies that will contribute to meeting the aspirational principles of the UNPRI in a cost effective way where supported by a robust investment case;
- reviewing the Authority's active (and directly held) investments against the Board's Policies, Standards and Procedures for avoiding prejudice to New Zealand's reputation as a responsible member of the world community;
- fully scoping the operations and functions of the GSF Business System, used for administering the GSF Schemes, as the first step in determining the specification for a new and more sustainable administration system;
- reviewing and monitoring the administration of the GSF Schemes by the schemes administrator to ensure contributions are collected, and entitlements are paid accurately in a cost effective and timely manner, and service levels are met;
- implementing the New Zealand equivalents to the International Financial Reporting Standards (NZ IFRS).

For readers who are interested to learn about the Authority, its policies and operations, we invite you to visit our website at www.gsfa.govt.nz.

Basil Logan.

Basil Logan, **Chairman**

The Authority's Operating Environment

(required under section 141 (1)(a) of the Crown Entities Act)

This section provides an overview of the Authority and describes the Fund and the GSF Schemes.

The Fund and the GSF Schemes

The Fund and the GSF Schemes were established in 1948 to provide a way for public sector employees to save for their retirement.

The GSF Schemes were closed to new members from 1 July 1992, except for people who were eligible for membership through their employment with certain Pacific Island governments. Membership was closed to these people in 1995.

There are seven GSF Schemes:

- General
- Armed Forces
- Police
- Prison Officers
- Members of Parliament
- Masters
- Judges and Solicitor General

Each of the GSF Schemes is registered as a superannuation scheme under the Superannuation Schemes Act 1989.

Currently the GSF Schemes have some 70,000 members, made up of nearly 22,000 contributors and more than 48,000 annuitants. It is expected that entitlements will continue to be paid by the Fund for the next 60 years.

Contributors contribute a defined percentage of their salaries to the Fund on a regular basis. In return, they receive a retiring allowance based on average superable salary for the last five years of contributory service, years of service and age at retirement.

Certain non-Crown employers contribute the balance of the accruing cost of their employees' retirement entitlements to the Fund.

The Crown, as an employer, meets its share of its employees' retirement entitlements as they fall due for payment. Thus, the GSF Schemes are only partially funded, with the accumulated employee contributions, investment returns and employer contributions (from non-Crown employers) being deemed by the Government Actuary to be sufficient to meet 25% of the entitlements at present (26% from 1 July 2007).

The actual and projected present values of the Unfunded Past Service Liabilities of the Fund have been calculated by the Government Actuary in his actuarial valuation dated 8 May 2007. The results are set out in the table below. The Unfunded Past Service Liabilities are estimates of the Crown contributions required to meet the Past Service Liabilities of the Fund.

TABLE 1: PROJECTED UNFUNDED PAST SERVICE LIABILITIES

	Actual 30-Jun-06 $ million	Projected 30-Jun-07 $ million	Projected 30-Jun-08 $ million
Past Service Liabilities	12,098	12,137	12,148
Net Assets	3,799	3,889	3,975
Unfunded Past Service Liabilities	8,299	8,248	8,173

The Unfunded Past Service Liabilities are recorded in the Crown's financial statements.

The Authority

The Authority was established in 2001 to manage and administer the assets of the Fund and the GSF Schemes in accordance with the Act. The Authority became an autonomous Crown entity under the Crown Entities Act 2004.

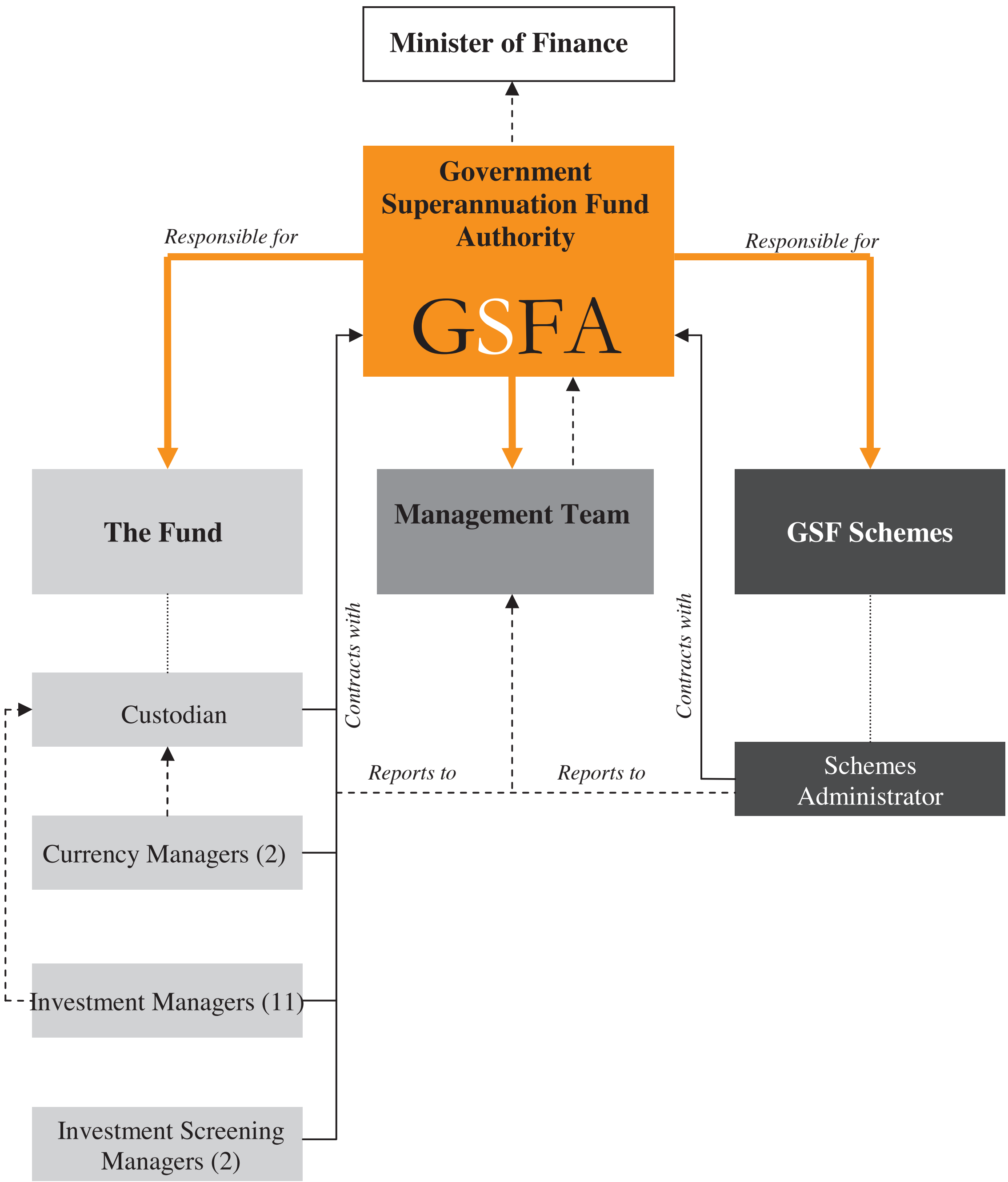
The Authority’s mandate is set out in the Act and the Crown Entities Act. The functions of the Authority are to manage and administer the assets of the Fund and the GSF Schemes in accordance with the Act. A Board, established by the Act, is the governing body of the Authority and determines the business of the Authority, either directly or by delegation.

Before the Authority was established in 2001, the Fund was invested entirely in New Zealand fixed interest securities and investment performance was measured against the NZX New Zealand Government Stock Gross Index. This investment strategy kept risk to a minimum, but it resulted in lower returns over the long term than if the Fund had been invested in a diverse portfolio. This also meant that the Crown needed to make greater contributions to the entitlements payable by the GSF Schemes. While the investment earnings of the Fund have no influence on GSF Scheme member entitlements, they influence the amount of the Crown’s contribution.

