Pūrongo Taupua a te Rōpū Kaunihera o Tāmaki Makaurau

31 o Hakihea 2020

Auckland Council Group Interim Report

31 December 2020

Auckland Council

Te Kaunihera o Tāmaki Makaurau

Mihi

Noho mai rā Tāmaki Makaurau,
moana waipiata,
maunga kākāriki.
Mai i ngā wai kaukau o ngā tūpuna,
ki ngā puke kawe i ngā reo o te tini,
i puta ai te kī mōu.
Tū ana he maunga,
takoto ana he raorao,
heke ana he awaawa.
Ko ō wahapū te ataahua,
ō tāhuna te mahora,
te taiao e whītiki nei i a koe he taonga tuku iho.
Tiakina kia meinga tonu ai koe
ko 'te tāone taioreore nui o te ao,
manakohia e te iwi pūmanawa'.
Tāmaki Mākaurau tirohia te pae tawhiti
he whakairinga tūmanako
mō ngā uri whakaheke ō āpōpō,
te toka herenga mō te hunga ka takahi ake
mā ō tomokanga,
te piriti e whakawhiti ai
tō iwi ki ngā huarahi o te ora.
Tāmaki Mākaurau e toro whakamua,
hīkina te mānuka.
Tērā te rangi me te whenua te tūtaki.
Maranga me te rā, he mahi māu me tīmata,
ka nunumi ana ki te pō,
whakatārewahia ō moemoeā ki ngā whetū.
Ko te oranga mutunga mōu
kei tua i te taumata moana.
Tūwherahia ō ringa, kūmea mai ki tō uma.
Tāmaki Makaurau
he tāone ūmanga kurupounamu koe;
tukua tō rongo kia rere i te ao.

Tāmaki Makaurau
who bestrides shimmering seas,
and verdant mountains.
From the bathing waters of our forebears,
and hills that echo with voices
that acclaim.
Your mountains stand lofty,
your valleys spread from them
and your streams run freely.
Your harbours are majestic,
your beaches widespread,
the environment that surrounds you is a legacy.
Take care of it so that you will always be known
as 'the world-class city
where talent wants to be'.
Tāmaki Makaurau looking to the future,
repository of our hopes
for generations to come,
anchor stone for those who venture
through your gateway,
and the bridge that connects
your citizens to life.
Tāmaki Makaurau moving on,
accepting all challenges.
Where even heaven and earth might meet.
Rise with the sun as there is work to be done
and when evening comes,
allow your dreams to glide among the stars.
Perpetual health and growth
is beyond the horizon of cresting waves.
Open your arms and pull them to your embrace.
Tāmaki Makaurau, you are a city
where valued business and enterprise thrives;
let your good name traverse the world.

On the cover: Magazine Bay Wharf, Maraetai.

Ngā Upoko Kōrero

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He karere nā te koromātua

Message from the Mayor

Auckland Council Group continues to respond to the financial impact of COVID-19 while maintaining the critical investments in transport, environmental and housing infrastructure that Auckland needs to be a world-class city.

Phil Goff helping at food distribution centre.

While the economic impact of COVID-19 has been less damaging than was feared at the start of the pandemic, the financial effect on the group is predicted to be around $1 billion by 2024. This is compounded by a requirement for $224 million of investment required to boost water supply in response to last year's drought, the worst the region has ever experienced.

In addition, the long-term outlook remains highly uncertain. Auckland is the main entry point for returning New Zealanders, putting it at heightened risk of further outbreaks and potential lockdowns, and new, more infectious strains of the virus increase the chances of an incursion into the community.

Given this uncertainty, and the necessity to continue delivering infrastructure to support Auckland's growth, the group has taken a prudent and responsible approach to financial management, controlling costs, pursuing efficiencies, reducing staff costs and cutting budgets for non-essential spending.

This strong financial management along with funding support from central government enabled the group to proceed with $1.2 billion of capital investment in the six months to 31 December 2020. This included $568 million in transport projects, and $376 million for water and wastewater, reflecting our increased investment to address the drought.

We have achieved $105 million in savings in the six months to December 2020, against a target of $120 million over the full financial year. Going forward, we plan to lock in $90 million a year of these savings permanently in the upcoming 10-year Budget. Staff costs across the group for the six months to 31 December 2020 were $23 million lower than for the same period a year earlier, and the group is becoming a leaner and more adaptable organisation.

We have maintained the essential services that Aucklanders rely on, such as transport, parks and playgrounds, community facilities, waste and recycling services, and libraries. The Emergency Budget reinstated $450,000 in funding to ensure that libraries could continue to operate at full opening hours; retained full discretionary operational funding for Auckland's local boards, enabling key local community projects to continue; and restored transport investment by $40 million, including safety funding such as for upgrading dangerous intersections.

The budgeted $224 million of additional investment in new water infrastructure will increase water capacity; alongside water savings efforts by Aucklanders and an increased take from the Waikato River. This has allowed us to ease the severity of water restrictions and has helped to improve the resilience of our long-term water supply.

General rates increases have been kept to the agreed level of 3.5 per cent on average, which has allowed us to protect the services and investments Aucklanders rely on, such as libraries, and continue to invest in important environmental projects and critical infrastructure.

Our continued prudent approach to managing debt and finances is reflected in the retention of our AA and Aa2 ratings from S&P Global and Moody's respectively in 2020, both with a 'stable' outlook. Despite the headwinds caused by COVID-19 we will maintain our prudent approach to ensure value for money for ratepayers and the efficient running of our city.

The COVID-19 crisis has created one of the most difficult financial challenges that the group has faced. The still-present risk of potential incursions of the virus into the community, the continued closure of the international border and the spread of new variants of the disease overseas contribute to ongoing uncertainty.

In response, the group continues to take a prudent and responsible approach to financial management, with the aim of protecting against future shocks and maintaining our ability to continue investing in the infrastructure, services and facilities we need to be a world-class city.

Hon Phil Goff
Mayor of Auckland
25 February 2021

He karere nā te tumu whakarae

Message from the Chief Executive


Jim Stabback

Managing the effects of both COVID-19 and one of the most severe droughts in Auckland's history make the challenges we face in the current financial year unprecedented. This interim report to 31 December 2020 demonstrates that we are dealing with these challenges in a prudent and responsible manner whilst playing our part in the recovery of our communities and region. We have reacted well to the immediate challenges we face however we have an obligation to Aucklanders to look at both the immediate and longer-term impacts and opportunities.

COVID-19 and border restrictions continue to impact group revenue, particularly fees and user charges. Compared to the same period a year earlier, public transport, parking and infringement revenues decreased by $54 million and, events and shows and conferences revenue was $12 million lower.

The drought has continued to affect financial performance of the group. Due to water restrictions, revenue from water and wastewater charges was $13 million less than the comparative period in the prior year. This is coupled with an increase in costs. In total, Watercare spent $12 million more on operating expenditure to increase the city's water supply and purchasing additional safety equipment required in the COVID-19 environment.

A large degree of uncertainty still remains requiring ongoing careful and prudent management of our finances for the foreseeable future. We need to carefully consider the changing needs of our communities and customers, so we serve Aucklanders effectively and efficiently now and in the future. This may mean we reshape services to better meet their needs.

Developer activity has rebounded well since the March 2020 COVID-19 lockdown, reflected in an increase of $37 million in infrastructure growth charges and a $40 million increase in development contributions, compared with the six months to 30 December 2019. This, together with the $39 million income from the central government's 'shovel ready' funding are promising signs of confidence in our region's recovery.

Our investment in infrastructure matched that of the same period in 2019. Group capital investment was $1.2 billion for the six-month period. This included $376 million for water supply and wastewater treatment and $568 million for roads, footpaths and public transport. The majority of water supply and wastewater treatment capital expenditure was in direct response to the drought including $57 million on sourcing water from the Waikato River and an additional $28 million on securing water supply from Hays Creek.

Our focus remains supporting our region's growth and keeping Auckland moving. We spent an additional $114 million on roads and footpaths, $29 million was spent on new energy efficient trains and $5 million on the Wynyard Quarter road programme. Continuing our infrastructure programme is a critical part of economic recovery and supporting employment.

From a group financial performance perspective, our key results are an operating surplus of $1,399 million, $50 million more than the same period last year. Revenue of $3,592 million was $98 million more than the same period last year. Total net group debt increased by $223 million to $10.1 billion against the backdrop of total assets increasing over the period by $2.2 billion to $58.2 billion.

Looking ahead, we acknowledge that COVID-19 will continue to impact us and we need to keep working towards recovery and to stimulate and support critical investment in regional transport, housing, community, water quality and the environment. Over the next three years, we will continue to work with central government and partners identifying co-funding projects and finding new ways to finance critical infrastructure.

