

GOVERNMENT
SUPERANNUATION FUND
AUTHORITY

STATEMENT OF INTENT
1ST JULY 2012

2012

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SUPERANNUATION FUND
AUTHORITY

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Government Superannuation Fund

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1. STATEMENT FROM THE BOARD

The Government Superannuation Fund Authority (**the Authority**) is an autonomous Crown Entity established under the Government Superannuation Fund Act 1956 (**the Act**).

The functions of the Authority are to manage and administer the Government Superannuation Fund (**GSF** or **the Fund**) and the GSF superannuation schemes (**the Schemes**) in terms of the Act.

The Fund has an actuarial deficit in that its assets are significantly less than the gross liabilities of the Schemes. The deficit exists primarily because, over the years, successive governments have elected not to pay employer contributions on behalf of their staff. Instead, governments provided funding as entitlements were paid. The Authority places reliance on the provisions in the Act for the Minister of Finance (**Minister**) to ensure that sufficient funds are available, or will be available, to the Fund to pay entitlements as they fall due.

In carrying out its functions, the Authority has established two desired outcomes:

1. Contribute to an improvement in the Crown's overall economic position by endeavouring to minimise the Crown's contributions to the Fund.
2. Meet the needs and reasonable expectations of stakeholders.

The Authority seeks to improve the Crown's overall economic position, and meet the needs of reasonable expectations of the Crown as a key stakeholder of the Fund, by maximising the returns of the Fund, within acceptable levels of risk, controlling costs and ensuring members receive their entitlements in accordance with the Act.

The members of the Schemes and the employer contributors to the Scheme are also key stakeholders of the Fund. The Authority has determined the needs and reasonable expectations of the members and the employers to be as follows:

- Members - for entitlements to be calculated correctly, consistent with the Act and the policies maintained by the Authority, and to be paid on time. Meeting this need and reasonable expectation is a key factor in the Authority's management and administration of the Schemes.
- Employers - for contributions to be minimised.

Outputs that will assist in achieving the desired outcomes and measures to assess performance against the outputs are set out in Sections 3 (Investment) and 4 (Schemes).

The Authority takes a long term view when developing its investment strategy because the Fund is expected to pay entitlements for the next 60 years or so. It has adopted an Investment Objective and strategy that involves taking additional investment risk to improve the Crown's position compared to investing solely in New Zealand Government Stock (see page 7).

The Authority reviews its investment strategy regularly. Although the additional risk was not rewarded over the last ten years and the Fund is tracking below its long term performance measure, the Authority believes the current strategy and risk profile are appropriate to achieve the measure over the Fund's long term horizon. In particular, we believe that the expected return from global equities will be higher than the expected return from New Zealand Government Stock over the long term. This belief is supported by a range of external and peer opinion.

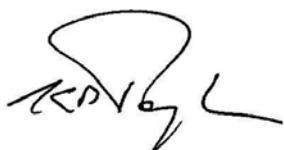
The Authority's investment strategy is also benchmarked against a Reference Portfolio, which is a simple, passive, low cost way to achieve the Investment Objective. This helps define the strategy's risk and is used to assess the actual performance of the Fund and the value added or subtracted by active decisions of the Fund's managers. Active investment management has been employed broadly by the Fund only since fiscal 2008 and has generally added value. The Fund has slightly underperformed its Reference Portfolio in that period but has also had less downside risk. The Authority believes diversifying away from equity risk into alternative return sources and engaging skilled active managers, where they can add value, is worthwhile after allowing for additional fees and costs.

The second statutory review of the Authority was undertaken during the year ended 30 June 2011. A key conclusion of the reviewer was that:

The Fund's investment objectives and strategy have been developed based on sound principles using a logical and consistent approach. In our view, the policies, standards and procedures developed by the Authority in determining the investment objectives and strategy are appropriate for the Fund.

The review made a number of recommendations and suggested enhancements to the operations of the Fund, most of which have been accepted by the Authority Board and action plans developed. Implementation of the plans will form a significant part of the Authority's work over the next 1-2 years.

More information on the Authority and its policies and operations is available on our website at www.gsfa.govt.nz.



Keith Taylor
Chairman



David May
Deputy Chairman

May 2012

2. THE AUTHORITY

OPERATING ENVIRONMENT

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

The Authority was established in 2001 to manage and administer the assets of the Fund and the Schemes in accordance with the Act.

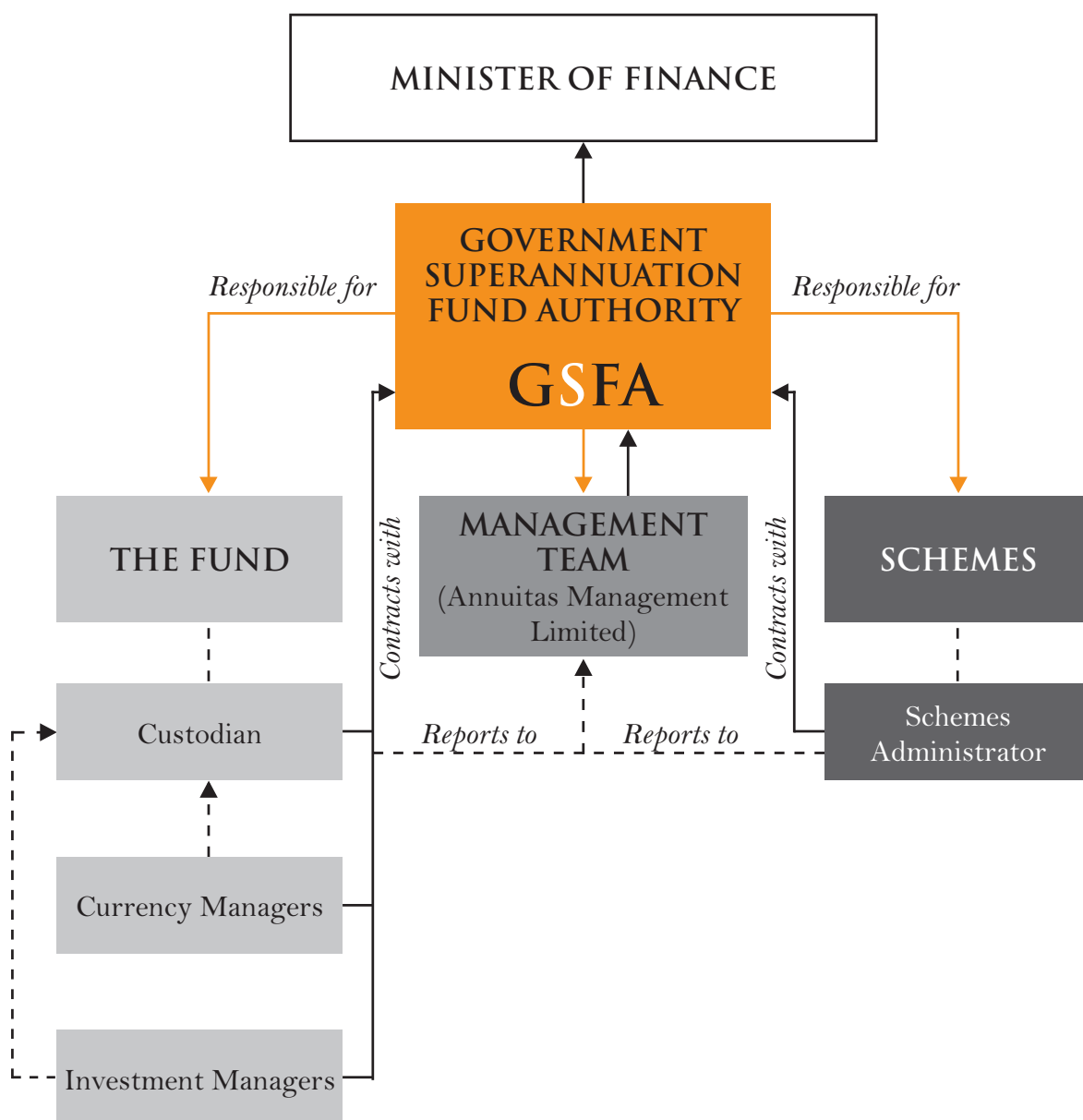
A Board, established by the Act and appointed by the Minister, governs the Authority and determines its business either directly or by delegation.