To help minimise the Crown’s contribution to GSF (and ultimately contribute to improving the Crown’s overall economic position), the Authority developed a new Investment Strategy, based on investing the assets of the Fund in a diverse portfolio of investment assets and investment management techniques.

The Authority has adopted an outsourcing model for the key activities of schemes administration and investment management (including custody of the Fund's assets). The organisational structure is set out in Diagram 1. Further information on organisational structure is set out on page 20.

DIAGRAM 1: STRUCTURE OF THE GOVERNMENT SUPERANNUATION FUND AUTHORITY AND ITS OPERATIONS



Nature and Scope of Functions

(required under section 141(1)(b) of the Crown Entities Act)

The Authority's functions, as set out in Section 15D of the Act, are to manage and administer the assets of the Fund and the GSF Schemes, in accordance with the Act. All decisions relating to the business of the Authority are made under the authority of the Board, in accordance with Section 25 of the Crown Entities Act.

The Minister of Finance has the power to add to the Authority's functions and may direct the Authority to have regard to Government policy relating to its objectives and activities. The Minister may also direct the Authority in investing the Fund to meet the Government's expectations as to the Fund's performance, including the Government's expectations as to risk and return, or not to invest in a specified investment or class of investments to which the Crown already has a direct or indirect exposure, for the purpose of limiting that exposure. No directions have been received from the Minister in terms of these powers.

The key activities of the Authority fall into the following two broad categories:

Investment

- management of the GSF assets (the Fund).

GSF Schemes

- management and administration of the GSF Schemes, including the agreement between the Authority and the schemes administrator; and
- interpretation of the provisions in the Act and exercising discretionary powers (set out in the Act).

Detail on the performance expectations against these activities can be found on pages 14-18.

Investment Management

The Act states that all property comprising the Fund must be held for the purpose of paying the entitlements, that are payable under the Act, and for the purpose of carrying out the Authority's functions. Section 15J(2) of the Act sets out the Authority's responsibilities with respect to investment of the Fund. Specifically, the Act requires that the Authority must:

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

Under the Act, "invest" means -

> *"… to carry on any activity, do any act, or enter into any transaction that the Authority considers to be for the purpose, directly or indirectly, of -*
>
> *(a) enhancing or protecting the value of the Fund;*
>
> *(b) managing, or enabling the management of, the Fund."*

The Act also requires, in section 15L, 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*."

In line with these requirements the Authority prepared a Statement of Investment Policies, Standards and Procedures (**SIPSP**) in 2002. The most recent annual review of the SIPSP was completed in June 2007. The current version of the SIPSP is included on the Authority's website, www.gsfa.govt.nz.

GSF Schemes

The Authority is responsible for managing and administering the GSF Schemes in accordance with the Act. Schemes administration is outsourced to Datacom Employer Services Limited (**Datacom**).

The Act sets out the basis for calculation of entitlements, payable to the members of the GSF Schemes, and specifies a number of procedural matters. In terms of Section 19 of the Act the Authority must, when exercising its discretionary powers in relation to the GSF Schemes, act in accordance with the GSF Statement of Provisions, Policies and Procedures (**the Policies**). The Policies are published on the Authority's website, www.gsfa.govt.nz.

If there is any doubt about any matter (for example the amount of any entitlement, how an entitlement has been calculated, length of service etc) the Authority can be approached to give a determination.

If the person concerned disagrees with or is dissatisfied with the Authority's decision or determination, the person can appeal to the Appeals Board. The Appeals Board is an independent body whose members are appointed by the Minister of Finance.

Booklets published by the Authority, providing information on the GSF Schemes, are made available to members on request by Datacom, or can be downloaded by members from the Authority's website, www.gsfa.govt.nz. The booklets are reviewed and updated on a regular basis.

Objectives and Strategies and Performance Measures

Efficient management of the assets and liabilities of the GSF contributes to an improvement in the Crown's overall economic position.

The Authority contributes by:

- having an Investment Strategy that will deliver returns significantly in excess of the after tax returns from New Zealand Government stock; and
- ensuring sustainable, cost-effective management of the GSF Schemes to enable accurate assessment, payment and reporting of members' entitlements;

within a best practice framework.

Investment Management

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 to the Fund, within a best practice framework.

Investment Performance Measure

The performance of the Fund will be assessed by comparing its 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

Risk tolerance for the Fund is expressed as a probability of loss, relative to the size of the Fund's assets. The revised Risk Parameter, adopted in May 2007, 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. (See section below, titled "Revision of the Investment Strategy" for an explanation).

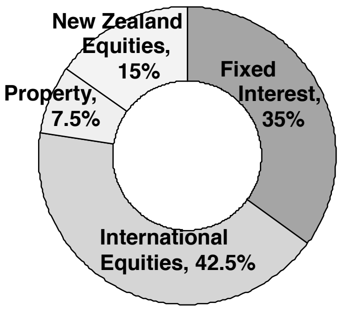
Important decisions for the Board are to determine the Fund's Investment Performance Measure and Risk Parameter. In seeking to maximise return for the Fund over the longer term, the Authority accepts a specified level of investment risk in exchange for a reasonable expectation of excess returns over the returns from Government Stock. Having determined the tolerance for risk, an Investment Strategy is put in place which best meets these parameters.

Investment Strategy

The Authority's Investment Strategy is to develop, implement and maintain a diversified, efficient and well managed investment portfolio that will meet the Investment Objective. The Investment Strategy is implemented by developing an asset allocation (**the Strategic Asset Allocation or SAA**) that is expected to meet the Authority's Investment Objective and Risk Parameter.

The existing SAA and the target SAA (approved in May 2007) are illustrated below.

EXISTING STRATEGIC ASSET ALLOCATION AT MARCH 2007



TARGET STRATEGIC ASSET ALLOCATION APPROVED MAY 2007

Note 1: The target strategic asset allocation to New Zealand equities may include an allocation to Australian equities to take advantage of the new tax regime.

Note 2: 15% of the Fund is to be invested in alternative assets. Of that allocation 3% has been invested in collateralised commodity futures funded from the fixed interest allocation. The allocation of the remaining 12% and its funding source has yet to be determined.

To provide a robust conceptual foundation for its Investment Strategy and to communicate shared values about investment, the Authority has agreed a set of Investment Beliefs, summarised below:

- higher returns are associated with higher risks;
- setting the SAA is the most important investment decision;
- diversification reduces risk;
- market timing is not a reliable source of return because of the short-term unpredictability of returns;
- nevertheless, account should be taken of unusual asset price behaviour;
- control of costs is important; and
- markets vary in their efficiency, and market inefficiencies offer skilful managers the opportunity to add value.

The Investment Strategy is regularly reviewed and changes are made as appropriate. This involves:

- ensuring the key investment and taxation assumptions used in developing the SAA, the Investment Performance Measure and the Risk Parameter remain reasonable and appropriate and that the Investment Strategy continues to meet the requirements of the Act and is consistent with the Authority's Investment Beliefs. Independent advice may be obtained; and
- regularly reviewing investment markets to determine whether asset classes should be added to or deleted from the SAA and whether the composition and style of management of asset class within the SAA should be changed.

Revision of Investment Strategy

The SOI for the year commencing 1 July 2006 noted that the proposed changes to the taxation of investment income (now enacted under the Taxation (Savings Investment and Miscellaneous Provisions) Act 2006) would mean the existing Investment Performance Measure, being

> *the NZX New Zealand Government Stock Index return (after tax), plus 2.5% per annum, measured over rolling 10 year periods*

would be unattainable without increasing the Risk Parameter set by the Authority of

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

The Board considered a number of possible responses to this issue, including accepting more risk to achieve the existing Investment Performance Measure or lowering the Investment Performance Measure in order to maintain the current Risk Parameter.