Throughout, our focus remains on providing the services Aucklanders value and rely on, in the most effective and efficient way possible. This includes a continued focus on value for money for ratepayers and meeting our efficiency savings of $120 million by 30 June 2021.

He waka eke noa. We are all in this together.

Jim Stabback
Chief Executive
25 February 2021

Tirohanga mō te pāinga ā moni

Financial performance overview

Hobson Bay walkway.

Tirohanga mō te päinga ā moni

Financial performance overview

The Auckland Council Group's (the group) unaudited results reflect a positive start to the recovery from the COVID-19 pandemic. We remain cautiously optimistic about the remainder of the financial year despite the continuing impacts of the pandemic, as evidenced by our recent move back into lockdown at Alert Level 3. While the severity, duration and long-term implications of the pandemic continue to be highly uncertain, we remain strongly committed to being fiscally responsible by managing our finances prudently. This financial management approach will ensure we can continue to deliver community services and infrastructure that Aucklanders expect.

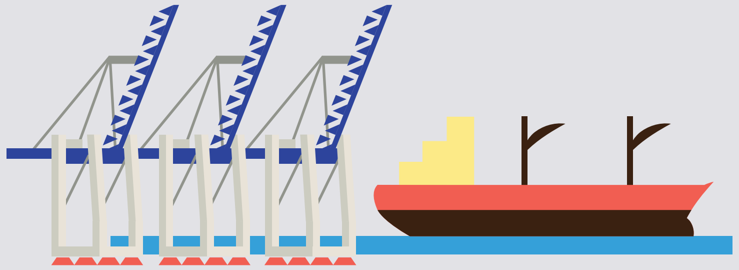
Our financial performance compared to the same period last year

In July 2020, the group adopted an Emergency Budget for 2020/2021 with a projected reduction in cash operating revenue of around $450 million compared to pre-COVID-19 projections. This Emergency Budget included a number of mitigations to enable relatively high levels of capital investment in Auckland to continue while maintaining the group's strong commitment to long-term financial prudence. These mitigations included:

- reductions in planned operating expenditure,
- deferral of some non-critical capital investment,
- increased targets for the disposal or lease of non-strategic property assets,
- maintaining a planned 3.5 per cent average rates increase, and
- additional funding support from central government.

For the six months to 31 December 2020, the group's overall revenue and operating surplus both increased compared to the same period for the prior year, but not to the extent previously planned pre-COVID-19. These increases were supported by movements in capital revenue and non-cash items that are not directly related to the group's key performance indicators and debt constraints.

The group generated an operating surplus before gains and losses of $1,399 million for the first six months to 31 December 2020, an increase of $50 million or 3.7% on the same period last year. The surplus reflects strong revenue growth particularly in revenue related to property development. Our commitment to post-COVID-19 recovery meant there was a strong focus on containing or decreasing costs where possible. However, a number of uncontrollable costs such as the provision for weathertightness and associated building defect claims have negatively affected our result. Details of changes in revenue and expenses compared to the prior year are as follows:



Revenue

The group's revenue of $3,592 million was $98 million higher than the comparative period in the prior year. Despite this, the group's cash operating revenue is lower than pre-COVID-19 projections for public transport, regulatory revenue, revenue from events, shows and stadia, ports revenue and dividends from Auckland International Airport Limited (AIAL). This has been exacerbated by the drought and associated water restrictions.

The most notable increases in revenue came from the following:

- The region had a 1.9% growth in the rating base, and that in addition to the 3.5% rates increase accounts for most of the $102 million increase in rates revenue.
- Development activity in Auckland picked up significantly following the first COVID-19 lockdown in 2020, which has resulted in an increase in development contributions and water infrastructure growth charges of $40 million and $36 million, respectively.
- Central Government-funded Shovel Ready initiatives are underway, providing the group with $39 million of capital subsidies during the period. In addition to Waka Kotahi NZ Transport Agency's operating subsidies, the group continued to receive top-ups of public transport revenue shortfalls because of COVID-19, which resulted in increased operating subsidies of $49 million compared to the prior half-year.

These increases were offset by the following:

- Vested assets revenue was $73 million less than the prior year comparative period. Vested assets are driven by the timing of completion of residential developments.
- Public transport, parking revenue and infringement revenues decreased by $54 million due to the lockdown period and changes to the way people work and safety concerns following COVID-19 lockdown. This loss was partly offset by subsidies from Waka Kotahi NZ Transport Agency (see above).
- There was a $13 million decrease in water and wastewater revenue due to water restrictions in response to the drought.
- Revenue from shows, events and conferences was $12 million less due to social distancing measures and the inability to secure overseas performers.
- Revenue from port operations decreased by $10 million due to stevedore shortages and capacity issues in the automation project.

Expenditure

Our commitment to post-COVID-19 recovery meant there was a strong focus on containing or decreasing costs where possible, however a number of uncontrollable costs have negatively impacted on our results.

Expenditure was $48 million higher than the comparative period in the prior year. The largest increases were in the following areas:

- The provision for weathertightness and associated building defect claims increased by $52 million as a result of an assessment of the assumptions around possible cost increases in the quantum of multi-unit claims as well as the percentage of claims the group may have to pay under the legal principle of joint and several liability.
- The provision for contaminated land and closed landfills increased by $7 million to reflect revised estimates for managing Greenmount Landfill.
- The cost of running and maintaining water and wastewater treatment plants and disposal systems increased by $12 million as more water was pumped from the Waikato River, and health and safety measures had to be increased in light of the COVID-19 pandemic.
- Depreciation and amortisation expense increased by $33 million due to increased capitalisation of assets delivered by the group's significant capital programme.

These increases were partly offset by the following:

- Employee benefit expenditure decreased by $23 million as we focused on better resourcing according to group needs.

- Finance costs decreased by $17 million, which was mainly due to the early close-out of the group's basis swaps. The group's Emergency Budget 2020/2021 included a savings target of $120 million to address funding shortfalls caused by COVID-19. One of the savings initiatives was to close out the group's basis swaps. They were closed out between September and November 2020, delivering a realised gain of $19 million. The associated underlying borrowings remain hedged through cross currency interest rates swaps and as a result, there was little effect on the group's exposure to interest rate risk.

Net other gains and losses

Net gains were $274 million higher than the comparative period in the prior year which is mainly attributable to unrealised gains from financial assets. The group actively manages its interest rate exposure to provide certainty over interest costs in the medium and long-term through derivatives. Derivatives were valued based on market interest rates and foreign exchange rates as at 31 December 2020. As a result of the movement in interest rates and foreign exchange rates between 30 June 2020 and 31 December 2020, an unrealised gain of $88 million has been recognised in net other gains and losses relating to its derivatives portfolio. The increase in derivative financial instruments was $245 million more than the prior year.

Our financial position compared to 30 June 2020

The group increased its net asset position by $1,879 million from 30 June 2020, to $41,728 million. Most of the increase arose from the increase in assets, mainly receivables and prepayments, other financial assets, property, plant and equipment, and our investment in joint ventures and associates. The increase was partly offset by the increase in net borrowings.

Receivables and prepayments

Rates revenue is recognised in full when annual rates notices are issued at the beginning of the financial year. This saw rates receivable rise from $1,006 million to $1,092 million.

Other financial assets

Other financial assets include the group's investment in AIAL which is held at fair value. AIAL's share price rose 15% in the six months to 31 December 2020, which accounts for the majority of the $265 million increase in listed shares.

Property, plant and equipment

Climate change and the drought accelerated our investment in water infrastructure to secure our future water supply. Watercare increased its spend in water supply assets by $96m to $200 million. This included $57 million on sourcing water from the Waikato River, and $28 million on securing water supply from Hays Creek.

The group continued to invest in critical roading infrastructure to keep Auckland moving safely, spending $341 million on roads and footpaths, an additional $114 million compared to the same period last year. We spent $29 million on new energy efficient trains and $5 million on the Wynyard Quarter roading programme.

Net borrowings

Net borrowings (net of cash and cash equivalents) increased by $223 million to $10,142 million during the six months to 31 December 2020. The increase includes a $500 million domestic green bond issuance, and $550 million in new borrowings from the Local Government Funding Agency. This increase is partly offset by repayments of matured debt, and an increase of $300 million in cash holdings.

Our cash flows compared to the same period last year

During the six months to 31 December 2020, management took a cautionary approach to liquidity management because of the uncertainty posed by the ongoing COVID-19 pandemic. Measures adopted included increasing cash holdings and pre-funding capital expenditure. As noted in Net borrowings above, the overall effect was an increase in debt as well as cash balances.

Cash inflows from operating activities

Our increased revenue receipts, along with cost containment have increased operating cash flows of $116 million.

Cash outflows from investing activities

Outflows from investing activities decreased by $200 million mainly as a result of a $78 million increase in proceeds from the sale of assets, and a $95 million decrease in fixed term deposits of surplus cash funds..