The Authority oversees the management of the Fund and the Schemes but has outsourced the key activities of scheme administration and investment management, including custody of the Fund's assets.

The Authority's organisational structure is set out in Diagram 1 on the next page. Further information on organisational structure is set out on page 21.

This Statement of Intent (**SOI**) is prepared pursuant to part 4 of the Crown Entities Act 2004 (**Crown Entities Act**). In addition, Section 15N of the Act requires the Authority to include in its SOI specific comments on the expected performance of investment assets of the Fund and the Schemes over the next financial year, as well as the risks to that performance and the steps taken to manage those risks. See pages 9 and 26.

Diagram 1: Structure of the Government Superannuation Fund Authority and its operations



NATURE AND SCOPE OF FUNCTIONS

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

The Authority's functions are to manage and administer the Fund and the 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 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 to meet the Government's expectations as to the Fund's performance, including the Government's expectations for 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 investment assets of the GSF.

Schemes

- Management and administration of the Schemes, including the agreement between the Authority and the scheme administrator.
- Interpretation of the provisions in the Act and exercise of discretionary powers (set out in the Act).

Details on the outputs and performance measures for these activities can be found on pages 6 –15 (**Investment**) and 16 - 19 (**Schemes**).

3. INVESTMENT

OBJECTIVES AND STRATEGY

(section 141(1)(c) and (d) of the Crown Entities Act)

The Authority's investment responsibilities under the Act are to:

- invest the Fund on a prudent, commercial basis, in a manner consistent with best practice portfolio management;
- maximise returns without undue risk to the Fund as a whole; and
- avoid prejudice to New Zealand's reputation as a responsible member of the world community (avoid prejudice).

The Authority meets these responsibilities by developing and implementing:

- principles for best practice portfolio management;
- an investment strategy centred on a defined return objective over the long term and within a defined risk limit; and
- responsible investment policies to meet the requirement to avoid prejudice.

BEST PRACTICE PORTFOLIO MANAGEMENT

The Authority interprets best practice portfolio management as:

- Having a clear investment objective that reflects its statutory responsibilities and desired outcomes.
- Maintaining a sound investment strategy consistent with that objective and the Authority's Investment Beliefs (**Beliefs**).
- Having strong governance with clear assignment of responsibilities that promotes accountability, clear reporting and effective communication with the Fund's stakeholders.
- Engaging external managers with the requisite skills to implement desired investment strategies on terms that align with the Authority's goals.
- Ensuring cost-effective management of investments measured by robust monitoring of performance.
- Encouraging the sharing of relevant knowledge and resources with other Crown Financial Institutions (**CFIs**), peer funds and experts.

The Authority's outputs and performance measures for investment are designed to achieve these elements and measure success.

The Authority has established a set of Beliefs to provide a robust foundation for its investment strategy and to communicate shared values about investment. The Beliefs comprise the Authority's views with regard to the sources of investment return and risk and how these can be captured cost effectively. The Beliefs are set out in the Statement of Investment Policies Standards and Procedures (**SIPSP**), published on the Authority's website www.gsfa.govt.nz, and are reviewed annually by the Board.

The Authority seeks to achieve returns in excess of the returns from Government Stock by accepting additional investment risk. Most of this additional return is the

expected reward for bearing systematic or market risk from owning equities and other assets whose values may fluctuate significantly. Further additional risk arises from the pursuit of active investment strategies that may produce returns that vary from market benchmarks from time to time.

The Authority has established a SIPSP that sets out how these risks are managed. The SIPSP is reviewed and updated at least annually by the Board.

MAXIMISING RETURN WITHOUT UNDUE RISK TO THE FUND AS A WHOLE

The Authority seeks to develop and maintain a diversified and efficient investment portfolio that will meet the Investment Objective (see below). It is implemented by allocating the Fund's assets across a mix of exposures to broad categories of market risk and return and supplementing this with active, skill-based sources of return.

Investment Objective (output)

Maximise the return on the assets of the Fund over the long term, without undue risk to the Fund as a whole, in a manner consistent with best practice portfolio management.

In seeking to achieve this objective, the Authority balances the level of investment risk of the Fund and the expected excess return over New Zealand Government Stock. The Risk Parameter and Investment Performance Measure define this balance of risk and return.

Risk Parameter (measure)

To have no more than a one in ten chance in any one year of a loss after tax greater than 9% of the total Fund.

Investment Performance Measure (IPM) (measure)

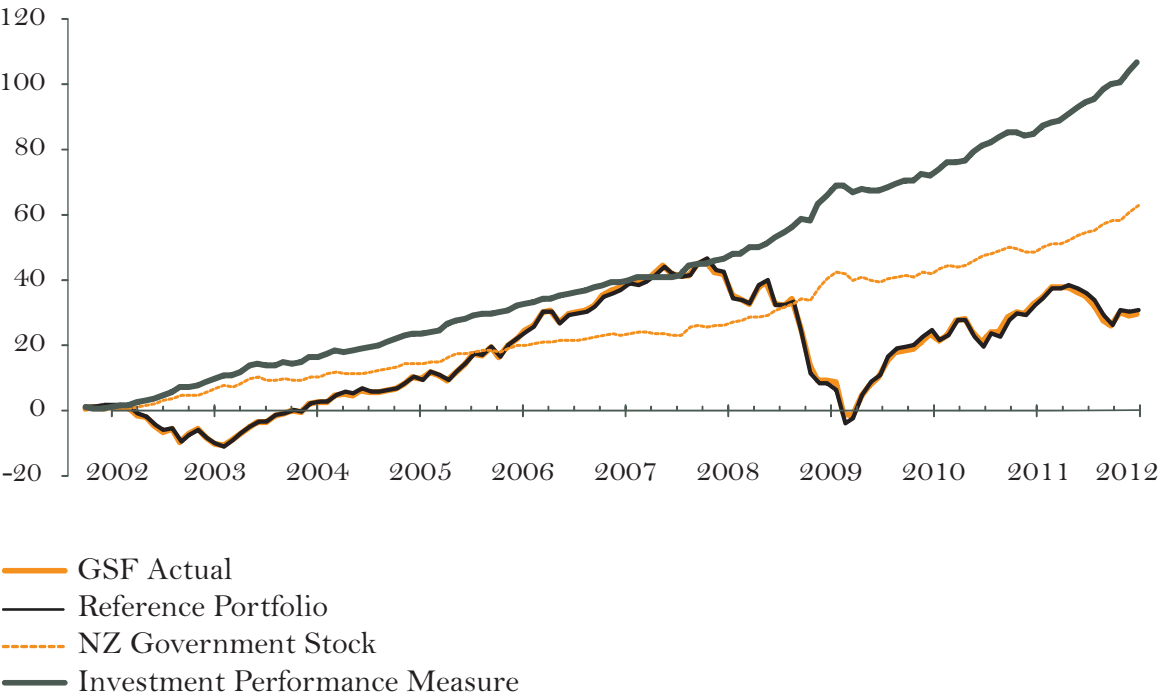
To achieve an after tax return equivalent to the ANZ New Zealand Government Stock Gross Return Index (after tax) plus at least 2.5% per annum, measured over rolling 10 year periods.