Now that the new tax environment has been confirmed, the Board has responded by revising its Investment Strategy and accepting a higher risk profile to enable the existing Investment Performance Measure to be maintained. The Board has determined to adopt a target SAA with an allocation of 72.5% to equities and property and 27.5% to fixed interest. The existing SAA had an allocation of 65% to equities and property and 35% to fixed interest.

The effects of this decision are:

1. The Investment Performance Measure remains unchanged;
2. The Risk Parameter is now expressed as

   having no more than a 1 in 10 chance in any one year of a loss after-tax greater than 6% of the total Fund.

The Board believes the new Investment Strategy is appropriate for the Fund in the current circumstances and will meet our mission. Implementation of the revised Investment Strategy will be a major focus for the year ahead.

Best practice portfolio management and avoiding prejudice to New Zealand's reputation as a responsible member of the world community

A key measure of the Authority's success will be the Fund's financial performance over the long term. Non-financial aspects of the Authority relate to best practice portfolio management and the requirement to manage and administer the Fund in a manner consistent with avoiding prejudice to New Zealand's reputation as a responsible member of the world community.

The Authority's mission is to use best practice to manage the Fund and administer the Schemes. The Authority seeks to meet the following standards:

- implement the Investment Strategy efficiently;
- maintain a governance model that reflects clear responsibilities and promotes accountability;
- be transparent in reporting and communicate effectively with the Fund's stakeholders; and
- access advice, experience and guidance from a wide group of the superannuation and investment sectors.

The Authority has become a signatory to the United Nations Principles for Responsible Investment (**UNPRI**). Where consistent with each signatory's fiduciary duties, signatories seek to address the six aspirational principles:

1 *We will incorporate environmental, social and governance issues into investment analysis and decision-making processes.*
2 *We will be active owners and incorporate environmental, social and governance issues into our ownership policies and practices.*
3 *We will seek appropriate disclosure on environmental, social and governance issues by the entities in which we invest.*
4 *We will promote acceptance and implementation of the UNPRI within the investment industry.*
5 *We will work together to enhance our effectiveness in implementing the UNPRI.*
6 *We will each report on our activities and progress towards implementing the UNPRI.*

Signatories to the UNPRI accept that they have a duty to act in the best long term interests of their funds and that environmental, social and governance issues can affect the performance of investment portfolios (to varying degrees across companies, sectors, regions, asset classes and through time).

These aspirational principles will form the framework for integrating governance, social and environmental issues into the Authority's investment process where this is supported by a robust investment case.

GSF Schemes

Objective

Ensure sustainable, cost effective management of the GSF Schemes to enable accurate assessment, payment and reporting of members' entitlements.

Strategy

The Authority's strategy with respect to the GSF Schemes is to ensure contributions are collected, entitlements are paid accurately and in a cost effective and timely manner, and service levels are met.

The sustainability of the GSF Business System, used for administration of the GSF Schemes, is fundamental to achievement of this strategy. While the current GSF Business System is stable, and the Authority is confident it will perform adequately for at least the next five years, investigations are being undertaken into viable alternatives for the future. During 2007/2008 the Authority will be fully scoping the operations and functions of the GSF Business System as the first step in determining the specification for a new administration system.

Also key is the role of the schemes administrator, Datacom. The Authority has established and maintains a partnering relationship style with Datacom to ensure all issues relating to the administration of the GSF Schemes are communicated early to the Authority and are managed and resolved in an open manner, taking into account the interests of the members and the Crown.

In communicating with members, the Authority seeks to ensure information provided is both of a high standard and timely. This includes information on member entitlements and on the activities of the Authority.

The Authority interprets the provisions of the Act and the Policies, and exercises its discretionary powers, in relation to matters raised by members. The Authority seeks to achieve equity and consistency in its application of the provisions of the Act and the Policies.

Forecast Service Performance for 2007/2008

(required under section 142(1)(b) of the Crown Entities Act)

Investment Management

A key measure of the Authority's success in managing the GSF assets is the Fund's financial performance over the long term. The Fund is expected to exist for at least 60 years and, for this reason, the Authority's Investment Strategy is based on maximising returns, without undue risk, over the long term.

The performance of the Fund will be assessed by comparing its 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 (Investment Performance Measure).

Investment Performance Expectations for 2007/2008

(required under section 15N of the Act)

Section 15N of the Act requires the Board to set out its expectations for the performance of the Fund over the 2007/2008 financial year in sufficient detail to enable meaningful assessment against those expectations at the end of the financial year. Greater volatility and uncertainty exists about returns over 1 year than 10 year periods. As a result, returns in any particular year are not necessarily indicative of the long term investment performance of the Fund.

The Authority is forecasting a surplus after tax and before membership activities of $270 million for the Fund for the 2007/2008 year. This represents a forecast return of 6.5% after tax (equivalent to the assumed return on the New Zealand Government Stock Gross Index (after tax) of 4.0% for the same period, plus 2.5%) and meets the Investment Performance Measure for the Fund.

From the establishment of the Authority in 2001 to 30 April 2007, the Fund has delivered an after tax return of 6.51% per annum, a margin of 2.61% over New Zealand Government stock (after tax). This represents 0.11% above the Authority's Investment Performance Measure.

Significant Assumptions used in the Forecast of the Fund

(required under section 142(1)(d) of the Crown Entities Act)

The volatility of investment markets means that the forecast increase in assets from investing activities, included in the Forecast Income Statement, is inherently uncertain over short term periods. The forecast increase in assets from investing activities is dependent on assumptions with respect to returns from each asset class, the effect of any changes to the SAA of the Fund and the impact of taxation changes. Actual returns from each asset class in the year may vary significantly from the long term return assumptions. Other, specific assumptions are listed below:

- the expected after tax investment returns for major asset classes are as follows:

	1 JULY 2007 – 30 SEPTEMBER 2007	FROM 1 OCTOBER 2007
International Equities	8.2%	7.2%
New Zealand Equities[1]	8.1%	8.9%
Property[2]	7.1%	7.1%
Fixed Interest	4.0%	4.0%

1. Includes selected Australian equities.
2. International Property entered the new taxation regime on 1 April 2007. As a result of a different taxation treatment, the expected return for International Property increased on 1 April from 6.2% to 7.1%.

- the expected after tax investment returns do not include any added value from active management;
- currency hedging is in place for international equities, international property and international fixed interest. No provision has been made, in the forecast financial statements, for changes in currency as currency movements cannot be predicted with accuracy in the short term;
- asset values as at 1 July 2007 are estimated using 30 April 2007 asset values and projected returns to 30 June 2007;
- taxation of gains on equities are summarised in the table below:

TABLE 2: EXPECTED AFTER TAX RETURNS TABLE AND TAX IMPACT

	Tax treatment of gains to 30/9/2007	Tax treatment of gains after 1/10/2007
International equities	0% The Fund is currently invested in passive vehicles with binding IRD rulings exempting gains from tax.	Tax on 5% of the opening value of the Fund, plus, in respect of "quick sales" during the year, taxation on the lesser of the gain on sale (including dividends) or 5% of cost.
New Zealand equities	33%	0%
Selected Australian equities	0% The Fund is currently invested in passive vehicles with binding IRD rulings exempting gains from tax.	0%

- entitlement payments out of the Fund of $12 million per month.

Other Investment Performance Measures and Standards

In addition to setting long term performance expectations, the Authority sets detailed responsibilities and projects each year. Achievement of these performance measures and standards will assist the Authority develop, implement and maintain a diversified, efficient and well managed investment portfolio that will meet the Investment Objective.

Some responsibilities and projects are perennial in nature, while others are in response to specific Investment Strategy decisions and may be completed over a period beyond 1 year.