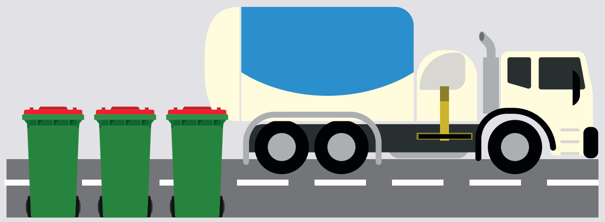
Cash inflows from financing activities

Pre-funding of capital expenditure resulted in an increase in financing activities of $107 million.

Looking ahead

COVID-19 has created challenges and is expected to reduce the group's income by $450 million this year, with cumulative losses projected to reach around $1 billion by 2024. The potential for further COVID-19 disruptions from the new, more transmissible strains of coronavirus and a consequential decline in economic conditions presents additional risk to the group's finances as well as operations.

The group is responding to this challenge in its upcoming 10-year Budget 2021-2031 – our Recovery Budget. The proposed Recovery Budget will increase total capital investment in our city from $26 billion to $31 billion over the next 10 years and will support operational expenditure of $55 billion to maintain and operate community assets such as museums, libraries, the zoo, parks, playgrounds, sports facilities, rubbish collections, recycling, roading and public transport. It positions Auckland to recover strongly from COVID-19 and continue moving towards fulfilling our role as New Zealand's world-class, globally competitive and inclusive city.



Tauāki ā-moni whiwhi, ā-whakapaunga pūtea

Statement of comprehensive revenue and expenditure

For the six months ended 31 December 2020

$Million	Note	Unaudited 6 months to 31 Dec 2020	Unaudited 6 months to 31 Dec 2019	Audited 12 months to 30 Jun 2020
Revenue				
Rates	A1	1,973	1,871	1,877
Fees and user charges		636	725	1,316
Grants and subsidies		409	341	821
Development and financial contributions		108	68	156
Other revenue		305	251	494
Vested assets		158	231	494
Finance revenue measured using effective interest method		3	7	9
Other finance revenue		-	-	1
Total revenue excluding other gains		3,592	3,494	5,168
Expenditure				
Employee benefits		479	502	997
Depreciation and amortisation		497	464	963
Grants, contributions and sponsorship		113	112	148
Other operating expenses		904	850	1,864
Finance costs		200	217	444
Total expenditure excluding other losses		2,193	2,145	4,416
Operating surplus before gains and losses		1,399	1,349	752
Net other gains/(losses)	A2	233	(41)	(628)
Share of surplus/(deficit) in associates and joint ventures		(4)	25	(15)
Surplus before income tax		1,628	1,333	109
Income tax expense		16	17	74
Surplus after income tax		1,612	1,316	35
Other comprehensive revenue/(expenditure)				
Net gain on revaluation of property, plant and equipment		-	-	731
Share of associates and joint ventures reserves		-	(2)	(146)
Reclassification of share of associates reserves		-	-	21
Fair value movement on revaluation of financial assets held at fair value through other comprehensive revenue and expenditure		265	14	164
Movement in cash flow hedge reserve		3	1	-
Tax movement in cash flow hedge reserve		(1)	-	-
Deferred tax written back to revaluation reserve on asset transfer		-	-	2
Total other comprehensive revenue		267	13	772
Total comprehensive revenue		1,879	1,329	807

The accompanying notes to the financial statements form part of, and are to be read in conjunction with, these financial statements.

Tauāki mō te tūāhua tahua pūtea

Statement of financial position

As at 31 December 2020

$Million	Note	Unaudited 6 months to 31 Dec 2020	Unaudited 6 months to 31 Dec 2019	Audited 12 months to 30 Jun 2020
Assets				
Current assets				
Cash and cash equivalents		598	173	298
Receivables and prepayments		1,573	1,425	543
Derivative financial instruments	B5	3	5	6
Other financial assets	B2	110	175	88
Inventories		54	49	58
Income tax receivable		2	-	3
Non-current assets held-for-sale		17	2	127
Total current assets		2,357	1,829	1,123
Non-current assets				
Receivables and prepayments		56	56	58
Derivative financial instruments	B5	490	367	641
Other financial assets	B2	2,167	145	1,890
Property, plant and equipment	B1	51,085	49,040	50,421
Intangible assets		663	665	684
Investment property		628	611	603
Investment in associates and joint ventures		770	1,968	565
Other non-current assets		8	11	6
Total non-current assets		55,867	52,863	54,868
Total assets		58,224	54,692	55,991
Liabilities				
Current liabilities				
Bank overdraft		7	9	3
Payables and accruals		902	876	883
Employee entitlements		96	95	127
Borrowings	B4	683	999	1,093
Derivative financial instruments	B5	3	12	5
Provisions	B3	141	151	99
Total current liabilities		1,832	2,142	2,210
Non-current liabilities				
Payables and accruals		144	116	137
Employee entitlements		5	5	5
Borrowings	B4	10,050	8,379	9,121
Derivative financial instruments	B5	2,472	1,923	2,715
Provisions	B3	439	272	416
Deferred tax liabilities		1,554	1,484	1,538
Total non-current liabilities		14,664	12,179	13,932
Total liabilities		16,496	14,321	16,142
Net assets		41,728	40,371	39,849
Equity				
Contributed equity		26,732	26,732	26,732
Accumulated funds		3,989	3,052	2,451
Reserves		11,007	10,587	10,666
Total equity		41,728	40,371	39,849

The accompanying notes to the financial statements form part of, and are to be read in conjunction with, these financial statements.

Tauāki mō ngā panonitanga o ngā hua uara

Statement of changes in equity

For the six months ended 31 December 2020

1 July 2020 to 31 December 2020 Unaudited $Million	Contributed equity	Accumulated funds	Reserves	Total equity
Balance as at 1 July 2020	26,732	2,451	10,666	39,849
Surplus after income tax	-	1,612	-	1,612
Other comprehensive revenue	-	-	267	267
Total comprehensive revenue	-	1,612	267	1,879
Transfers to/(from) reserves	-	(74)	74	-
Balance as at 31 December 2020	26,732	3,989	11,007	41,728
1 July 2019 to 31 December 2019 Unaudited $Million				
Balance as at 1 July 2019	26,732	1,788	10,522	39,042
Surplus after income tax	-	1,316	-	1,316
Other comprehensive revenue	-	-	13	13
Total comprehensive revenue	-	1,316	13	1,329
Transfers to/(from) reserves	-	(52)	52	-
Balance as at 31 December 2019	26,732	3,052	10,587	40,371
1 July 2019 to 30 June 2020 Audited $Million				
Balance as at 1 July 2019	26,732	1,788	10,522	39,042
Surplus after income tax	-	35	-	35
Other comprehensive revenue	-	-	772	772
Total comprehensive revenue	-	35	772	807
Transfers to/(from) reserves	-	628	(628)	-
Balance as at 30 June 2020	26,732	2,451	10,666	39,849

The accompanying notes to the financial statements form part of, and are to be read in conjunction with, these financial statements.

Tauāki mō ngā moni utu, whiwhinga rānei

Statement of cash flows

For the six months ended 31 December 2020

$Million	Note	Unaudited 6 months to 31 Dec 2020	Unaudited 6 months to 31 Dec 2019	Audited 12 months to 30 Jun 2020
Cash flows from operating activities				
Receipts from rates, grants and other services		2,585	2,465	4,667
Interest received		5	6	14
Dividends received		2	33	34
Payments to suppliers and employees		(1,510)	(1,541)	(2,908)
Income tax refund/(paid)		-	-	1
Interest paid		(220)	(217)	(438)
Net cash inflow from operating activities	C3	862	746	1,370
Cash flows from investing activities				
Proceeds from sale of property, plant and equipment, investment property and intangible assets		146	68	108
Acquisition of property, plant and equipment, investment property and intangible assets		(1,068)	(1,152)	(2,303)
Acquisition of other financial assets		(22)	(117)	(11)
Proceeds from sale of other financial assets		9	21	25
Investment in joint ventures		(210)	(130)	(258)
Advances to external parties		(25)	(60)	(58)
Net cash outflow from investing activities		(1,170)	(1,370)	(2,497)
Cash flows from financing activities				
Proceeds from borrowings		1,411	2,234	4,129
Repayment of borrowings		(789)	(1,716)	(2,966)
Proceeds from derivative financial instruments		26	7	7
Payment for derivative financial instruments		(44)	(28)	(44)
Repayment of finance lease principal		-	-	5
Net cash inflow from financing activities		604	497	1,131
Net increase/(decrease) in cash and cash equivalents and bank overdraft		296	(127)	4
Opening cash and cash equivalents and bank overdraft		295	291	291
Closing cash and cash equivalents and bank overdraft		591	164	295

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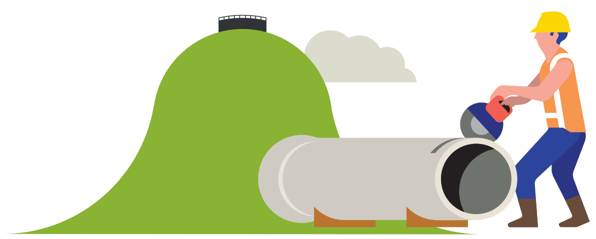


He pito kōrero mō ngā Tauākī Tahua Pūtea

Notes to the Financial Statements

Basis of reporting

Auckland Council (the council) is a local authority domiciled in New Zealand and governed by the following legislation:

- Local Government Act 2002 (LGA 2002);
- Local Government (Auckland Council) Act 2009 (LGACA 2009); and
- Local Government (Rating) Act 2002.