Since 2009 the Authority has benchmarked its investment performance against a Reference Portfolio (**RP**), which is a simple, passively managed, notional portfolio that meets the Risk Parameter and could achieve the IPM by investing only in major, liquid, public markets at low cost. The Reference Portfolio reflects the Fund's risk and return objectives and provides a benchmark for its actual performance. Most of the Fund's performance is expected to be attributable to the market risk factors captured in the Reference Portfolio. However, the Authority believes certain alternative market exposures and active management can add value to the Fund by improving returns and/or lowering risk, consistent with best practice portfolio management. The extra cost and the potential added value are considered carefully before investing and are measured against the Reference Portfolio.

The Fund's overall performance since October 2001, when the Authority assumed responsibility for managing the Fund, is assessed by comparing its investment return and

risk with the IPM and Risk Parameter as illustrated in Graph 1 below. (Graph 1 is before investment management fees as data after investment management fees is not available prior to 1 July 2009).

Graph 1: GSF Cumulative Returns since Inception (after tax, before fees)



The Fund has not achieved its IPM over the full period since inception in 2001. This reflects poor returns from global equities compared to Government Stock over this period, notably in 2000-02 and again in the global financial crisis of 2007-08.

It is important to recognise that the Fund will pay entitlements for the next 60 years or so and that the Authority takes a long term view in setting the investment strategy. Investment performance is measured over rolling ten year periods. Although returns have been below expectations in the ten years since inception, they were within the risk parameters set.

The Authority reviews its investment strategy regularly and believes the current strategy and risk profile are appropriate to achieve the Investment Objective over the Fund's long term horizon. In particular, forward projections suggest that equities will earn a significant premium over Government Stock in the next ten years, in contrast to the past ten years when they earned less.

AVOID PREJUDICE

The Authority's Responsible Investment Policies can be viewed on its website www.gsfa.govt.nz. It has developed programmes to monitor the risk of investments to New Zealand's reputation, exclude prejudicial investments where practicable, engage companies on environmental, social and governance (**ESG**) issues and generally support greater integration of material ESG issues into investment processes.

The Authority is a signatory to the United Nations Principles for Responsible Investment (**UNPRI**). Where they are consistent with each signatory's fiduciary duties, signatories seek to address six aspirational principles established by UNPRI. The principles can be viewed on unpri.org/principles.

The Authority has entered into a resource sharing agreement with other CFIs to help the Authority meet its 'avoid prejudice' obligations and implement its policies, including its UNPRI commitments, efficiently.

FORECAST SERVICE PERFORMANCE FOR 2012/2013

(Sections 141(1)(c) and (d) and sections 142(2)(a) and (b) of the Crown Entities Act, and section 15N of the Act)

The two outcomes established by the Authority for investment are to:

- Contribute to an improvement in the Crown's overall economic position by endeavouring to minimise the Crown's contribution to the Fund.
- Meet the needs and reasonable expectations of stakeholders – employer contributions to be minimised.

Investment Performance Expectations for 2012/2013

The Board's forecast increase in assets from investing activities, included in the Forecast Income Statement for the Fund, is based on expected long term average returns from each asset class held (see Significant Assumptions used in the Forecast of the Fund on page 13.) The volatility of markets for growth assets like equities means that the forecast in any given year is subject to a wide margin of error. Volatility and uncertainty is higher for returns for 1 year than for 10 year periods. As a result, returns in any particular year are not necessarily indicative of the long term investment performance of the Fund. Actual returns from each asset class in the year may vary significantly from the assumptions, which represent a mean or mid-point of the range of expected returns.

In that context, the Board's forecast return for the Fund for the year ended 30 June 2013 is 6.8% after tax and before total investment costs (see Table 1 on the next page). This translates to a forecast surplus after tax and before total investment costs of \$201 million for the Fund (\$176 million after tax and total investment costs).

The forecast return corresponds to a 1 in 17 chance of a loss after tax greater than 9% of the total Fund, compared with a 1 in 10 chance for the Risk Parameter.

The forecast includes an allowance for added value from alternative market exposures and active management strategies. These increase the Fund's expected risk-adjusted return compared with the Reference Portfolio and lower the probability of significant loss as defined by the Risk Parameter. The Fund is forecast to return 0.4% (\$11 million) more than the Reference Portfolio, after tax and total investment costs, and have significantly less chance of a loss greater than 9% (1 chance in 17 compared to 1 in 13).

Table 1: Projected Investment Performance and Risk for the Projected Portfolio and the Reference Portfolio for the year ended 30 June 2013

	PROJECTED PORTFOLIO		REFERENCE PORTFOLIO	
	\$m	Basis points pa	\$m	Basis points pa
Investment performance	243	816	206	692
Increase in assets from investing activities (<i>before tax and total investment costs</i>)				
Surplus (<i>after tax and before total investment costs</i>)	201	677	172	578
Investment Performance Measure		574		574
Surplus (<i>after tax and total investment costs</i>)	176	596	165	555
Investment risk		600		800
Risk (<i>chance of loss after tax >9% of total Fund</i>)		(1 in 17)		(1 in 13)
Investment costs				
Direct investment management fees	20	66	4	14
Custody expenses	2	7	1	3
Overheads (<i>share of Authority's operating expenses</i>)	3	9	2	5
Total investment costs	25	82	7	23

- One basis point equals 0.01%.
- The Projected Portfolio is the portfolio used as the basis for projecting the increase in assets from investment activities (IA) as shown in the Forecast Income Statement for the Fund.
- Table 2, on page 13, shows the assumed asset allocations for the Projected Portfolio and the Reference Portfolio.
- The assumed returns from each asset class, used to calculate the IA, are set out in Table 3 on page 14 and include, where appropriate, 50% of the alpha (added value) expected from active management of the asset class.
- Total investment costs include the projected direct investment management fees and custody expenses and 70% (50% for the Reference Portfolio) of the Authority's projected operating expenses (see page 31). Investment costs are not deductible for tax.
- The Investment Performance Measure is calculated using an assumed return from NZ Government Stock (before tax) of 4.5%.

Outputs and Performance Measures

In addition to setting the Investment Objective the Authority sets specific outputs and performance measures for investment. These will assist the Authority to achieve the investment outcomes it has established, eg:

- Contribute to an improvement in the Crown's overall economic position by endeavouring to minimise the Crown's contributions to the Fund.
- Meet the needs and reasonable expectations of the Crown as a stakeholder.

Some outputs are ongoing, while others reflect specific projects that may be completed over a period beyond one year.

For the 2012/2013 year the Authority has identified the following service performance outputs and performance measures for investment:

OUTPUTS	MEASURES
Manage investments to maximise returns over the long term, without undue risk to the Fund as a whole, in accordance with best practice portfolio management.	<ul style="list-style-type: none"> • Fund return versus the IPM. • Actual performance (returns and assessed risk) compared to the RP to determine the added value of alternative asset exposures and active management (net of additional fees and costs). • Expected and actual volatility of Fund returns versus the Risk Parameter. <p>All measured with reference to independent market valuations by the custodian and by the Authority's investment management staff.</p>
Endeavour to achieve competitive investment costs justified by value added.	<ul style="list-style-type: none"> • Comparison of investment managers' actual performance against contracted mandates and representative benchmarks, measured independently by the custodian and assessed by the Authority's investment management staff, with monthly management reporting and quarterly reporting to the Board. • Comparison of expected and actual value added, in terms of excess return (net of additional expenses) and/or reduced risk, versus the RP. • Annual comparison of the Fund's performance and cost structure with those of similar organisations, prepared by independent party. • Independent statutory review every 5 years.
Monitor individual investment managers to ensure compliance with contracted mandates and, where appropriate, out performance against benchmarks.	<ul style="list-style-type: none"> • External review by independent adviser and regular reviews by the Authority's investment management staff.
Maintain a SIPSP that meets best practice.	<ul style="list-style-type: none"> • Periodic review by independent adviser to assess whether the SIPSP meets best practice and is relevant.