For the 2007/2008 year the Authority has identified the following performance measures and standards:

- develop and implement a shift from passive to active management of international equities taking into account the increase in SAA, as determined by the Board in May 2007 in response to the new taxation legislation;
- continue to investigate alternative asset classes and active management strategies that, when combined with existing asset classes and strategies, improve the diversification, efficiency or management of the investment portfolio (by increasing returns or reducing risk);
- commence a review of the structure and investment arrangements for fixed interest and property to identify enhancements to diversification, efficiency or management of the Fund (through increasing returns or reducing risk).
- undertake a benchmark review of the custodial management for the Fund's assets to ensure the arrangements reflect best practice and remain competitive;
- maintain the safe custody of the Fund's assets, and monitor the custodian's performance in accordance with the requirements of the custody agreement to ensure that the quality of service and the accuracy and timeliness of reports on the Fund are maintained. Key performance standards for the custodian are set out below:
  - safekeeping and settlement of transactions and registration of assets for all GSF transactions in non-pooled investment management arrangements;
  - preparation of monthly accounting reports by the 7^{th} business day following the end of the month, in compliance with New Zealand Financial Reporting Standards;
  - preparation of investment manager reconciliation reports by 8^{th} business following the end of the month; and
  - preparation of independent investment performance reports, by 14^{th} business day following the end of the month.

- monitor investment managers' capabilities through robust, monitoring and assessment against performance requirements, as specified in investment management agreements;
- keep under review the key investment and taxation assumptions used in developing the SAA, the Investment Performance Measure and the Risk Parameter to ensure the SAA remains efficient and able to meet the Investment Objective and Investment Performance Measure.
- develop and implement 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;
- review the Authority's active (and directly held) investments against policies, standards and procedures for avoiding prejudice to New Zealand's reputation as a responsible member of the world community through regular (at least annual) screening and monitoring programmes; and
- ensure the Authority adheres to its SIPSP, and records all amendments to its policies, standards and procedures in this document. This will be achieved through continual review of investment mandates and monitoring of the Authority's practices and policies in relation to investments.

GSF Schemes

The Authority's key activities in relation to the GSF Schemes, as noted on page 8, are: the management and administration of the GSF Schemes, including the agreement between the Authority and the schemes administrator, Datacom, and interpretation of the provisions in the Act and exercising discretionary powers (set out in the Act).

Forecast measures and standards for GSF Schemes' activities for the 2007/8 year are:

- fully scope the operations and functions of the GSF Business System, used for administering the GSF Schemes, as the first step in determining the specification for a new administration system;
- provide sufficient funding to Datacom to ensure all entitlement payments are able to be made as they become due;
- respond to member correspondence, in accordance with the Act and the Policies, within five working days;
- respond to appeals by members, against decisions made by or on behalf of the Authority, in accordance with the Act. The Authority's reports to the Appeals Board will be provided at least 14 days before each scheduled hearing date;

- maintain a Business Continuity Plan (**BCP**) for schemes administration that is in accordance with best industry practice. The BCP is tested periodically and reviewed annually;
- maintain the Policies and, subject to consultation with interested parties, amend to record any policy changes made by the Authority;
- provide actuarial data on the Fund, required for the Crown financial statements, in accordance with the timetable agreed with Treasury;
- communicate annually with contributors, annuitants, and employers regarding the activities of the Authority and the performance of the Fund;
- monitor the schemes administrator's performance in accordance with the performance standards included in the schemes administration management agreement between the Authority and Datacom, including sustainability of service, service levels to contributors, annuitants, and employers and other key performance standards, within an overall framework of seeking continual improvement.

  Key performance standards have been established and are used by the Authority for monitoring and measurement of the schemes administrator's performance. The key performance standards for the schemes administrator are set out below:

  - 70% of all correspondence (except for requests for entitlement quotes, or entitlement calculations or recalculations) to be responded to within 3 working days of receipt;
  - 70% of all requests for entitlement quotes, entitlement calculations or entitlement recalculations, to be responded to within 5 working days of receipt;
  - 100% of all annuities to be paid on due date;
  - 70% of all other payments to be paid within 3 working days of receipt of all requirements;
  - all contributions to be banked on receipt, and allocated as soon as identified to the correct Scheme, to the correct employer where they are employer contributions, and to the correct member account once reconciled to contribution data;
  - all transactions to be processed correctly.

  The performance standards are reviewed from time to time to ensure they remain appropriate and relevant. In addition, an annual survey is undertaken to provide, among other things, an indication as to the level of satisfaction of members and employers with the service provided by the schemes administrator.

Organisational Health and Capability

(required under section 141(1)(e) of the Crown Entities Act)

Governance

The Board is the governing body of the Authority and is responsible for making all decisions relating to the Fund and the GSF Schemes. The Board has all the powers necessary for managing, and for directing or supervising the management of, the business of GSF.

The Minister of Finance appoints the members of the Board. The members have a wide range of experience and expertise in the investment, financial and business sectors.

The Authority has established a Corporate Governance Statement, which incorporates legislative and regulatory requirements as well as the policies and practices developed by the Board. This statement is available on the Authority's website, www.gsfa.govt.nz.

The key policies and practices developed by the Authority are set out below:

- the Authority's obligations with respect to the Fund and the GSF Schemes are supported by business planning, business risk assessment, management reporting, and arrangements for audit, internal control and compliance, all conducted on a regular basis;
- the Authority regularly reviews its own activities and the activities of Management, to ensure that clear and proper sets of accountabilities remain in effect, delegations are properly implemented and reporting is comprehensive;
- the Board reviews its own performance annually and at all times aims to achieve best-practice;
- the Board has established four committees 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. The four committees are -
  - Audit and Risk Review
  - Schemes
  - Investment
  - Responsible Investing
- Each committee reviews its performance annually and is also reviewed by the Board;
- the Board meets at least ten times per annum and ensures that it receives appropriate and reliable reporting on the Fund and the GSF

Schemes and the actions of its Management and other service providers;

- the Board regularly considers the resources required for the effective and proper management of the Fund and the administration of the GSF Schemes and acts to ensure that resources available to the Authority, both internally and externally, align with these requirements. The Board aims to use resources of appropriate quality and capacity for its needs, at a reasonable cost. The Board ensures that comprehensive service level agreements are entered into with each external service provider which specify reporting and compliance standards;
- the Board has a systematic compliance programme with its service providers and any breaches of compliance are reported to the Board;
- the Board has established a risk management programme which is implemented and reviewed quarterly by Management. The Audit and Risk Review Committee monitors matters of risk management and reports to the Board.

Organisational Structure

The Authority has adopted an outsourcing model for the key activities of schemes administration and investment management (including custody of the Fund's assets).

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 management and secretarial roles on behalf of the Authority and NPF. 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 schemes' administration arrangements. Each month the Board receives reports from Management on all decisions made and matters determined under the delegations of authority.

The joint venture with NPF is seen to be the most appropriate way of providing the management and support required by the Board. The GSF and NPF schemes are closed to new members and both organisations have adopted an outsourced model for the major activities of investment, custody and schemes administration. Annuitas allows economies of scale and higher quality resourcing than could be justified if each organisation operated on a standalone basis.