The council is an FMC Reporting Entity under the Financial Markets Conduct Act 2013 (FMCA 2013).

The council's principal address is 135 Albert Street, Auckland Central, New Zealand.

The Auckland Council Group (the group) consists of the council, its subsidiaries, associates and joint ventures. All entities are domiciled in New Zealand.

Significant council-controlled organisations and subsidiaries comprise:

- Auckland Transport
- Auckland Unlimited Limited (previously Auckland Tourism Events and Economic Development Limited and Regional Facilities Auckland Limited)
- Panuku Development Auckland Limited
- Ports of Auckland Limited
- Regional Facilities Auckland
- Watercare Services Limited

The primary objective of the group is to provide services and facilities to the Auckland community for social benefit rather than to make a financial return. Accordingly, the council has designated itself and the group as public benefit entities (PBEs) and applies New Zealand Tier 1 PBE Accounting Standards. These standards are based on International Public Sector Accounting Standards (IPSAS), with amendments for the New Zealand environment.

Statement of compliance

These interim financial statements are for the six months ended 31 December 2020 and have been prepared for the group only and are to be read in conjunction with the annual report for the year ended 30 June 2020. They are prepared in accordance with New Zealand Generally Accepted Accounting Practice (NZ GAAP) and they comply with PBE IAS 34 *Interim Financial Reporting*. The financial results for the six-month period ended 31 December 2020 are unaudited, however they have been subject to a review by the Auditor-General, pursuant to the NZ SRE 2410 (Revised) *Review of Financial Statements Performed by the Independent Auditor of the Entity*.

Basis of preparation

The interim financial statements are presented in New Zealand dollars (NZD), which is the functional currency of each of the group's entities and are rounded to the nearest million dollars unless otherwise stated. All items in the interim financial statements are stated exclusive of Goods and Services Tax (GST), except for receivables and payables which include GST.

The interim financial statements have been prepared on a going concern basis and the accounting policies applied are consistent with those used at 30 June 2020 except as described below.

Basis of reporting (continued)

Change in accounting policy

Change in frequency of revaluations of property, plant and equipment

From 1 July 2020, the group changed its accounting policy to revalue its property, plant and equipment held at fair value, at least every five years. Management takes the view that this change in policy would provide the group with the flexibility to revalue when it is appropriate, or when there is a material movement given the need to manage our finances prudently. The policy has been applied prospectively from the beginning of this financial year because it was not practicable to estimate the effects of applying the policy either retrospectively or prospectively from any earlier date. Accordingly, the adoption of the new policy has no effect on prior periods.

Implementation of new and amended accounting standards by the group

Early adoption of PBE IPSAS 40 *PBE Combinations*

The group adopted PBE IPSAS 40 early. The new standard supersedes PBE IFRS 3 *Business Combinations*. PBE IPSAS 40 has a broader scope than PBE IFRS 3 since it establishes requirements for accounting for both acquisitions and amalgamations. A PBE combination is the bringing together of separate operations into one public benefit entity, which might occur by mutual agreement or by compulsion (for example, by legislation).

<u>Identifying a PBE Combination</u>

PBE IPSAS 40 requires an entity to determine whether a transaction or event is a PBE Combination, which requires that the assets and liabilities constitute an operation. PBE IPSAS 40's definition of an "operation" is similar to the definition of a "business" under PBE IFRS 3, which includes three elements: input, process and output. Similar to PBE IFRS 3, to qualify as an operation, two essential elements are required – inputs and processes applied to those inputs, which together are or will be used to create outputs.

<u>Classification of a PBE Combination</u>

A PBE Combination can be classified as an amalgamation or an acquisition.

An amalgamation is where no party to a PBE combination gains control of one or more operations as a result of the combination or if one party gains control, the economic substance of the PBE combination based on evidence relating to the consideration, the decision-making process and other matters is that of an amalgamation. A "resulting entity" shall account for the amalgamation by applying the modified pooling of interests method.

An acquisition is where one party to a PBE combination gains control of one or more operations as a result of the combination and the economic substance is not that of an amalgamation. The acquisition method of accounting is applied.

The modified pooling of interests method requires recognition and measurement of the assets, liabilities and non-controlling interests at their carrying amounts, recognition and measurement of any other adjustments (e.g. to align accounting policies) within net assets/equity. An amalgamation does not give rise to goodwill.

The acquisition method of accounting is consistent with PBE IFRS 3 and generally requires the recognition and measurement of assets and liabilities at fair value and the recognition of goodwill or gain or loss from acquisition.

Notes to the financial statements

Basis of reporting (continued)

The group adopted this standard early to facilitate the merger of Auckland Tourism Events and Economic Development Limited (ATEED) and Regional Facilities Auckland Limited (RFAL) in order to apply the modified pooling of interests method for amalgamation. The adoption of PBE IPSAS 40 did not result in any significant impact on the group financial statements.

Comparatives

Apart from the matters disclosed below, there has been no other change to balances and disclosures reported in the prior period.

Reclassification within net other gains and losses

In the six months to 31 December 2019, foreign exchange gains on financial instruments held at amortised cost were included in Net gains/(losses) from financial instruments and derivatives. The current presentation of Net other gains and losses in Note A2 provides additional detail to improve the understandability of the nature of the gains and losses. The 31 December 2019 and 30 June 2020 comparatives have been reclassified to reflect current year presentation.

Significant accounting policies

Accounting policies that are considered critical to the portrayal of the group's financial condition and results, and contain judgements, estimates and assumptions about matters that are inherently uncertain have been included in the notes to these interim financial statements. These accounting policies are consistent with those used at 30 June 2020.

Going concern

The group is in a net surplus position of $1,612 million for the six months ended 31 December 2020 (31 December 2019: $1,316 million) and, as of that date, the group had net current assets of $525 million (31 December 2019: net current liabilities of $313 million). The group's debt to revenue ratio is expected to increase to approximately 290% by 30 June 2021 (from 264% in the prior financial year). This exceeds the group's policy limit of 270%. The debt to revenue ratio is expected to return to more prudent and sustainable levels in future financial years as the effects of COVID-19 dissipate. The potential breach of the debt to revenue policy limit has been discussed with S&P Global Ratings and Moody's Investors Services, who continue to monitor the group's financial position.

Management and those charged with governance reviewed the group's financial conditions. The review confirmed that all entities in the group were able to continue as going concerns and were able to realise their assets, and discharge their liabilities, in the ordinary course of business. Accordingly, the use of the going concern assumption is appropriate in the preparation of the financial statements of the group.

As outlined in the 10-year Budget 2018-2028, and each group entity's statement of intent 2020/2021, the council will continue to provide funding to all group entities except Watercare Services Limited and Ports of Auckland Limited, and will maintain its loan facilities with Watercare Services Limited. The boards of both Watercare Services Limited and Ports of Auckland Limited have also confirmed their going concern status.

Impact of the COVID-19 pandemic

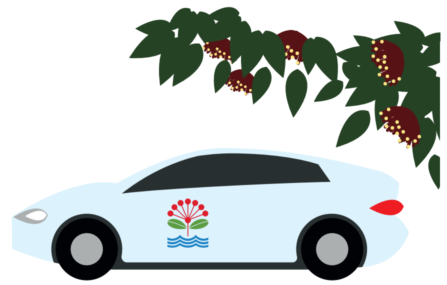
COVID-19 has created challenges for our group as outlined in the Financial Performance Overview. Although revenue has increased compared to the prior year, it has significantly reduced compared to the pre-COVID-19 expectations. The largest impact can be seen in the decrease in fees and user charges compared to the comparative period in the prior year, however the group has received some funding from central government and its agencies to assist with recovery.