OUTPUTS	MEASURES
Comply with the SIPSP.	<ul style="list-style-type: none"> • No unauthorised variations from the SIPSP (which may be varied by the Board from time to time) identified on annual review. • Actual asset allocation rebalanced monthly to within rebalancing tolerances set out in the SIPSP. • Investment manager risk remains in line with expectation by comparing investment managers' actual risk profiles against expected risk. • Review of quarterly key performance indicators to determine that the custodian's performance meets its Service Level Agreement.
Put in place a sound investment strategy consistent with the SIPSP and the Authority's Beliefs.	<ul style="list-style-type: none"> • Board review of the investment strategy, including the key investment and taxation assumptions, at least annually that confirms the strategy is consistent with the SIPSP and the Authority's Beliefs.
Ensure compliance with Responsible Investment Policies, including the Board's policies on ethical investment.	<ul style="list-style-type: none"> • No investments that breach the Responsible Investment Policies and the Board's policies on ethical investment. • Measured by internal and external review.
Collaborate with other CFIs to increase the extent to which the Authority meets the aspirational principles established by UNPRI consistent with its other investment responsibilities.	<ul style="list-style-type: none"> • Above average ratings on the implementation of the aspirational principles established by UNPRI, assessed by UNPRI review.
Ensure the Authority complies with the GSF Act.	<ul style="list-style-type: none"> • Conclusions of in-house legal compliance programme developed with advice from the Authority's legal firm.

Overall expected costs (Investment) \$24.5 million

Note: Overall expected costs (Investment) include the projected investment management expenses and 70% of the Authority's projected operating expenses (see page 32).

SIGNIFICANT ASSUMPTIONS USED IN THE FORECAST OF THE FUND

(Sections 142(1)(d) and (e) of the Crown Entities Act)

- Table 2 sets out the assumptions made for the asset allocations for the Projected Portfolio and the Reference Portfolio. The Authority seeks to enhance the Fund's performance by investing in certain alternative market exposures, such as real estate, insurance linked assets, private equity and global tactical asset allocation, and active management strategies. These exposures and strategies are expected to result in a reduction in investment risk and/or an increase in returns compared to the Reference Portfolio, after allowing for incremental costs.

Table 2: Assumed Asset Allocations of the Projected Portfolio and the Reference Portfolio as at 30 June 2012

ASSET CLASS	PROJECTED PORTFOLIO %	REFERENCE PORTFOLIO %
International Equities	42.4	55.0
New Zealand Equities	9.4	10.0
Global Fixed Interest	22.6	30.0
Collateralised Commodity Futures	3.3	5.0
Real Estate	5.0	n/a
Multi-Asset Class	7.0	n/a
Catastrophe Risk	5.1	n/a
Life Settlements	1.9	n/a
Global Tactical Asset Allocation	3.3	n/a
Total	100.0	100.0

- The Reference Portfolio is a simple, passively managed notional portfolio, which invests only in major liquid public markets.*
- The actual asset allocation for the Fund is rebalanced if required.*
- The Board's forecast of the performance of the Fund depends on assumptions with respect to the returns (before tax) from each asset class in the projected asset allocation. These assumptions are long term (see Table 3) and actual returns from each asset class over the next year may vary significantly from the long term return assumptions used.*

Table 3: Assumed Returns for each Asset Class (before tax)

ASSET CLASS	ASSUMED RETURNS (BEFORE TAX) %	
	PROJECTED PORTFOLIO	REFERENCE PORTFOLIO
International Equities	9.0	7.8
New Zealand Equities	8.9	7.2
Global Fixed Interest	5.9	5.2
Collateralised Commodities Futures	6.8	5.3
Real Estate	8.5	n/a
Multi-Asset Class	8.4	n/a
Catastrophe Risk	8.5	n/a
Life Settlements	8.9	n/a
Global Tactical Asset Allocation	6.8	n/a

- The assumed returns for the Reference Portfolio have been independently sourced from Russell Investment Group Limited (**Russell**).
- The assumed returns for the Projected Portfolio are based on the assumed returns sourced from Russell, adjusted by the Authority for risk and/or added value by managers as appropriate.
- The assumed returns for the Projected Portfolio are lower than those used in the 2011 Statement of Intent. For example, the assumed return for International Equities is 9.0% in 2012 (2011: 10.4%).
- Investment management agreements with managers contain return expectations and the methodology for calculating fees, based primarily on assets under management. Actual returns from each asset class in the year may vary significantly from expected returns. In addition, in projecting its expenses, the Authority allows for the payment of performance fees to some managers if agreed performance targets are exceeded. Consequently actual fees may vary from those projected.
- The assumed returns for each asset class in the Projected Portfolio include, where appropriate, 50% of the alpha (added value) expected from active management of the asset class.
- Currency hedging is in place for all international assets while leaving an overall level of foreign currency exposure the Board considers is prudent. The net currency exposure benchmark is currently 20% of the Fund's assets. The projections make no allowance for changes in the value of the New Zealand dollar against other currencies, which could affect the value of the unhedged portion of the Fund.
- Asset values, as at 1 July 2012, are projected from actual 31 January 2012 asset values.
- Projected entitlement payments from the Fund are \$11 million per month.
- Taxation assumptions are summarised in Table 4 (see next page).

Table 4: Taxation Assumptions

ASSET CLASS	TAX TREATMENT
International Equities Real Estate Life Settlements and Multi-Asset	<ul style="list-style-type: none">• 28% on 5% of the average value of the portfolios during the year.
New Zealand Equities	<ul style="list-style-type: none">• 28% on dividends, allowing for 20% imputation credits
Fixed Interest Collateralised Commodities Futures Catastrophe Risk and Global Tactical Asset Allocation	<ul style="list-style-type: none">• 28% on accounting profit or loss

BACKGROUND

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

The 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 Schemes, each of which is registered as a superannuation scheme under the Superannuation Schemes Act 1989.

Currently the Schemes have just under 66,000 members, made up of around 19,000 contributory members and deferred annuitants (eg. members who have elected to receive their entitlements from a future date) and around 46,800 annuitants. It is expected that entitlements will continue to be paid by the Fund for the next 60 years or so.

Contributory members contribute a defined percentage of their superable salaries (which may be different to their total remuneration) to the Fund on a regular basis. In return, they receive a retiring entitlement based on their average superable salary for the last five years of contributory service, years of service and age at retirement.

Certain non Government employers contribute the balance of the accruing cost of their employees' retirement entitlements to the Fund. The Government, as an employer, meets its share of members' retirement entitlements as they fall due for payment. Therefore, the Schemes are only partially funded, with the accumulated employee contributions, investment returns and employer contributions (from non Government employers) being deemed by the Government Actuary to be sufficient to meet 20% of the entitlements at present (21.1% from 1 July 2012).