The Authority has appointed:

- Datacom Employer Services Limited as the administrator of the GSF Schemes. Datacom is responsible for the collection and processing of contributions to the Schemes, maintenance of member records, calculating, notifying, processing and paying of all entitlements under the GSF Schemes, maintaining toll-free lines and a Help-Desk to log and process all oral and written enquiries, and maintaining the financial records of the Schemes. All interpretation issues and determinations, arising under the Act, must be referred by Datacom to the Authority for a decision.
- JP Morgan Chase Bank as the global custodian for the Fund. The custodian is responsible for the safekeeping of the assets of the Fund, settling transactions, and reporting on the performance and compliance of the investment managers appointed by the Authority;
- Eleven specialist investment management organisations to undertake day-to-day investment decisions and specific buy and sell decisions, two to undertake currency hedging and two investment screening organisations, as follows:

New Zealand Equities
AllianceBernstein New Zealand Limited
Tower Asset Management Limited

New Zealand Fixed Interest and Cash
AMP Capital Investors (New Zealand) Limited

International Equities
AMP Capital Investors (New Zealand) Limited
Assure Funds Management Limited

International Fixed Interest
Pacific Investment Management Company LLC
Wellington Management Company LLP
Goldman Sachs Asset Management International Limited

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

Collateralised Commodities Futures
Goldman Sachs International

Currency Hedging
State Street Global Advisors Australia Limited
ANZ National Bank Limited

Investment Screening Organisations
Innovest Strategic Value Advisors
Sustainable Investment Research Institute Pty Ltd (SIRIS)

Organisational Development

Board members are normally appointed for two terms of three years. Wherever possible the Board, through the Chairman, will look to work with the Minister to ensure an appropriate balance of skills and experience is maintained in the membership of the Board.

The Board sets aside two days per year, one for strategic planning and the other for an investment workshop. During the strategic planning day the Board reviews its mission and objectives in the context of the investment and superannuation environment. It assesses whether its strategies remain appropriate, and the capabilities of the organisation to achieve the strategies. In particular, the Board reviews the robustness and sustainability of systems and technology and assesses whether appropriate resources and skills are in place for the Authority and Management to be best placed to achieve their accountabilities and responsibilities.

The investment workshop provides an opportunity for the Board and Management to receive presentations and discuss contemporary issues and new approaches relating to investment management, or other parts of the GSF business. Board members are also encouraged to take advantage of training and development opportunities available in superannuation and investment.

The Authority maintains close working relationships with other Crown Financial Institutions and, where appropriate, seeks to liaise on matters of mutual interest.

Management of the Fund's assets and schemes administration will continue to be outsourced to specialist organisations. The key element of an outsourcing model is to ensure each contracted manager, where appropriate, has in place a well planned and tested business continuity plan, including a disaster recovery programme (**DRP**). This is particularly important in the key areas of custody and schemes administration. The DRPs for the custodian and the schemes administrator are tested on a regular basis and reported to the Board.

As both the Authority and NPF employ an outsourced model for the major functions of administering and managing groups of large superannuation schemes the Management team is small. Senior managers are responsible for the key functions - Investment, Schemes, Finance and Chief Executive, and back-up support is maintained to reduce the key person risk. Management is responsible for the identification and implementation of appropriate strategies for the Authority to meet its obligations, under the Act, and its objectives.

Each year performance measures and standards are set for each of the key functions and senior members of Management, and progress on achieving these objectives is monitored by the Board on a regular basis.

The Annuitas Board has a key role to resolve any conflicts or priority issues that may arise between the Authority and NPF. It has not been necessary for the Annuitas Board to exercise this function as Management has been able to manage the workloads, achieve the performance objectives and meet deadlines to the satisfaction of the Authority Board and the NPF Board.

The Chief Executive is responsible for the development and training of all staff to ensure that they are best placed to achieve their accountabilities and responsibilities to the Authority. To achieve this the Chief Executive develops and implements individual training and personal development programmes for each staff member with the overall objectives of maintaining a high level of knowledge of investment and schemes issues, and of best practice in investment and superannuation.

Consultation and Reporting to the Minister

(required under section 141(1)(g) of the Crown Entities Act)

Matters Requiring Consultation with the Minister

The Authority is required to consult with the Minister on the following matters:

- the method for calculating interest on contributors' contributions, where the contributor is discharged or released from the regular forces in circumstances where no retiring allowance is payable (Section 71K(b) of the Act);
- approval of any class of transactions which involve:
  - borrowing money;
  - mortgaging or charging any of the real property of the Fund, whether present or in the future, as security; or
  - entering into a derivative transaction, or amending the terms of that transaction (where derivative transaction includes swaps, options, futures and any combination of those things); and
  - approval to operate bank accounts outside the provisions set out in Section 158 of the Crown Entities Act.

Approvals have been sought and granted for some of the matters outlined above. With regards to derivative transactions, the Minister has given approval for the Authority to enter into such transactions where the use is consistent with the Authority's SIPSP.

No approvals have been sought from the Minister with respect to Section 71K(b), or to borrow money and mortgage real property.

Reporting to the Minister

The accounts of the Authority and the Fund are maintained and reported in accordance with the Act and the Crown Entities Act. The Act requires the Authority to report to the Minister on the Fund at intervals and include any information that the Minister requires. In addition to the annual reports of the Authority and the Fund information is provided to the Minister for inclusion in the Crown's budget and economic updates. This includes the salaries of contributors and their contribution history, which is provided to the Government Actuary so that the Unfunded Past Service Liability can be calculated and reported in the Crown's financial statements.

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

Processes in Relation to Acquisitions

(required under section 141(1)(h) of the Crown Entities Act)

Section 141 of the Crown Entities Act requires the Authority to report on any processes to be followed for the purpose of Section 100 (Acquisitions of shares or interests in companies, trusts and partnerships).

The Authority believes that the intention of Section 100 is to cover situations where the Authority buys shares to facilitate an acquisition strategy. The Authority has no plans to acquire shares for this purpose.

A key element of the Authority's business is the purchase and sale of shares for investment and trading purposes. In carrying out its activities, the Authority is bound by Sections 15B and 15K of the Act.

Under Section 15B(6) of the Act, the Authority may subscribe for, acquire, or hold shares, or any other securities issued by a company, if the company provides scheme administration, investments services for any part of the Fund, or the provision of secretariat or other services to the Authority.

In terms of Section 15B(6) the Authority has formed a joint venture with NPF, Annuitas. The functions of Annuitas are described on page 20.

Section 15K of the Act requires that "the Authority must use its best endeavours to ensure that the Fund does not control any other entity or hold a percentage of the voting rights in any other entity that would require it to seek control of that entity". The requirements of this section have been met by the Authority.

Risk Management

(required under section 141(1)(i) of the Crown Entities Act)

A summary of the Board's assessment of the key risks to the business, including the key risks to the performance of the Fund, and actions being taken by the Authority to manage those risks are set out below.

Investment Risks

RISK	ACTION TO MANAGE
Investment strategy and asset allocation are inappropriate	▪ Diversify the assets and management techniques of the Fund. ▪ Seek professional advice on the Investment Strategy and Strategic Asset Allocation. ▪ Peer reviews of advice. ▪ Review annually the Statement of Investment Policies, Standards and Procedures, as required by Section 15L of the Act.
Poor performance of investment managers:	▪ Robust selection process for investment managers based on demonstrated ability. ▪ Diversification among managers. ▪ Mandates for active managers based on best practice portfolio management. ▪ Regular monitoring and review of manager performance. ▪ Management agreements, which provide for dismissal at the discretion of the Authority.
Overall investment management risk.	▪ Specific mandate for each investment manager, based on best practice portfolio management. ▪ Constraints to govern credit and liquidity risks. ▪ Use of a custodian to record transactions, report on performance and monitor compliance of investment managers with mandates. ▪ A comprehensive Statement of Investment Policies, Standards and Procedures developed and enforced by the Authority. ▪ A clear separation of functions between investment management, custody, and overall supervision.