Notes to the financial statements

Basis of reporting (continued)

The potential for further COVID-19 disruptions from the new, more transmissible strains of coronavirus and a consequential decline in economic conditions presents additional risk to the group's finances as well as operations. This risk was addressed in the Emergency Budget 2020/2021, and is being considered further in the Recovery Budget (10-Year Plan 2021-2031), with proposed measures including rates increases, the continued sale of surplus properties, ongoing savings initiatives and a moderate increase in borrowings.

At 30 June 2020 the fair value of our revalued property, plant and equipment, as well as investment properties was based on valuations or fair value assessments from independent valuers. Those valuers expressed material valuation uncertainty within their valuation opinions due to COVID-19. The initial COVID-19 lockdown resulted in a lack of comparable sales and there was significant uncertainty as to future increases in the cost of materials and labour. At 31 December 2020, those valuation uncertainties were no longer material.



Notes to the Financial Statements

Section A Financial performance

A1 Rates revenue

Rates are set annually by resolution of the council and relate to a particular financial year in accordance with the Local Government (Rating) Act 2002. Rates comprise general and targeted rates, and are stated net of rates remissions.

Rates revenue is recognised at the date of issuance of ratings notice and is measured at the present value of cash received or receivable.

Sources of revenue are consistent with prior periods.

A2 Net other gains and losses

$Million	Unaudited 6 months to 31 Dec 2020	Unaudited 6 months to 31 Dec 2019	Audited 12 months to 30 Jun 2020
Net gains/(losses) on change in fair value of derivative financial instruments	88	(157)	(665)
Net foreign exchange gains/(losses) recognised in surplus/(deficit) on financial instruments held at amortised cost	105	100	(86)
Other net gains	40	16	123
Total net other gains and losses	233	(41)	(628)

Net gains mainly relate to foreign exchange gains on financial instruments held at amortised cost due to favourable foreign currency movements. They also relate to fair value gains on the group's derivatives which resulted from higher market interest rates in the six months to 31 December 2020.

Notes to the Financial Statements

Section B Financial position

B1 Property, plant and equipment

Accounting policy

The property, plant and equipment of the Auckland Council Group (the group) are classified into three categories:

- Infrastructure assets include land under roads and systems and networks integral to the city's infrastructure. These assets are intended to be maintained indefinitely, even if individual assets or components are replaced or upgraded.
- Operational assets include property, plant and equipment used to provide core council services, either as a community service, for administration, or as a business activity. Other operational assets include landfills, motor vehicles, office equipment, library books and furniture and fittings.
- Restricted assets include property and improvements where the use or transfer of title outside of the group or the council is legally restricted.

<u>Initial recognition and subsequent measurement</u>

Property, plant and equipment is initially recognised at cost, unless acquired through a non-exchange transaction, in which case the asset is recognised at fair value at the date of acquisition. The cost of third party constructed assets generally comprises the sum of costs invoiced by the third party. The cost of self-constructed assets comprises purchase costs, time allocations and excludes, where material, any abnormal costs and internal surpluses.

Subsequent costs that extend or expand the asset's future economic benefits and service potential are capitalised. After initial recognition, certain classes of property, plant and equipment are revalued. Work in progress is recognised at cost less impairment, if any, and is not depreciated.

<u>Useful lives</u>

The useful lives used to calculate the depreciation of property, plant and equipment are as follows:

Asset class	Estimated useful life (years)	Asset class	Estimated useful life (years)
Infrastructure		Operational (continued)	
Land and road formation	Indefinite	Bus stations and shelters	10 to 40
Roads	3 to 110	Marinas	9 to 45
Water and wastewater	10 to 201	Rolling stock	5 to 35
Machinery	3 to 200	Wharves	4 to 100
Storm water	15 to 150	Works of art	Indefinite
Other infrastructure	3 to 80	Other operational assets	1 to 60
Operational		Restricted	
Land	Indefinite	Parks and reserves	Indefinite
Buildings	10 to 100	Buildings	5 to 100
Specialised sporting and cultural venues	3 to 100	Improvements	2 to 50
Train stations	6 to 60	Specified and cultural heritage assets	Indefinite

<u>Disposals</u>

Gains and losses on the disposal of property, plant and equipment are recognised in surplus or deficit. Any amounts included in the asset revaluation reserve in respect of the disposed assets are transferred to accumulated funds on disposal.

Notes to the Financial Statements

Section B Financial position

B1 Property, plant and equipment (continued)

Accounting policy (continued)

Impairment
Property, plant and equipment is reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable.

An impairment loss is recognised in surplus or deficit for the amount by which the carrying amount of property, plant and equipment exceeds its recoverable amount. The recoverable amount is the higher of an asset's fair value less costs to sell and its value in use.

Assets are considered cash generating if their primary objective is to provide a commercial return. The value in use for cash-generating assets is the present value of expected future cash flows.

For non-cash generating assets, value in use is determined using an approach based on a depreciated replacement cost.

Revaluation
Infrastructure assets (except land), restricted assets (except improvements and specified cultural and heritage assets) and operational assets (except other operational assets) are revalued with sufficient regularity, and at least every five years to ensure that their carrying amounts do not differ materially from fair value. The carrying values of revalued assets are assessed at each reporting period to ensure that they do not differ materially from the assets' fair values. If there is a material difference, then those asset classes are revalued. Revaluations are accounted for on an asset class basis.

Net revaluation gains are recognised in other comprehensive revenue and expenditure and are accumulated in the asset revaluation reserve in equity for each class of asset. Revaluation losses that result in a debit balance in an asset class' revaluation reserve are recognised in surplus or deficit. Any subsequent gain on revaluation is recognised first in surplus or deficit up to the amount previously expensed and then recognised in other comprehensive revenue and expenditure.

$Million	Unaudited 6 months to 31 Dec 2020	Unaudited 6 months to 31 Dec 2019	Audited 12 months to 30 Jun 2020
Additions	1,123	1,236	2,593
Net disposals and transfers to non-current assets held-for-sale	(24)	2	(249)
Capital commitments	2,052	2,353	2,158
Share of capital commitments from joint ventures (CRLL)	1,020	871	783

There have been no material changes in fair value for property, plant and equipment between 30 June 2020 and 31 December 2020.

Notes to the Financial Statements

Section B Financial position

B2 Other financial assets

$Million	Unaudited 6 months to 31 Dec 2020	Unaudited 6 months to 31 Dec 2019	Audited 12 months to 30 Jun 2020
Total current other financial assets	110	175	88
Listed shares	2,068	58	1,803
Other non-current other financial assets	99	87	87
Total non-current other financial assets	2,167	145	1,890
Total other financial assets	2,277	320	1,978

B3 Provisions

Accounting policy

Provisions are recognised in the statement of financial position where the group has a present legal or constructive obligation as a result of past events, and where it is probable that an outflow of resources will be required to settle the obligation, and the amount can be estimated reliably.

Provisions are measured at the present value of the expected future cash outflows required to settle the obligation. The increase in the provision due to the passage of time is recognised as a finance cost in surplus or deficit.

Financial guarantees
Financial guarantee contracts are recognised as a financial liability at the time the guarantee is issued. The liability is initially measured at fair value and subsequently at the higher of:

- the amount determined in accordance with the expected credit loss model under PBE IFRS 9 *Financial Instruments*; and
- the amount initially recognised less, where appropriate, the cumulative amount of amortisation recognised in accordance with the principles of PBE IPSAS 9 *Revenue from Exchange Transactions*.

The fair value of financial guarantees is determined based on the present value of the difference in cash flows between the contractual payments required under the debt instrument and the payments that would be required without the guarantee, or the estimated amount that would be payable to a third party for assuming the obligations.

The provision for weathertightness and associated defect claims increased by $53 million which is represented by a $75 million increase in the provision offset against settlements of $22 million.

There have been no other material changes in provisions between 30 June 2020 and 31 December 2020.

Notes to the Financial Statements

Section B Financial position

B4 Borrowings

Accounting policy

Borrowings are initially recognised at face value plus transaction costs and are subsequently measured at amortised cost using the effective interest method.

Foreign currency borrowings are translated into NZD using the spot rates at balance date. Foreign exchange gains and losses resulting from the settlement of borrowings and from translation are recognised in the surplus or deficit.

$Million	Unaudited 6 months to 31 Dec 2020	Unaudited 6 months to 31 Dec 2019	Audited 12 months to 30 Jun 2020
Borrowings	10,733	9,378	10,214
Add bank overdraft	7	9	3
Less cash and cash equivalents	(598)	(173)	(298)
Total borrowings and bank overdraft less cash and cash equivalents	10,142	9,214	9,919

Net borrowings increased by $223 million with a $519 million increase in borrowings partly offset by $296 million in higher cash holdings. The increase in borrowings is largely from a Green Bond issuance and Floating Rate Notes issued between 30 June 2020 and 31 December 2020 which is partially offset by debt maturities during the period.

There were no defaults or breaches on any borrowing arrangement during the period (31 December 2019: nil; 30 June 2020: nil).