The actual and projected present values of the Unfunded Past Service Liabilities (**UPSLS**) of the Fund have been calculated by the Government Actuary in his actuarial valuation, as at 30 June 2011, dated August 2011. The results are set out in Table 5. The UPSLS are estimates of the Crown contributions required to meet the past service liabilities of the Fund.

Table 5: Actual and Projected Unfunded Past Service Liabilities

	ACTUAL 30 JUN 11 \$M	PROJECTED 30 JUN 12 \$M	PROJECTED 30 JUN 13 \$M
Past Service Liabilities	12,255	12,187	12,096
Net Assets	3,159	3,220	3,278
Unfunded Past Service Liabilities	9,096	8,967	8,818

- *The actual and projected unfunded past service liabilities were calculated by the Government Actuary using a net of tax investment rate. The Unfunded Past Service Liabilities, calculated using a gross discount rate, are recorded in the Crown's financial statements.*
- *Investment markets have declined since the Government Actuary carried out his valuation. The Board projects net assets to be \$3,026 million, as at 30 June 2012, and \$3,096 million, as at 30 June 2013.*
- *In future the valuations will be undertaken by an Actuary appointed by the Authority.*

The position of Government Actuary was disestablished in 2011. An Actuary appointed by the Authority will calculate the actual and projected UPSLs from 30 June 2012. The Actuary has already indicated that she will allow for continued improvements in mortality (eg. annuitants are living longer) which will increase the past service liabilities and consequently the UPSLs. The Authority estimates, based on calculations prepared by the Actuary for the Crown, that the improved mortality may add \$1 billion to the past service liabilities and the UPSLs.

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

OBJECTIVES AND STRATEGY

(sections 141(1)(c) and (d) of the Crown Entities Act)

The Authority aims to ensure sustainable, cost effective management of the Schemes to enable accurate calculation, payment and reporting of members' entitlements.

The Authority does this by ensuring:

- contributions are collected and entitlements are calculated and paid correctly, in terms of the Act and the policies maintained by the Authority (**Policies**), and in a cost effective and timely manner; and
- service levels agreed with the scheme administrator are met.

The sustainability of the Business System, used for administration of the Schemes, is fundamental to achievement of this strategy. The 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 scarce. While the current Business System is stable, and the Authority is confident it will perform adequately in the short term, the Authority is developing a new Business System, which will be more relevant and sustainable over the longer term.

Also key in achieving the Schemes' outcome (see next page) is the performance of the scheme administrator, Datacom. The Authority has established and maintains a partnering relationship style with Datacom to ensure all issues relating to the administration of the Schemes are communicated early to the Authority and are managed and resolved in an open collaborative manner, taking into account the interests of the members of the schemes and the Crown.

The Actuary appointed by the Authority undertakes actuarial examinations of the Fund on a regular basis. Based on these examinations, the Authority reports to the Crown on the value of the liabilities of the Fund, as required by section 94 of the Act.

In communicating with members and employers, 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 2012/2013

(sections 142(1)(c) and (d) of the Crown Entities Act)

The Authority's key activities in relation to the Schemes are:

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

For 2012/2013 the Authority has identified the following outputs and performance measures to assist in achieving the Schemes' outcome:

- To meet the needs and reasonable expectations of the members and employers as stakeholders.

OUTPUTS	MEASURES
<p>Accurately calculate and pay entitlements, and process contributions correctly and on time, and respond appropriately to stakeholders' inquiries.</p>	<ul style="list-style-type: none"> • Performance is in line with the key performance indicators (KPIs) set out in the Management Agreement between the Authority and scheme administrator. <p>KPIs are:</p> <ul style="list-style-type: none"> - 100% of all annuities are paid on time; - all contributions are banked on receipt and allocated as soon as verified as being correct; - all transactions are processed correctly; - all routine correspondence is responded to within 5 working days; and - all non-routine correspondence is responded to within 7 working days. <p>Performance against the KPIs is measured through monthly reporting by the scheme administrator, monitored by the Authority's schemes management team.</p> <ul style="list-style-type: none"> • The Business System is relevant and supportive of the requirements of the Schemes. • Assessed by: <ul style="list-style-type: none"> - no major loss or corruption of data or functionality; - the ability to access required data from the current and new Business System; and - the new Business System being fully operational by 30 June 2013.
<p>Respond appropriately to stakeholders' inquiries and provide relevant information.</p>	<ul style="list-style-type: none"> • Timely responses to all requests for information from Treasury and meeting deadlines measured by: <ul style="list-style-type: none"> - no requests being received for missing or incomplete information; and - timeframes being met. • Regular updating of website information on Schemes and Investment, sending the annual Chairman's letter to members by the end of September each year and sending member and employer updates. • Achieving consistently good satisfaction scores in the major aspects of the annual survey of members and employers and positive feedback from other stakeholders. • Timely processing of appeals. On receipt of an appeal, complete papers are provided to the Appeals Board at least 14 days before each scheduled hearing.

Overall expected costs (Schemes) \$5.2 million

Note: Overall expected costs (Schemes) include the expected scheme administration expenses, estimated actuarial costs and 30% of the Authority's projected operating expenses (see page 32).

5. 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 strategic decisions relating to the Fund and the Schemes. The Board has all the powers necessary for managing, and for directing or supervising the management of, the business of the GSF.

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

The Authority Board has prepared a Governance Manual and a Corporate Governance Statement. The documents incorporate legislative and regulatory requirements as well as the policies and practices developed by the Board. The Authority's Corporate Governance Statement is available on the 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 Schemes are supported by business planning, business risk assessment, management reporting, and arrangements for audit, internal control and compliance, all conducted on at least an annual basis.
- The Authority reviews, on at least an annual basis, 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 two committees:
 - Audit and Risk Review; and
 - Investmentto perform and exercise the functions and powers of the Board delegated to each committee, as applicable. The committees have written terms of reference and ensure their activities remain consistent with the Crown Entities Act. Each committee reviews its performance annually and their performance is also reviewed by the Board.
- The Board meets at least nine times per annum and ensures that it receives appropriate and reliable reporting on the Fund and the Schemes, and on 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 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 the major external service providers, 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 regularly 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 outsourced model for the key activities of scheme 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 scheme administration functions. At each meeting the Board receives reports from Management on all significant 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 Schemes and the NPF schemes are closed to new members and both organisations have adopted an outsourced model for the major activities of investment, custody and scheme administration. Annuitas allows economies of scale and higher quality resourcing than could be justified if each organisation operated on a stand-alone basis.

The Authority has appointed:

- Datacom as the administrator of the 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 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 and the Policies, must be referred by Datacom to the Authority for 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;
- Specialist management organisations to undertake day to day investment decisions and trading, currency hedging and investment advice; and
- Russell Employee Benefits Pty Ltd to provide specialist actuarial and valuation advice.

ORGANISATIONAL DEVELOPMENT

Board members are appointed for three years and often serve two or more terms.

The Board, through the Chairman, advises the Minister to help ensure an appropriate balance of skills and experience is maintained in the membership of the Board.

The Board generally sets aside a session each year for strategic planning and holds investment workshops from time to time. During the strategic planning session the Board reviews its outcomes, outputs and performance measures (**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 its Objectives. 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 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 Authority's 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 CFIs. A formal collaboration process is in place to facilitate sharing of information and strategies with other CFIs where appropriate, including joint evaluation of investments.

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

A small Management team, reporting to the Chief Executive, is responsible for overseeing the key functions – investment, schemes administration, finance and an over-arching BCP. Back up support is maintained to reduce key person risk. Management is responsible for identifying then implementing appropriate strategies approved by the Board for the Authority to meet its obligations under the Act and to meet the Objectives.