RISK	ACTION TO MANAGE
Currency risk, for example the risk that the Fund will lose value through adverse exchange rate movements	▪ The engagement of a currency manager to hedge a specified percentage of the international equities currency exposure to the New Zealand dollar. The Board has determined to increase the hedge ratio for international equities from its current level of 104% pre tax to 120% pre tax (this equates to an after tax level of 80% due to different taxation treatments of capital gains on equities and foreign exchange hedging contracts). ▪ The engagement of a currency manager to hedge the United States dollar exposure to international fixed interest to the New Zealand dollar (the benchmark for international fixed interest being 100% hedged pre tax to the United States dollar). ▪ The engagement of a currency manager to hedge the foreign currency exposure to international property to the New Zealand dollar.
The assumed gross pre tax investment returns for each asset class are not achieved	▪ The Authority has adopted a diversified asset allocation strategy for the Fund and has appointed investment managers, based on demonstrated ability. However, the volatility of investment markets means that the projected return from the Fund is inherently uncertain. Actual returns from each asset class over the next year may vary significantly from the long term return assumptions used in calculating the increase in assets from investing activities.
Major structural changes to investment markets and/or taxation environment	▪ Neither of these risks is within the control of the Authority. However, the Authority will take into account changes in these risks in its reviews of the Strategic Asset Allocation and Investment Strategy.

Reputation Risk

RISK	ACTION TO MANAGE
The Authority's reputation risk	▪ Assessment of evolving practices in portfolio management, including review of their applicability to the GSF business. ▪ Robust selection process for investment managers. ▪ Determination of authorised investments (which may include authorised markets) in investment mandates. ▪ Maintenance of an internal governance framework for appropriate fiduciary oversight, performance management and control of functions carried out by the Board and Management. ▪ Implementation of a comprehensive risk management programme. ▪ Sustainable management of the GSF schemes to enable accurate assessment, payment and reporting of members entitlements. ▪ Comprehensive management and service agreements and clearly defined and agreed mandates and reporting standards.

Risks Relating to the Fund Liabilities

The Fund liabilities arise from the defined benefit schemes specified in the Act. Risks that may affect the liabilities include:

- movements in the consumers' price index (all retiring allowances and spousal annuities are CPI indexed);
- the rate of increase in contributors' salaries, especially as it affects the last five years of contributory service;
- the discount rate used to value the liabilities;
- factors affecting retirement or cessation of contributors, including state sector restructuring and privatisations;
- patterns of entitlement selection on retirement; and
- mortality rates.

None of the above risks is within the control of the Authority. The Authority will, however, ensure that accurate and timely information is provided to the Government Actuary to enable preparation of actuarial projections of the liabilities in accordance with the provisions of the Act.

RISK	ACTION TO MANAGE
The provisions for the schemes are not complied with and discretions relating to the schemes are inappropriately applied	▪ Monitoring the performance of Datacom and the resolution of any issues of interpretation of the legislation. ▪ Ensuring all discretionary decisions are exercised in accordance with the Statement of Provisions, Policies and Procedures. ▪ Ensuring any changes to the Statement of Provisions, Policies and Procedures are made only after taking into account the interests of relevant persons, including the Crown, in accordance with the Act.

GSF Schemes Administration Risks

The Authority is responsible for the management and administration of the GSF Schemes. Day-to-day administration duties are carried out by Datacom in accordance with an agreement that expires on 25 April 2011. In administering the GSF Schemes, heavy reliance is placed on the GSF Business System owned by the Authority.

RISK	ACTION TO MANAGE
Poor performance by Datacom Employer Services Limited	▪ Having a detailed schemes administration management agreement in place with Datacom, backed by a parent company guarantee. ▪ Maintaining a close liaison with Datacom. ▪ Monitoring Datacom's performance against the key performance standards. ▪ Carrying out an annual survey that assesses, amongst other things, the level of satisfaction of members and employers with the service provided by Datacom. ▪ Taking remedial action on any issues identified in the survey.
Serious information technology problems	▪ Ensuring any system modifications are approved by the Authority and that the system is well maintained. ▪ Ensuring that Datacom has in place back up systems and a fully tested business continuity plan and disaster recovery plan and that systems reliability is regularly monitored. The information technology hardware and operating software were upgraded and/or replaced in December 2003 to ensure the ongoing availability of maintenance support from the suppliers. ▪ In addition, during the 2007/2008 year, the Authority will be fully scoping the operations and functions of the GSF Business System, used for administering the GSF Schemes, as the first step in determining the specification for a new administration system.

Forecast Financial Statements

Forecast financial statements for the year ending 30 June 2008:

The Authority

(required under section 142(1)(a) of the Crown Entities Act)

- forecast income statement;
- forecast balance sheet;
- forecast statement of cash-flows;
- forecast reconciliation of net operating result to net operating cash-flows; and
- statement of accounting policies.

The Fund

(required under section 15N of the Act)

- forecast income statement;
- forecast balance sheet;
- forecast statement of cash flows;
- forecast reconciliation of income statement to net operating cash flows; and
- statement of accounting policies.

Government Superannuation Fund Authority
Forecast Financial Statements

Forecast Income Statement

Estimate 2006/07 $000		Forecast 2007/08 $000
14,407	Transfer from the Government Superannuation Fund	25,247
693	Other revenue	695
15,100	**Total revenue**	**25,942**
2,292	Schemes administration	2,400
9,075	Investment management *	19,400
3,733	Operating expenses	4,142
15,100	**Total expenses**	**25,942**
-	**Net operating result**	-

Forecast Balance Sheet

Estimate as at 30 June 2007 $000		Forecast as at 30 June 2008 $000
	Tax payers' equity	
-	General funds	-
-	**Total tax payers' equity**	**-**
	Represented by	
	Current assets	
130	Cash	170
2,045	Receivables and prepayments	2,170
2,175	**Total assets**	**2,340**
	Current liabilities	
2,175	Payables and accruals	2,340
2,175	**Total liabilities**	**2,340**
-	**Net assets**	**-**

* Refer explanation - paragraph 7, page 36.

Government Superannuation Fund Authority
Forecast Financial Statements - *continued*

Forecast Statement of Cash Flows

Estimate 2006/07 $000		Forecast 2007/08 $000
	Cash flows from operating activities	
	Cash was provided from	
14,872	Government Superannuation Fund	25,122
14	Interest	11
671	Other	684
	Cash was disbursed to	
(15,694)	Operating expenses	(25,777)
(137)	**Net cash flows from operating activities**	**40**
(137)	Net (decrease) increase in cash held	40
267	Opening cash brought forward	130
130	**Closing cash balance**	**170**

Forecast Reconciliation of Net Operating Result to Net Operating Cash Flows

Estimate 2006/07 $000		Forecast 2007/08 $000
-	**Net operating result**	-
	Add (less) movements in working capital items	
516	Decrease (increase) in receivables and prepayments	(125)
(653)	(Decrease) increase in payables and accruals	165
(137)	**Net cash flows from operating activities**	**40**

Government Superannuation Fund Authority

Statement of Accounting Policies and Significant Assumptions

1. Reporting entity and statutory base

The Government Superannuation Fund Authority ("the Authority") was established as a Crown entity by Section 15A of the Government Superannuation Fund Act 1956 as amended ("the Act"). The core business of the Authority is to manage and administer the Government Superannuation Fund ("the Fund") and the GSF Schemes.

The Fund was established by Section 13 of the Act. It consists of various defined benefit superannuation schemes (the GSF Schemes) as prescribed in the Act. A separate financial forecast has been prepared for the Fund. Pursuant to Section 19H of the Act, the GSF Schemes are registered under the Superannuation Schemes Act 1989.

The forecast financial statements have been prepared on the basis that the Authority is a going concern. The Authority is an Autonomous Crown Entity for legislative purposes and a Public Benefit Entity for financial reporting purposes.

2. Measurement base

The forecast financial statements have been prepared in accordance with Section 142 of the Crown Entities Act 2004.

These forecast financial statements have been prepared for the special purpose of the 2007/2008 Statement of Intent of the Authority for the Minister of Finance. They are not prepared for any other purpose and should not be relied upon for any other purpose.

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

3. Particular accounting policies

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

(a) *Forecast figures*

The forecast figures have been prepared in accordance with generally accepted accounting practice, and are consistent with the accounting policies adopted by the Authority for the preparation of the financial statements. Revenue and expenses are recognised on an accrual basis.