B5 Derivative financial instruments

Accounting policy

The group uses derivative financial instruments, such as forward foreign currency contracts and interest rate swaps, to mitigate risks associated with foreign currency and interest rate fluctuations. The group does not hold or issue derivative financial instruments for trading purposes. Derivative financial instruments are initially recognised at fair value on the date on which a derivative contract is entered into and are subsequently remeasured to fair value. Any gains or losses arising from changes in the fair value of derivatives are taken directly to surplus or deficit, except for the effective portion of derivatives designated in cash flow hedges.

Derivatives are carried as assets when their fair value is positive and as liabilities when their fair value is negative.

Derivative assets and derivative liabilities are classified as current when the maturity is 12 months or less from balance date or non-current when the maturity is more than 12 months from balance date.

Cash flow hedges

The effective portion of changes in the fair value of derivatives that are designated and qualified as cash flow hedges are recognised directly in other comprehensive revenue and expenditure. The gain or loss relating to the ineffective portion is recognised immediately in surplus or deficit. On derecognition, amounts accumulated in cash flow hedge reserve are transferred to surplus or deficit.

Notes to the Financial Statements

Section B Financial position

B5 Derivative financial instruments (continued)

Accounting policy (continued)

When a hedging instrument expires or is sold, or when a hedge no longer meets the criteria for hedge accounting, any cumulative gain or loss existing in the cash flow hedge reserve at that time remains in equity and is recognised when the forecast transaction occurs.

The group entered into derivative financial instrument contracts to hedge exposure to fluctuations in interest and foreign exchange rates in accordance with approved financial risk management policies.

Fair value ($Million)	Unaudited As at 31 Dec 2020		Unaudited As at 31 Dec 2019		Audited As at 30 Jun 2020	
	Assets	Liabilities	Assets	Liabilities	Assets	Liabilities
Interest rate swaps						
Cash flow hedge	-	7	-	8	-	11
Fair value through surplus or deficit	73	2,340	54	1,738	83	2,636
Forward foreign currency contracts						
Cash flow hedge	-	-	-	1	-	-
Fair value through surplus or deficit	-	1	-	9	-	3
Cross-currency interest rate swaps						
Fair value through surplus or deficit	420	127	309	179	553	70
Basis swaps						
Fair value through surplus or deficit	-	-	9	-	11	-
Forward rate agreements						
Fair value through surplus or deficit	-	-	-	-	-	-
Total derivative financial instruments	493	2,475	372	1,935	647	2,720

Notional ($Million)	Unaudited As at 31 Dec 2020		Unaudited As at 31 Dec 2019		Audited As at 30 Jun 2020	
	Assets	Liabilities	Assets	Liabilities	Assets	Liabilities
Interest rate swaps	1,534	10,154	1,345	9,989	1,205	10,329
Forward foreign currency contracts	-	26	2	115	6	63
Cross-currency interest rate swaps	2,970	1,606	2,130	2,446	2,970	1,606
Basis swaps	-	-	2,056	-	2,056	-
Forward rate agreements	-	-	-	-	-	200
Total derivative financial instruments	4,504	11,786	5,533	12,550	6,237	12,198

As one of the group's COVID-19 recovery measures, all basis swaps were closed out during the six months to 31 December 2020, giving rise to a gain of $19 million.

Notes to the Financial Statements

Section C Other disclosures

C1 Investment in other entities

Accounting policy

Basis of consolidation
The consolidated financial statements comprise the financial statements of the council and its CCOs and subsidiaries as at 31 December 2020.

CCOs and subsidiaries are entities controlled by the group. Control is achieved when the group has the power to govern their financial and operating policies. In order to establish control, the controlling entity presently has exercisable power to govern decision making to be able to benefit from the activities of the other entity.

Consolidation of a subsidiary begins when the group obtains control over the subsidiary and ceases when the group loses control of the subsidiary. Assets, liabilities, income, and expenses of a subsidiary acquired or disposed of during the year are included in the consolidated statements from the date the group gains control until the date the group ceases to control the subsidiary. The accounting policies of controlled entities are consistent with the policies adopted by the controlling entity, or if not, adjustments are made to the consolidated financial statements to bring alignment of subsidiaries with the group's accounting policies. All intra-group balances, transactions, income, expenses, and cash flows relating to transactions between members of the group are eliminated in full on consolidation.

PBE Combinations involving entities under common control
PBE Combinations involving entities under common control are accounted for by applying the modified pooling of interest method which involves the following:

- the assets and liabilities of the combining entities are reflected at their carrying amounts reported in the combined financial statements of the resulting entity;
- licenses and similar rights granted by one combining operation to another combining operation will not be eliminated and continue to be recognised as an intangible asset;
- tax forgiven as part of the terms of an amalgamation, if any, shall be derecognised prior to amalgamation;
- the resulting entity shall recognise and measure a liability (or asset, if any) related to the combining operations' employee benefit arrangements in accordance with PBE IPSAS 39 *Employee Benefits*;
- no adjustments are made to reflect the fair values on the date of combination, or recognise any new assets or liabilities;
- no additional goodwill is recognised as a result of the combination;
- any difference between the consideration paid/transferred and the equity "acquired" is reflected within the equity as merger reserve; and
- the statement of comprehensive revenue and expenditure reflects the results of the combining entities from the point when the combination took place.

On 27 August 2020, the Auckland Council Governing Body approved the recommendation from the Review of Auckland Council's Council-Controlled Organisations Report to merge Auckland Tourism Events and Economic Development Limited (ATEED) and Regional Facilities Auckland Limited (RFAL).

Regional Facilities Auckland (RFA) is a charitable trust managed by Auckland Unlimited Limited (AUL) (formerly Regional Facilities Auckland Limited), a CCO and corporate trustee appointed by the council.

Notes to the Financial Statements

Section C Other disclosures

C1 Investment in other entities (continued)

In order to preserve the charitable trust status of RFA, the merger was executed by way of a short form amalgamation, merging ATEED into AUL.

On 1 December 2020, ATEED's operation was amalgamated into AUL. The legal status of RFA remained unchanged following the merger. The amalgamation has no financial impact on the group.

C2 Contingencies

Local Government Funding Agency
The group is a shareholder and guarantor of the Local Government Funding Agency (LGFA). The group's cross-guarantee on LGFA's other borrowings was $10.4 billion at 31 December 2020 (30 June 2020: $9.1 billion). The group considers the risk of the LGFA defaulting on repayment of interest or capital to be very low and accordingly the expected credit loss on this guarantee has been assessed as immaterial.

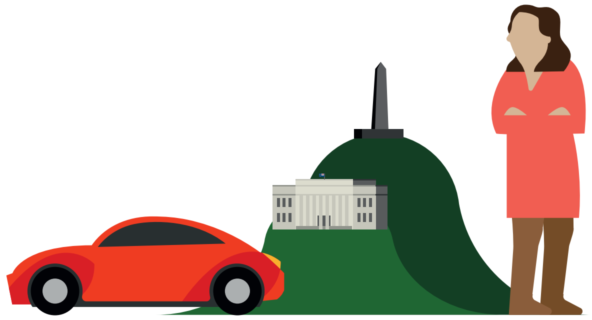
There have been no other material changes in contingencies between 30 June 2020 and 31 December 2020.

C3 Reconciliation of surplus after income tax to net cash inflow from operating activities

$Million	Unaudited 6 months to 31 Dec 2020	Unaudited 6 months to 31 Dec 2019	Audited 12 months to 30 Jun 2020
Surplus after income tax	1,612	1,316	35
Add/(less) non-cash items:			
Depreciation and amortisation	497	464	963
Vested assets	(158)	(231)	(494)
Other non-cash revenue	(238)	48	732
Add/(less) items classified as investing or financing activities	(30)	1	32
Add/(less) movements in working capital items	(821)	(852)	102
Net cash inflow from operating activities	862	746	1,370

C4 Events after the reporting period

There were no material events after the reporting period that would require adjustment or disclosure for the group.



Controller and Auditor-General
Tumuaki o te Mana Arotake

Independent Auditor's Review Report

To the readers of Auckland Council Group's Interim Financial Statements for the six months ended 31 December 2020

I am the auditor of Auckland Council and its subsidiaries (together, the Auckland Council Group). I have used my staff and appointed auditors and their staff to carry out a review of the Auckland Council Group's interim financial statements for the six months ended 31 December 2020 (hereafter the interim financial statements).

Conclusion

I have reviewed the interim financial statements of the Auckland Council Group on pages 14 to 29, which comprise the statement of financial position as at 31 December 2020, and the statement of comprehensive revenue and expenditure, statement of changes in equity and statement of cash flows for the six months ended on that date, and the notes, including a summary of significant accounting policies and other explanatory information.