Each year performance objectives and standards are set for each of the key management functions and for senior Management. Progress is monitored regularly and reviewed annually by the Board.

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 Objectives and meet deadlines to the satisfaction of both Boards.

6. 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).
- 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 regard to derivative transactions, the Minister has given approval for the Authority to enter into such transactions where the use is consistent with the SIPSP.

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

REPORTING TO THE MINISTER

The financial statements 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. The Actuary appointed by the Authority calculates the Unfunded Past Service Liabilities for inclusion in the Crown's financial statements.

Treasury, through the Crown Ownership Monitoring Unit (**COMU**), 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. Commentary on the investment activities of the Authority is also included in the Crown's annual Investment Statement.

The Authority has introduced a Reference Portfolio (see page 7) against which the added value (before and after tax and investment management fees) of implementing alternative investment market exposures and the performance of active managers can be measured and reported quarterly. This assists the Authority in ensuring that investment management fees represent the optimal level of fees to meet the Investment Objective.

The Act requires that an independent review must be conducted every five years of how effectively and efficiently the Authority is performing its functions under the Act. The second review was undertaken in the year ended 30 June 2011 by an independent consultant appointed by the Minister. The review considered:

- Whether or not, and how effectively and efficiently the Authority is performing its functions under section 15D of the Act.
- Whether or not the investment policies, standards, and procedures established by the Authority are appropriate to the Fund and have been complied with in all material respects.
- Whether the Authority's operations across all aspects of its organisation are consistent with best practice, in particular whether the level of investment management fees represents the optimal level of fees to meet the Fund's investment objectives and strategies.
- The investment performance of the Fund to date, including an assessment of how the Fund has performed against a passive fund management benchmark.

The report can be viewed at http://treasury.govt.nz/releases/2011_07_28.

The reviewer stated in their report:

- *The Fund's investment objectives and strategy have been developed based on sound principles using a logical and consistent approach. In our view, the policies, standards and procedures developed by the Authority in determining the investment objectives and strategy are appropriate for the Fund.*
- *The policies, standards and procedures used by the Authority to establish the asset allocation mix of the Fund and the approach to portfolio construction for the Fund's investment portfolio and within asset classes are considered and robust. The establishment of a Reference Portfolio as a benchmark makes the Authority's strategy, implemented through the Target Portfolio, quite transparent.*
- *The investment performance of the Fund to date has been satisfactory. The Target (actual) Portfolio has struggled to out-perform the Reference Portfolio over time, but its return profile has been less volatile and has exhibited downside protection characteristics. The Fund's performance in listed asset classes relative to passive market benchmarks has been strong. Whilst the inclusion of 'alternative' investments appears to have detracted value during the strong rebound in equity markets over the past two years, the portfolio construction approach pursued by the Authority has resulted in a reduction in the risk profile of the Fund's returns.*
- *The Fund's overall investment cost level is consistent with meeting the Fund's investment objectives and is in line with that of similarly sized funds with a broadly similar asset allocation mix in the Australian and New Zealand market place.*

In respect of organisation and governance, schemes administration and information and financial management, the reviewer concluded that the Authority is well structured and well managed with appropriate systems in place or under development.

In the report the reviewer made a number of recommendations and suggested enhancements to practices and policies in the operations of the Fund, which have been largely accepted by the Board, and action plans put in place. Implementation of the plans will form a significant part of the Authority's work over the next 1-2 years.

The Authority Board's responses to the comments made by the reviewer in the Executive Summary of the report, and on the recommendations and suggested enhancements, can be viewed on the Authority's website.

7. 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 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.

8. RISK MANAGEMENT

(required under section 141(1)(i) of the Crown Entities Act and section 15N of the Act)

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

INVESTMENT RISKS

RISK	ACTION TO MANAGE
Investment strategy and asset allocation are inappropriate.	<ul style="list-style-type: none"> • Establish clear investment objectives in terms of risk, return and horizon reflected in a Reference Portfolio. • Diversify the risk exposures, assets and management techniques of the Fund. • Seek professional advice on the investment strategy and asset allocation. • Compare the investment strategy and asset allocation with independent surveys. • Peer reviews of advice and regular consultation with other CFIs and large investment funds. • Independent statutory review every 5 years. • Review the SIPSP annually, as required by section 15L of the Act.
Poor performance of active investment managers.	<ul style="list-style-type: none"> • Robust selection process for all investment managers, based on demonstrated ability. • Diversification among strategies and managers where appropriate. • Avoid investment in strategies with low likelihood of adding value. • Mandates for active investment managers with clearly prescribed risk limits. • Regular monitoring and review of manager performance. • Management agreements, which provide for dismissal at the discretion of the Authority.

RISK	ACTION TO MANAGE
Overall investment management risk.	<ul style="list-style-type: none"> • Adoption of a Reference Portfolio that reflects a desired level of risk. • Specific mandate for each investment manager, based on best practice portfolio management. • Constraints to govern credit and liquidity risks. • Regular rebalancing of the Fund to approved risk exposure limits, and use of strategic tilts. • Use of a custodian to hold securities, settle and record transactions, report on performance and monitor compliance of investment managers with mandates. • Operational risk review of commingled investment vehicles, including robust due diligence of managers, and monitoring of their prior and ongoing contractual obligations. • A comprehensive SIPSP developed, reviewed annually and enforced by the Authority. • Clear separation of functions between investment management, custody, and overall supervision. • Appropriate resourcing of the Management team to conduct the oversight function.
Currency risk, for example the risk that the Fund will lose value through adverse exchange rate movements.	<ul style="list-style-type: none"> • Maintaining an overall level of foreign currency risk that is prudent in the context of the total Fund. • Limiting external managers' ability to add currency risk.
The assumed gross pre tax investment returns for each asset class are not achieved.	<ul style="list-style-type: none"> • Adopting a diversified asset allocation for the Fund, reflected in the Reference Portfolio, and governance arrangements that ensure adherence to the strategy through time. • Appointing investment managers based on demonstrated ability, with benchmarks relevant to total portfolio risk. • Shifting asset or risk allocation to avoid losses from extreme market events where asset values are extreme.
Major structural changes to investment markets and/or taxation environment.	<ul style="list-style-type: none"> • Neither of these risks is within the control of the Authority. However, the Authority takes into account changes in these risks in its reviews of the investment strategy and asset allocation.

REPUTATION RISK

RISK	ACTION TO MANAGE
Prejudice to New Zealand's reputation.	<ul style="list-style-type: none"> • Determination of authorised investments (which may include authorised markets) in investment mandates. • Exclusion of direct investment in certain activities that are illegal in New Zealand, contrary to international obligations and/or widely discouraged in New Zealand, such as nuclear weapons, landmines, cluster bombs, tobacco and whaling. • Implementing the Responsible Investment Policies in collaboration with other CFIs and with support from the Guardians of New Zealand Superannuation and the UNPRI. The Authority monitors securities with significant environmental, social and governance (ESG) risks, engages with high risk entities and may exclude those with unacceptable risks. • Encouraging external investment managers to consider ESG factors.
The Authority's reputation risk.	<ul style="list-style-type: none"> • Robust selection process for contracted managers. • Comprehensive management and service level agreements and clearly defined and agreed mandates and reporting standards. • Informing contracted managers of the Authority's Responsible Investment Policies and excluded investments. • 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 Schemes to enable accurate calculation, payment and reporting of members' entitlements. • Clear communication with stakeholders.

SCHEMES RISKS

Liabilities

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

- Movements in the consumer price index (**CPI**) (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 service by contributors, including state sector restructuring and privatisations.
- Patterns of entitlement selection on retirement.
- 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 Actuary to enable preparation of actuarial projections of the liabilities in accordance with the provisions of the Act.