(b) *Goods and Services Tax*

The Authority is principally an exempt supplier in respect of Goods and Services Tax (“GST”), as it manages superannuation schemes. Transactions relating to the lease of levels 3 and 4 of 33 Bowen Street, Wellington are subject to GST. From 1 January 2005, GST was imposed on imported services if those services would be a taxable supply in New Zealand. The affected transactions for the Authority are fees incurred in relation to the custody of assets and investment reports. GST is included in expenditure.

(c) *Statement of Cash Flows*

The Forecast Statement of Cash Flows has been prepared using the direct approach.

(d) *Taxation*

As a Public Benefit Entity, in terms of the Income Tax Act 1994, the Authority is exempt from income tax.

(e) *Accounting for associates*

The Authority has a 50% ownership in Annuitas Management Limited (“Annuitas”). Staff employed by Annuitas act in management and secretarial roles on behalf of the Authority. Reimbursement of Annuitas costs, calculated on a time basis, are included in the operating expenses of the Authority. The Authority does not equity account for Annuitas as this is deemed to be immaterial.

4. Basis of preparation

The forecast financial statements have been prepared in accordance with New Zealand Generally Accepted Accounting Practice (NZ GAAP). They comply with New Zealand equivalents to International Financial Reporting Standards (NZ IFRS), and other applicable Financial Reporting Standards, as appropriate for Public Benefit Entities.

5. Impact of adoption of NZ equivalents to International Financial Reporting Standards (NZ IFRS)

From 1 July 2007 the Authority adopted NZ IFRS for financial reporting purposes. As the Authority operates without Equity or investments, the adoption of NZ IFRS has no impact on its financial performance and financial position.

6. Changes in accounting policies

All policies have been applied on bases consistent with those used in the year ended 30 June 2007.

7. Investment management expenses

The Authority is projecting an increase in investment management expenses from $9.1 million in 2007/2008 to $19.4 million. Of the increase of $10.3 million, $9.3 million reflects the planned move from passive to active management of international equities and the increase in allocation to international equities. The balance of $1 million reflects the increase in the size of the Fund.

8. Recovery of expenses

The forecast expenses of the Authority for the management and administration of the Fund and the GSF Schemes for the 2007/2008 year are $25.942 million. These expenses, net of other revenue of $695,000, are recovered from the Fund in accordance with Section 15E of the Act.

The Fund then recovers the payments made to the Authority (forecast $25.247 million) partly from the Crown, under a Permanent Legislative Authority (**PLA**), and partly from non-Crown employer contributions.

Previously the recovery by the Fund from the Crown was partly under a PLA and partly under a Non-Departmental Output Class appropriation. The recovery arrangement was changed to a PLA only with the approval of the Minister of Finance with effect from 1 July 2007.

The payments to the Authority by the Fund are recovered from the Crown and from non-Crown employer contributions in proportions determined by the Government Actuary. The Fund currently recovers 81% of the payments to the Authority from the Crown and 19% from non-Crown employer contributions. The Government Actuary has determined that, from 1 July 2007, the Crown's share will be 78.9% (forecast $19.920 million) and the share to be met from the non-Crown employer contributions 21.1% (forecast $5.327 million).

The expenses of the Authority include:

- management of the GSF assets (the Fund);

- expenses related to investment management, custodial arrangements and fees for implementing processes for avoiding prejudice to New Zealand's reputation as a responsible member of the world community;
- management of the GSF Schemes, including the agreement between the Authority and the schemes administrator; and
- interpretation of the provisions of the Act and the exercising of discretionary powers (set out in the Act);
- the fee paid to Annuitas under the Management Services Agreement between the Authority and Annuitas.

Government Superannuation Fund
Forecast Financial Statements

Forecast Income Statement

Estimate 2006/07 $000		Forecast 2007/08 $000
	Increase in assets from:	
590,112	**Investing activities**	328,044
	Operating activities	
14,407	Operating revenue	25,247
(14,407)	Funding the GSF Authority	(25,247)
590,112	**Surplus before tax and membership activities**	**328,044**
(181,436)	Tax	(58,013)
408,676	**Surplus after tax and before membership activities**	**270,031**
	Membership activities	
622,576	Contributions - Government	577,895
70,331	Contributions - members	61,435
15,683	Contributions - Other entities	15,310
(844,485)	Benefits paid	(796,085)
(135,895)	**Net benefits paid**	**(141,445)**
272,781	**Surplus after tax and after membership activities**	**128,586**
3,793,114	Opening assets available to pay benefits	4,065,895
4,065,895	**Net assets available to pay benefits**	**4,194,481**

Government Superannuation Fund
Forecast Financial Statements - *continued*

Forecast Balance Sheet

Estimate as at 30 June 2007 $000		Forecast as at 30 June 2008 $000
4,093,830	**Investments**	4,134,772
	Other assets	
10,000	Cash at bank	10,000
313,444	Receivables and prepayments	238,167
323,444		248,167
4,417,274	**Total assets**	**4,382,939**
	Less	
348,785	Other payables	186,064
2,594	Benefits accrued	2,394
351,379		188,458
4,065,895	**Net assets available to pay benefits**	**4,194,481**
	Estimated actuarial present value of Promised Retirement Benefits	
12,137,000	Gross liability	12,148,000
8,071,105	Deficit	7,953,519
4,065,895	**Net assets available to pay benefits**	**4,194,481**

Note - Deficit
The actuarial present value of Promised Retirement Benefits (Gross Liability) is the present value of the expected payments by the Fund to existing and past members, attributable to the services rendered. The present value has been calculated by the Government Actuary using a gross of tax discount rate. In previous years the present value has been calculated using a net of tax discount rate.

The Deficit shown in the Forecast Balance Sheet differs from that calculated by the Government Actuary in his actuarial valuation of the Fund under NZ IAS26, dated 8 May 2007 and shown on page 5. The Government Actuary projects a lower value for the assets of the Fund compared with the forecast made by the Authority.

There is no requirement on the Crown to fully fund the Deficit in relation to the GSF Schemes. Reliance is placed by the Authority on the provisions of section 95 of the Government Superannuation Fund Act 1956 which requires the Minister of Finance to appropriate funds from public money to ensure that sufficient funds are available, or will be available, to pay benefits as they fall due.

Government Superannuation Fund
Forecast Financial Statements - *continued*

Forecast Statement of Cash Flows

Estimate 2006/07 $000		Forecast 2007/08 $000
	Cash flows from operating activities	
	Cash was provided from	
582,976	Contributions - Government	597,561
70,740	Contributions - members	60,693
18,315	Contributions - other entities	20,669
99,666	Interest	136,913
855	Other	866
	Cash was disbursed to	
(844,133)	Benefits payments	(795,045)
(139,255)	Income tax	(60,000)
(14,872)	Operating expenses	(25,122)
(225,708)	**Net cash outflows from operating activities**	**(63,465)**
	Cash flows from investing activities	
	Cash was provided from	
6,302,728	Maturities and sales of investment assets	6,297,940
112	Mortgage repayments	24
	Cash was disbursed to	
(6,103,324)	Purchase of investment assets	(6,234,499)
199,516	**Net cash inflows from investing activities**	**63,465**
(26,192)	Net (decrease) increase in cash held	-
36,192	Opening cash brought forward	10,000
10,000	**Closing cash balance**	**10,000**

Government Superannuation Fund
Forecast Financial Statements - *continued*

Forecast Reconciliation of Net Changes in Net Assets to Net Operating Cash Flows

Estimate 2006/07 $000		Forecast 2007/08 $000
272,781	**Net increase in net assets**	128,586
	Non-cash items	
(7)	Capitalised interest	(3)
1	Mortgage management expense	1
(6)		(2)
	Add (less) movements in working capital items	
(144,615)	(Increase) decrease in receivables and prepayments	75,388
25,045	Decrease in tax receivables	-
(208,575)	(Decrease) increase in other payables	(162,721)
310	Increase (Decrease) in benefits accrued	(200)
(327,835)		(87,533)
	Add (less) items classified as investing activities	
3,857	Decrease (increase) in accrued interest portion of fixed interest bonds	1,559
(494,293)	Increase in net market values of investment assets	(192,684)
144,356	Increase (decrease) in investment receivables	(72,802)
175,432	Decrease in investment payables	159,411
(170,648)		(104,516)
(225,708)	**Net cash outflows from operating activities**	**(63,465)**

Government Superannuation Fund
Statement of Accounting Policies

1. Reporting entity and statutory base

The Government Superannuation Fund ("the Fund") was established by Section 13 of the Government Superannuation Fund Act 1956 ("the Act"). It consists of the assets held in respect of various defined benefit superannuation schemes (the GSF Schemes) prescribed in the Act. Pursuant to Section 19H of the Act, the GSF Schemes are registered under the Superannuation Schemes Act 1989.