Based on my review, nothing has come to my attention that causes me to believe that the accompanying Auckland Council Group interim financial statements do not present fairly, in all material respects, the financial position of the Auckland Council Group as at 31 December 2020, and its financial performance and cash flows for the six months ended on that date, in accordance with PBE IAS 34 *Interim Financial Reporting* (Tier 1).

Basis for conclusion

I conducted my review in accordance with NZ SRE 2410 (Revised): *Review of Financial Statements Performed by the Independent Auditor of the Entity*. My responsibilities are further described in the *My Responsibilities for the Review of the Interim Financial Statements* section of my report.

My staff, and appointed auditors and their staff are independent of the Auckland Council Group in accordance with the Auditor-General's ethical requirements relating to the audit of the annual financial statements, which incorporate the relevant independence requirements issued by the New Zealand Auditing and Assurance Standards Board, and I have fulfilled my other ethical responsibilities in accordance with these requirements.

In addition to this review, I and my staff, and appointed auditors and their staff have carried out, or commenced the following engagements in the past year:

- an assurance engagement in respect to the Auckland Council's foreign borrowings programme;
- a limited assurance engagement in respect to the Auckland Council's Debenture Trust Deed and Master Trust Deed reporting certificates;
- the audit of the Auckland Council Group's long-term plan and the related consultation document, as required by the Local Government Act 2002;

- review of service performance audits, as required by s104 of the Auckland Council legislation, on the effectiveness of the Council's post implementation review process and Auckland disaster preparedness and resilience; and
- other engagements for Watercare Services Limited in the areas of cyber and security risk advisory, probity services, quality assurance review on the Central Interceptor project, and limited assurance on selected non-financial information which are compatible with those independence requirements.

These matters have not impaired my independence as auditor of the Auckland Council Group. Other than these engagements, and in exercising my functions and powers under the Public Audit Act 2001 as the auditor of public entities, I have no relationship with, or interests in the Auckland Council Group.

Emphasis of matter – impact of Covid-19

Without modifying my conclusion, I draw attention to the disclosures about the impact of Covid-19 on the Auckland Council Group as set out on pages 20 and 21 of the interim financial statements.

The Council's responsibilities for the interim financial statements

The Council is responsible, on behalf of the Auckland Council Group, for the preparation and fair presentation of these interim financial statements in accordance with PBE IAS 34 *Interim Financial Reporting* (Tier 1).

The Council is responsible for such internal control as it determines is necessary to enable it to prepare interim financial statements that are free from material misstatement, whether due to fraud or error.

My responsibilities for the review of the interim financial statements

My responsibility is to express a conclusion on the interim financial statements based on my review. NZ SRE 2410 (Revised) requires me to conclude whether anything has come to my attention that causes me to believe that the interim financial statements, taken as a whole, are not prepared in all material respects, in accordance with PBE IAS 34 *Interim Financial Reporting* (Tier 1).

A review of the interim financial statements in accordance with NZ SRE 2410 (Revised) is a limited assurance engagement. I perform procedures, consisting of making enquiries, primarily of persons responsible for financial and accounting matters, and applying analytical and other review procedures. The procedures performed in a review are substantially less than those performed in an audit conducted in accordance with International Standards on Auditing (New Zealand) and consequently does not enable me to obtain assurance that I might identify in an audit. Accordingly, I do not express an audit opinion on these interim financial statements.

Greg Schollum
Deputy Auditor-General
Wellington, New Zealand
25 February 2021

Ngā rerekētanga matua o ngā Pae Tikanga Kaute Pūtea a IFRS me PBE

Main differences between IFRS and PBE Accounting Standards

Introduction

Under the New Zealand Accounting Standards Framework, public sector public benefit entities (PBEs) apply PBE Accounting Standards. The New Zealand Accounting Standards Framework defines public benefit entities (PBEs) as reporting entities "whose primary objective is to provide goods or services for community or social benefit and where any equity has been provided with a view to supporting that primary objective rather than for a financial return to equity holders". Many public sector entities are classified as PBEs. The Auckland Council Group (the group) is classified as a public sector PBE for financial reporting purposes and therefore the financial statements of the group have been prepared in accordance with PBE Accounting Standards.

The PBE Accounting Standards are primarily based on International Public Sector Accounting Standards (IPSAS). IPSAS are based on IFRS but are adapted to a public sector context where appropriate, by using more appropriate terminology and additional explanations where required. For example, IPSAS introduces the concept of service potential in addition to economic benefits in the asset recognition rules, and provides more public sector specific guidance where appropriate. This is in contrast with IFRS that are written for the for-profit sector with capital markets in mind.

The key differences in recognition and measurement between PBE Accounting Standards applicable to the group and IFRS (applicable to annual periods beginning on or after 1 July 2020) are set out below. Differences that impact only on presentation and disclosure have not been identified.

PBE Accounting Standards with comparable IFRS equivalent

Formation of Auckland Council Group

PBE

PBE IFRS 3 *Business Combinations* contains a scope exemption for business combinations arising from local authority reorganisations. This scope exemption is carried forward from NZ IFRS 3 (PBE) *Business Combinations*, the standard that was applicable to the group at the time it was formed on 1 November 2010 as a result of the amalgamation of eight predecessor Auckland local authorities.

Under the exemption, all assets and liabilities of the predecessor local authorities were recognised by the group using the predecessor values of those assets and liabilities. The initial value at which those assets and liabilities were recognised by the group is deemed to be their cost for accounting purposes.

IFRS

Without the scope exemption, the amalgamation of the predecessor local authorities into the group would have been accounted for as a business combination under IFRS 3 applying the acquisition method. Under the acquisition method, an acquirer would have been identified and all of the identifiable assets and liabilities acquired would have been recognised at fair value at the date of acquisition.

Impact

The impact of the above accounting treatment is that the carrying value of the assets and liabilities received were not remeasured to fair value and no additional assets and liabilities such as goodwill and contingent liabilities, or a discount on acquisition were recognised as would have been required if the transaction was accounted for as a business combination under IFRS 3.

PBE Accounting Standards with comparable IFRS equivalent (continued)

Business combination

PBE

PBE IPSAS 40 PBE *Combinations* has a broader scope compared to IFRS 3 *Business Combinations*. The scope of PBE IPSAS 40 includes combinations that are acquisitions and combinations that are amalgamations, such as combinations under common control.

Acquisitions are accounted for using the acquisition method consistent with the requirements of IFRS 3.

PBE IPSAS 40 contains additional guidance on the accounting for amalgamations. Amalgamations are accounted for using the modified pooling of interest method, where the resulting entity recognises the combining operations' assets, liabilities at their historical values as at the amalgamation date.

IFRS

All transactions in the scope of IFRS 3 are accounted for applying the acquisition method.

IFRS 3 does not contain guidance on the accounting for amalgamations. Therefore, under IFRS, an entity would need to adopt a policy on accounting for combinations under common control, either applying acquisition accounting or predecessor accounting.

Impact

Accounting for acquisitions is similar under both IFRS 3 and PBE IPSAS 40.

The accounting for amalgamations is also similar under PBE IPSAS 40 and IFRS, if, under IFRS, the entity's accounting policy for such transactions is to apply predecessor accounting.

Property, plant and equipment

PBE

In accordance with PBE IPSAS 17 *Property, Plant and Equipment*, PBEs are required to account for revaluation increases and decreases on an asset class basis rather than on an asset-by-asset basis.

IFRS

IFRS requires asset revaluations to be accounted for on an asset-by-asset basis.

Impact

Decreases on revaluation will be recognised in operating surplus except to the extent there is sufficient asset revaluation reserves surplus relating to the same class of assets under PBE Accounting Standards, and relating to the same asset under IFRS. This difference could result in higher operating results under PBE Accounting Standards where there is a decrease in the carrying value of an asset. This is because, to the extent that there is sufficient revaluation surplus in respect of the same asset class (as opposed to the same asset), the group recognises a revaluation decrease in asset revaluation reserves.

Borrowing costs

PBE

PBE IPSAS 5 *Borrowing Costs* permits PBEs to either capitalise or expense borrowing costs incurred in relation to qualifying assets. A qualifying asset is defined in PBE IPSAS 5 "as an asset that necessarily takes a substantial period of time to get ready for its intended use or sale". The group's accounting policy is to expense all borrowing costs. As a consequence, borrowing costs are not included in the original cost or revaluations of qualifying assets.

IAS 23 *Borrowing Costs* requires capitalisation of borrowing costs incurred in relation to qualifying assets. The definition of a qualifying asset is identical to that definition in PBE IPSAS 5.

Impact

This difference results in the group's property, plant and equipment value, and subsequent depreciation expense, being lower than they would be under IFRS. In addition, there is higher interest expense in the periods in which qualifying assets are constructed.