RISK	ACTION TO MANAGE
The provisions of the Act, relating to the Schemes are not complied with and discretions relating to the Schemes are inappropriately applied.	<ul style="list-style-type: none">• Monitoring the performance of Datacom and resolving any issues of interpretation of the Act.• Ensuring all discretionary decisions are exercised in accordance with the Act and the Policies.• Ensuring any changes to the Policies are made only after taking into account the interests of relevant persons, including the Crown, in accordance with the Act.

Administration

The Authority is responsible for the management and administration of the Schemes. Day to day administration duties are carried out by Datacom in accordance with an agreement that expires on 25 April 2013. A new agreement has been negotiated with Datacom for a term through to 31 March 2019.

In administering the Schemes, heavy reliance is placed on the Business System owned by the Authority.

RISK	ACTION TO MANAGE
Poor performance by Datacom.	<ul style="list-style-type: none">• Having a detailed scheme 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 KPIs.• 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.

RISK	ACTION TO MANAGE
Serious information technology problems.	<ul style="list-style-type: none"> • Ensuring any system modifications to the existing Business System are approved by the Authority and that the system is well maintained. • Developing a new and more sustainable Business System (see comment below). • 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.
<i>The Authority is undertaking the development of a new Business System, used for administering the Schemes. It is expected the construction phase of the project will be completed by June 2012 and that the new system will be fully operational by 30 June 2013.</i>	
Transition of data from the old to the new Business System.	<ul style="list-style-type: none"> • Development of a comprehensive transition plan. • Contingency provided in the overall budget.

9. FORECAST FINANCIAL STATEMENTS

FORECAST FINANCIAL STATEMENTS FOR THE YEAR ENDING 30 JUNE 2013

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
- 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
- Statement of accounting policies

GOVERNMENT SUPERANNUATION FUND AUTHORITY

FORECAST INCOME STATEMENT

Estimate 2011/12 \$000		Forecast 2012/13 \$000
26,131	Transfer from the Fund	29,724
<u>25</u>	Other revenue	<u>21</u>
26,156	Total revenue	29,745
3,114	Schemes administration	4,014
19,343	Investment management	21,703
<u>3,699</u>	Operating expenses	<u>4,027</u>
26,156	Total expenses	29,745
<u>-</u>	Net operating result	<u>-</u>

FORECAST BALANCE SHEET

Estimate as at 30 June 2012 \$000		Forecast as at 30 June 2013 \$000
	Tax payers' equity	
<u>-</u>	General funds	<u>-</u>
<u>-</u>	Total tax payers' equity	<u>-</u>
	Represented by	
	Current assets	
180	Cash	160
<u>2,584</u>	Receivables and prepayments	<u>2,450</u>
2,764	Total assets	2,610
	Current liabilities	
<u>2,764</u>	Payables and accruals	<u>2,610</u>
2,764	Total liabilities	2,610
<u>-</u>	Net assets	<u>-</u>

GOVERNMENT SUPERANNUATION FUND AUTHORITY

FORECAST STATEMENT OF CASH FLOWS

Estimate 2011/12 \$000		Forecast 2012/13 \$000
	Cash flows from operating activities	
	<i>Cash was provided from</i>	
27,318	Government Superannuation Fund	30,467
5	Interest	8
20	Other	13
	<i>Cash was disbursed to</i>	
(27,347)	Operating expenses	(30,508)
(4)	Net cash flows from operating activities	(20)
(4)	Net (decrease)/increase in cash held	(20)
184	Opening cash brought forward	180
180	Closing cash balance	160

FORECAST RECONCILIATION OF NET OPERATING RESULT TO NET OPERATING CASH FLOWS

Estimate 2011/12 \$000		Forecast 2012/13 \$000
-	Net operating result	-
	<i>Add/ (less) movements in working capital items</i>	
1,482	Decrease in receivables and prepayments	134
(1,486)	Increase in payables and accruals	(154)
(4)	Net cash flows from operating activities	(20)

GOVERNMENT SUPERANNUATION FUND AUTHORITY

STATEMENT OF ACCOUNTING POLICIES AND SIGNIFICANT ASSUMPTIONS

Reporting entity and statutory base

The Authority was established as a Crown entity by section 15A of the Act. The core business of the Authority is to manage and administer the Fund and the Schemes (see below).

The Fund was established by section 13 of the Act. It consists of various defined benefit superannuation schemes as prescribed in the Act. A separate financial forecast has been prepared for the Fund. Pursuant to section 19H of the Act, the 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, as the primary objective is not to make a financial return, the Authority has designated itself a Public Benefit Entity for the purposes of New Zealand Equivalents to International Financial Reporting Standards (**NZ IFRS**).

Basis of preparation

Statement of compliance

The forecast financial statements have been prepared in accordance with section 142 of the Crown Entities Act 2004, which includes the requirement to comply with New Zealand Generally Accepted Accounting Practice (**NZ GAAP**). The forecast financial statements comply with other applicable Financial Reporting Standards, as appropriate for Public Benefit Entities.

These forecast financial statements have been prepared for the Statement of Intent of the Authority commencing on 1 July 2012 and for the Minister. They are not prepared for any other purpose and should not be relied upon for any other purpose.

Actual financial results achieved for the period are likely to vary from the information presented.

Measurement base

The forecast financial statements are prepared on the historical cost basis.

Functional and presentation currency

The reporting currency of the Authority forecast financial statements is New Zealand dollars and all values are rounded to the nearest thousand dollars (\$000). The functional currency of the Authority is New Zealand dollars.

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.

b. Revenue and expenses

Revenue and expenses are recognised on an accrual basis.

Revenue is measured at the fair value of consideration received/or receivable.

Revenue from the Fund is recognised as earned and reported in the financial period to which it relates.

Expenses paid in foreign currency are recorded at the rates of exchange prevailing at the date of the transactions and there are no currency gains or losses.

c. Goods and Services Tax

The Authority makes principally exempt supplies for Goods and Services Tax (GST), as it manages superannuation schemes. GST is 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 undertaken overseas. GST on services is not reclaimable and GST is therefore included in expenditure.

d. Statement of Cash Flows

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

e. Taxation

As a Public Authority, in terms of section CW 38(2) of the Income Tax Act 2007, the Authority is exempt from income tax.

f. Accounting for Joint Ventures

The Authority has a 50% ownership in Annuitas. Staff employed by Annuitas act in management 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.

Changes in accounting policies

All policies have been applied on bases consistent with those used in the year ended 30 June 2011.

Investment management expenses

Investment management fees (including custody costs) are forecast to increase from the estimate of \$19.34 million in 2012 to a forecast of \$21.70 million in 2013. This is primarily due to an increase in forecast investment performance fees.

Schemes administration expenses

The forecast schemes administration expenses include reimbursement to the Fund for amortised expenditure on the Business System owned by the Fund.

Recovery of expenses

The forecast expenses of the Authority, for the management and administration of the Fund and the Schemes for the 2012/2013 year, are \$29.74 million. These expenses, net of other revenue of \$0.02 million are recovered from the Fund in accordance with section 15E of the Act.

The Fund then recovers payments made to the Authority (forecast \$29.72 million), partly from the Crown, under a Permanent Legislative Authority (**PLA**), and partly from non Government employer contributions.