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

2. Measurement base

The forecast financial statements have been prepared as required by Section 15N of the Act. These forecast financial statements have been prepared for the special purpose of the 2007/2008 Statement of Intent of the Authority for the Minister of Finance. They are not prepared for any other purpose and should not be relied upon for any other purpose.

The forecast financial statements have been prepared on the basis of historical cost with the exception that certain assets and liabilities are measured at fair value. The reporting currency is in New Zealand dollars.

3. Particular accounting policies

The following particular accounting policies, which significantly affect the measurement of changes in net assets, net assets and cash flows, have been consistently applied:

(a) *Reporting requirements*
The forecast financial statements have been drawn up in accordance with all relevant New Zealand equivalents to International Financial Reporting Standards (NZIFRS). NZ IFRS including Standard NZ IAS 26: *Accounting and Reporting by Retirement Benefit Plan*, and with the provisions of relevant legislative requirements.

(b) *Investments*
Investments are recorded on a trade date basis and are stated at fair value

(c) *Actuarial valuation*

The actuarial present value of promised retirement benefits is the present value of the expected payments by the Fund to existing and past members, attributable to the services rendered.

(d) *Financial instruments*

The Fund is party to financial instruments as part of its normal operations. These financial instruments include bank accounts, investments, receivables and payables. Financial instruments, including derivatives that are hedges of specific assets, are recognised on the same basis as their underlying hedged assets. All financial instruments are recognised in the Balance Sheet and all revenues and expenses in relation to financial instruments are recognised in the Income Statement.

Investments are recorded at fair value and all other financial instruments are shown at their estimated fair value.

(e) *Other receivables*

Receivables are stated at their estimated realisable value.

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 discounted at the financial asset's original effective interest rate.

If, in a subsequent period, the amount of an impairment loss recognised on a financial asset carried at amortised cost decreases and the decrease can be linked objectively to an event occurring after the write-down, the write down is reversed through the Income Statement.

(f) *Investment income and expenses*

Dividend income is recorded on the ex-dividend date. Interest is recorded on an accrual basis.

Gains and losses on the sale of equities are determined by using the average cost of equities sold and are recorded on the settlement date.

All realised and unrealised gains and losses, at the end of the year, are included in the Income Statement.

Costs of administration of the Fund, including investment management and custodian fees, are paid out of the Fund and recovered in accordance with Section 15E of the Act.

(g) *Operating revenue*
In terms of section 15E(1) of the Act, the administration expenses of the Authority, including investment management and custody expenses, are reimbursed by the Fund. Both the Crown and other employers reimburse the Fund under section 95 of the Act for the Authority's expenses.

(h) *Contributions and benefits*
Contributions are recognised in the Income Statement, when they become receivable, resulting in a financial asset for amounts receivable from both employees and employers.

Benefits are recognised in the Income Statement when they become payable, resulting in a financial liability for current payments owing.

(i) *Taxation*
Income taxation expense includes both the current year's provision and the income tax effects of temporary differences, calculated using the liability method.

Tax effect accounting is applied on a comprehensive basis to all temporary differences. A balance in the deferred tax account, arising from temporary differences or income tax benefits from income tax losses, is only recognised where there is virtual certainty of realisation.

(j) *Statement of Cash Flows*
The following are the definitions of the terms used in the Statement of Cash Flows:

Operating activities include all transactions and other events that are not investing or financing activities.

Investing activities are those activities relating to the acquisition, holding and disposal of investments. Investments include securities not falling within the definition of cash, including cash flows from the settlement of forward foreign exchange contracts.

Cash and other cash equivalents includes cash balances on hand, held in bank accounts, demand deposits and other highly liquid investments in which the Fund and its managers invest as part of its day-to-day cash management.

(k) *Consolidation*
The Fund's financial statements include the Judges' Superannuation Account and the Parliamentary Superannuation Account.

4. Basis of preparation

The forecast financial statements have been prepared in accordance with New Zealand Generally Accepted Accounting Practice (NZ GAAP). They comply with New Zealand equivalents to International Financial Reporting Standards (NZ IFRS), and other applicable Financial Reporting Standards, as appropriate for profit oriented entities. Compliance with NZ IFRS ensures that the financial statements also comply with International Financial Reporting Standards (IFRS). Actual financial results achieved for the period covered are likely to vary from the information presented, and the variations may be material.

5. Measurement adjustments

The transition to NZ IFRS resulted in two significant adjustments as follows:

(a) *Valuation of investments*
The removal of disposal costs from the valuation of investments. Under NZ GAAP investments were measured at net market value (ie market value less an allowance for anticipated disposal costs). Under NZ IFRS investments are measured at fair value (in the case of marketable securities this is equal to market value). The investments impacted were:

- New Zealand equities
- International fixed interest
- Listed property

The estimated overall impact of the removal of disposal costs from the valuation of investments at 30 June 2007 is $3.452 million (30 June 2006: $2.552 million).

(b) *Receivable for other entities' contributions*
This adjustment has two parts, provisioning and valuation method.

Under NZ IFRS general provisioning is prohibited. A provision for doubtful debts can only be recognised when a loss event has been deemed to occur. No such loss event has occurred with the receivable for other entities' contributions. Therefore, a provision established under NZ GAAP has been reversed, increasing the debt by $3.305 million at 30 June 2006.

The second part to this adjustment relates to the accounting policy for loans and receivables under NZ IFRS. Under NZ IFRS, loans and receivables are to be initially recorded at fair value, and then subsequently measured using the amortised cost method. The fair value of the debt is measured as the net present value of the future cash flows of the transaction. As there is a repayment schedule for the other entities' contributions, the future cash flows were readily identifiable. An applicable discount rate has been determined (8.95%) and the cash flows discounted back using this rate.

The adjustment is estimated to result in a calculated fair value of the other entities contributions of $3.306 million at 30 June 2007 ($3.477 million at 30 June 2006) and a recorded amortised cost value at 30 June 2007 of $3.524 million (30 June 2006 $3.695 million).

Classification Adjustments
A number of investment balances have been reclassified to comply with the requirements of NZ IFRS. The most significant of these are in respect of:

- Derivative assets and liabilities – these have been grossed up where they were previously reported net and split out from the related investment assets to comply with the requirements of NZ IAS 32: Financial Instruments: Disclosure and Presentation, and
- Cash and cash equivalents – this balance has increased to include all amounts previously classified within related investment balances that meet the definition of cash or cash equivalents as defined in NZ IAS 7: Cash Flow Statements.

Taxation Adjustment
Under NZ IFRS (NZIAS 12 Income Taxes), deferred tax is calculated and provided using the balance sheet liability method. This may result in temporary differences arising between the carrying amounts of assets and liabilities used for accounting purposes and the amounts used for tax purposes.

6. Changes in accounting policies

There are no other significant changes in accounting policies, except as required by NZ IFRS and detailed above.