The payments to the Authority by the Fund are recovered from the Crown and from non Government employer contributions in proportions determined by the Government Actuary. The Fund currently recovers 80.0% of the payments to the Authority from the Crown and 20.0% from non Government employer contributions. The Government Actuary has determined that, from 1 July 2012, the Crown's share will be 79% (forecast \$23.48 million) and the share to be met from the non Government employer contributions 21% (forecast \$6.24 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 Schemes, including the agreement between the Authority and the scheme administrator.
- Interpretation of the provisions of the Act and the Policies 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 INCOME STATEMENT

Estimate 2011/12 \$000		Forecast 2012/13 \$000
	Increase in assets from:	
33,320	Investing activities	243,000
	Operating activities	
26,131	Operating revenue	29,724
(26,131)	Funding the Authority	(29,724)
33,320	Surplus before tax and membership activities	243,000
(40,481)	Tax	(41,205)
(7,161)	(Deficit)/surplus after tax and before membership activities	201,795
	Membership activities	
705,000	Contributions - Crown	700,000
50,000	Contributions - members	44,000
25,000	Contributions - other entities	20,000
(906,000)	Benefits paid	(895,000)
(126,000)	Net membership activities	(131,000)
(133,161)	(Deficit)/surplus after tax and after membership activities	70,795
3,159,158	Opening assets available to pay benefits	3,025,997
3,025,997	Net assets available to pay benefits	3,096,792



GOVERNMENT SUPERANNUATION FUND

FORECAST BALANCE SHEET

Estimate as at 30 June 2012 \$000		Forecast as at 30 June 2013 \$000
3,037,045	Investments	3,198,632
	Other assets	
135,943	Cash and cash equivalents	170,645
68,126	Receivables and prepayments	66,815
204,069		237,460
3,241,114	Total assets	3,436,092
	Less	
211,589	Other payables	336,332
3,528	Benefits accrued	2,968
215,117		339,300
3,025,997	Net assets available to pay benefits	3,096,792
	Estimated actuarial present value of Promised Retirement Benefits	
12,187,000	Gross liability	12,096,000
9,161,003	Deficit	8,999,208
3,025,997	Net assets available to pay benefits	3,096,792

Note – Deficit

- The estimated 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 was calculated by the Government Actuary using a net discount rate.
- The Deficit shown in the Forecast Balance Sheet differs slightly from that calculated by the Government Actuary in his actuarial valuation of the Fund, as at 30 June 2011, under NZ IAS 26, dated August 2011. The Government Actuary projected a higher value for the assets of the Fund compared with the forecast made by the Authority.
- The position of Government Actuary was disestablished in 2011. An Actuary appointed by the Authority will calculate the gross liabilities from 30 June 2012. The Actuary has already indicated that she will allow for continued improvements in mortality (eg. annuitants are living longer) which will increase the gross liabilities and consequently the deficits. The Authority estimates, based on calculations prepared by the Actuary for the Crown, that the improved mortality may add \$1 billion to the gross liabilities.
- There is no requirement on the Crown to fully fund the Deficit in relation to the Schemes. Reliance is placed by the Authority on the provisions of section 95 of the Act which requires the Minister to appropriate funds from public money to ensure that sufficient funds are available, or will be available, to pay entitlements as they fall due.

GOVERNMENT SUPERANNUATION FUND

FORECAST STATEMENT OF CASH FLOWS

Estimate 2011/12 \$000		Forecast 2012/13 \$000
	Cash flows from operating activities	
	<i>Cash was provided from</i>	
675,719	Contributions - Crown	723,213
48,009	Contributions - members	44,110
30,065	Contributions - other entities	26,227
79,827	Interest	81,039
	<i>Cash was disbursed to</i>	
(861,858)	Benefits payments	(895,570)
(65,523)	Income tax	(41,835)
(27,318)	Operating expenses	(30,467)
(121,079)	Net cash outflows from operating activities	(93,283)
	Cash flows from investing activities	
	<i>Cash was provided from</i>	
5,497,422	Maturities and sales of investment assets	4,237,558
	<i>Cash was disbursed to</i>	
(5,402,086)	Purchase of investment assets	(4,109,573)
95,336	Net cash inflows from investing activities	127,985
(25,743)	Net (decrease)/increase in cash held	34,702
161,686	Opening cash brought forward	135,943
135,943	Closing cash balance	170,645



GOVERNMENT SUPERANNUATION FUND

FORECAST RECONCILIATION OF NET CHANGES IN NET ASSETS TO NET OPERATING CASH FLOWS

Estimate 2011/12 \$000		Forecast 2012/13 \$000
(133,161)	Net (decrease)/increase in net assets	70,795
	<i>Add/ (less) movements in working capital items</i>	
50,971	Decrease in receivables and prepayments	1,926
(20,780)	(Decrease) in other payables	(28,243)
1,100	Increase/(decrease) in benefits accrued	(560)
31,291		(26,877)
	<i>Add/ (less) items classified as investing activities</i>	
142	Decrease in accrued interest portion of fixed interest securities	793
43,490	Increase/(decrease) in net market values of investment assets	(163,700)
(7,302)	Decrease in investment receivables	(1,899)
(55,539)	(Decrease)/increase in investment payables	27,605
(19,209)		(137,201)
(121,079)	Net cash outflows from operating activities	(93,283)

GOVERNMENT SUPERANNUATION FUND

STATEMENT OF ACCOUNTING POLICIES

Reporting entity and statutory base

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

The Fund is managed by 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.

As the primary objective of the Fund is to make a financial return, the Authority has determined the Fund is a profit oriented entity for the purposes of New Zealand equivalents to International Financial Reporting Standards (**NZ IFRS**).

Basis of preparation

Statement of Compliance

The forecast financial statements meet the requirements of section 15N of the Act and comply with New Zealand Generally Accepted Accounting Practice (**NZ GAAP**).

The forecast financial statements also comply with New Zealand equivalents to NZ IFRS, and other applicable Financial Reporting Standards, as appropriate for profit oriented entities. Compliance with NZ IFRS ensures that the financial statements comply with International Financial Reporting Standards (**IFRS**).

These forecast financial statements have been prepared for the Statement of Intent of the Authority commencing on 1 July 2012 and for the Minister. They are not prepared for any other purpose and should not be relied upon for any other purpose.

Actual financial results achieved for the period covered are likely to vary from the information presented, and the variations may be material.

Measurement Base

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.

Functional and presentation currency

The reporting currency of the Fund is New Zealand dollars. All values are rounded to the nearest thousand dollars (\$000). The functional currency of the Fund is New Zealand dollars.



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 *NZ IAS 26: Accounting and Reporting by Retirement Benefit Plans*, 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. Promised retirement benefits

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. Receivables

Receivables are carried at amortised cost.

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 as the difference between the asset's carrying amount and the present value of the recoverable amount.

f. Other assets

Other assets include capitalised expenditure on the Business System. The Business System will be amortised over seven years from completion (expected to be in the year ended 30 June 2013). Amortisation will be recovered from the Authority as the user of the Business System.

g. 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 (including those arising on translation of foreign currencies), 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.

h. 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.

i. 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.

Entitlements are recognised in the Income Statement when they become payable.

j. Taxation

For tax purposes, the Fund is classified as a portfolio investment entity (**PIE**).

Income taxation expense includes both the current year's provision and the income tax effects of temporary differences (if any).

Since the Fund became a PIE there have been no temporary differences.

The Fund is not registered for Goods and Services Tax.

k. Statement of Cash Flows

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

- 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. All balances have an original maturity of less than three months.
- 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.
- Operating activities include all transactions and other events that are not investing or financing activities.

l. Consolidation

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

Changes in accounting policies

There are no significant changes in accounting policies.





GOVERNMENT
SUPERANNUATION FUND
AUTHORITY