Ngā rerekētanga matua o ngā Pae Tikanga Kaute Pūtea a IFRS me PBE
Main differences between IFRS and PBE Accounting Standards

PBE Accounting Standards with comparable IFRS equivalent (continued)

Impairment of Assets

PBE

PBEs apply PBE IPSAS 21 *Impairment of Non-Cash-Generating Assets* or PBE IPSAS 26 *Impairment of Cash-Generating Assets*, as appropriate to determine whether a non-financial asset is impaired. PBEs are therefore required to designate non-financial assets as either cash-generating or non-cash-generating. Cash-generating assets are those that are held with the primary objective of generating a commercial return. Non-cash-generating assets are assets other than cash-generating assets.

The PBE Accounting Standards require the value in use of non-cash-generating assets to be determined as the present value of the remaining service potential using one of the following: the depreciated replacement cost approach; the restoration cost approach; or the service units approach.

IFRS

IFRS does not provide specific guidance for the impairment of non-cash-generating assets. The value in use of an asset or a cash generating unit is the present value of the future cash flows expected to be derived from an asset or cash-generating unit.

Impact

Assets with future economic benefits that are not primarily dependent on the asset's ability to generate cash and may not be impaired under PBE Accounting Standards because of the asset's ability to generate service potential might be impaired under IFRS due to limited generation of cash flows. The group's asset values may therefore be higher under PBE Accounting Standards because some impairment may not be required to be recognised, that would be required to be recognised under IFRS. Further, the value in use of an asset may be different under PBE Accounting Standards due to differences in calculation methods.

PBE Accounting Standards that have no IFRS equivalent / IFRS equivalent is not comparable

The following standards provide guidance on the same or similar topics but are not directly comparable. The comparison below identifies the key recognition and measurement difference.

Revenue from non-exchange transactions

PBE

The PBE Accounting Standards require revenue to be classified as revenue from exchange or non-exchange transactions. Exchange transactions are transactions in which one entity receives assets or services, or has liabilities extinguished, and directly gives approximately equal value (primarily in the form of cash, goods, services, or use of assets) to another entity in exchange. Non-exchange transactions are transactions that are not exchange transactions.

PBE IPSAS 23 *Revenue from Non-Exchange Transactions* deals with revenue from non-exchange transactions. The group's non-exchange revenue includes revenue from general rates, fuel tax, grants and subsidies.

Fees and user charges derived from activities that are partially funded by general rates are also considered to be revenue arising from non-exchange transactions.

The group recognises an inflow of resources from a non-exchange transaction as revenue except to the extent that a liability is also recognised in respect of the same inflow. A liability is recognised when a condition is attached to the revenue that requires that revenue to be returned unless it is consumed in the specified way. As the conditions are satisfied, the liability is reduced and revenue is recognised.

Ngā rerekētanga matua o ngā Pae Tikanga Kaute Pūtea a IFRS me PBE
Main differences between IFRS and PBE Accounting Standards

PBE Accounting Standards that have no IFRS equivalent / IFRS equivalent is not comparable (continued)

Revenue from non-exchange transactions (continued)

IFRS

IFRS does not have a specific standard that deals with revenue from non-exchange transactions. IAS 20 *Accounting for Government Grants and Disclosure of Government Assistance* contains guidance relating to the accounting for government grants. Under IAS 20, government grants are recognised in profit or loss on a systematic basis over the periods in which the entity recognises expenses for the related costs for which the grants are intended to compensate. In the case of grants related to assets, IAS 20 results in setting up the grant as deferred income or deducting it from the carrying amount of the asset.

Impact

The group's accounting policy may lead to earlier recognition of revenue from non-exchange transactions than if it was recognised under IAS 20. It may also result in differences in asset values in relation to grants related to assets.

Under PBE IPSAS 23, the timing of recognising the group's rates revenue is at the date of issuing the rating notices for the annual general rate charge resulting in the entire rates revenue being recognised in the interim financial statements of the group. This is likely to be an earlier recognition than if this revenue was accounted for under IFRS.

Revenue from exchange transactions

PBE

As discussed above, the PBE Accounting Standards require revenue to be classified as revenue from exchange or non-exchange transactions.

PBE IPSAS 9 *Revenue from Exchange Transactions* deals with revenue from exchange transactions. The group's exchange revenue includes revenue from fees and user charges (water and wastewater charges, development contributions, infrastructure charges, port operations, consents, licences and permits) and revenue from sales of goods.

The group recognises revenue related to services on a percentage of completion basis over the period of the service supplied. Revenue from sale of goods is recognised when the substantial risks and rewards of ownership have been passed to the buyer.

IFRS

IFRS 15 *Revenue from Contracts with Customers* introduces a single revenue model for contracts with customers. It does not distinguish between sales of goods and services. It defines transactions based on performance obligations, which are promises to transfer goods or services in a contract with a customer.

The core principle of the standard is that revenue is recognised as a result of the entity satisfying performance obligations or promises to transfer goods or services at an amount that reflects the consideration that it expects to be entitled to in exchange for those goods or services. These may be satisfied over time versus at a point in time based on when control of the good or service transfers to a customer.

Impact

The group's accounting policy may result in a different timing of recognition of revenue from exchange transactions compared to IFRS 15.

For example, IFRS 15 contains more detailed guidance on identifying distinct performance obligations in a contract and allocating the consideration to these based on the standalone selling price of the performance obligations. This may result in some revenue recognised earlier or later than under PBE IPSAS 9.

Ngā rerekētanga matua o ngā Pae Tikanga Kaute Pūtea a IFRS me PBE
Main differences between IFRS and PBE Accounting Standards

PBE Accounting Standards that have no IFRS equivalent / IFRS equivalent is not comparable (continued)

Revenue from exchange transactions (continued)

Further, IFRS 15 contains detailed guidance on the accounting treatment of variable consideration which may result in change in timing of recognising revenue related to items such as rebates and price concessions.

The impact of these differences may result in revenue recognised earlier/later in the contract period however it should not impact on the total revenue recognised during the contract term.

Service Concession Arrangement (also known as Public Private Partnership Arrangements)
PBE
PBE IPSAS 32 *Service Concession Arrangements* deals with the accounting for service concession arrangements from the grantor's perspective. Service concession arrangements are more commonly known as Public Private Partnership (PPP) arrangements. Broadly, service concession arrangements are arrangements between the public and private sectors whereby public services are provided by the private sector using public infrastructure (service concession asset).

PBE IPSAS 32 requires the grantor (public entity) to recognise the service concession asset and a corresponding liability on its statement of financial position. The liability can be a financial or other liability or a combination of the two depending on the nature of the compensation of the operator.

A financial liability is recognised if the grantor compensates the operator by the delivery of cash or another financial asset. A non-financial liability is recognised if a right is granted to the operator to charge the users of the public service related to the service concession asset (liability for unearned revenue).

IFRS
IFRS contains no specific guidance addressing the accounting by the grantor (public entity) in a service concession arrangement. However, IFRS contains guidance for the operator's accounting (private entity).

Impact
Applying IFRS to service concession arrangements would not result in a significant impact on the group's financial position or financial performance as, in absence of specific guidance in NZ IFRS, prior to the adoption of PBE Accounting Standards, NZ practice has been to 'mirror' the accounting treatment of the private entity under IFRS which is consistent with the requirements of the PBE Accounting Standards.

Fair Value Measurement
PBE
There is no specific standard in the PBE Accounting Standards, however a number of PBE Accounting Standards contain guidance on the measurement of fair value in specific context (for example PBE IPSAS 17 *Property, Plant and Equipment* and PBE IFRS 9 *Financial Instruments*).

IFRS
IFRS 13 *Fair Value Measurement* does not extend the use of fair value accounting but provides guidance on how it should be applied where its use is already required or permitted by other standards within IFRS.

Impact
The application of IFRS 13 may result in differences in the measurement of certain property, plant and equipment compared to PBE IPSAS 17 and financial assets and liabilities compared to PBE IFRS 9.

Ngā rerekētanga matua o ngā Pae Tikanga Kaute Pūtea a IFRS me PBE
Main differences between IFRS and PBE Accounting Standards

PBE Accounting Standards that have no IFRS equivalent / IFRS equivalent is not comparable (continued)

Lease accounting
PBE
Under PBE IPSAS 13 *Leases*, the group's current accounting policy is to make a distinction between finance leases and operating leases.

Finance leases are recognised on the statement of financial position.

Operating leases are not recognised on the statement of financial position, instead, payments are recognised in the statement of financial performance on a straight-line basis or another systematic basis that is more representative of the pattern of the lessee's benefit.

IFRS
IFRS 16 *Leases* requires the lessee to recognise almost all lease contracts on the statement of financial position; the only optional exemptions are for certain short-term leases and leases of low-value assets.

There is no significant difference in respect of the accounting treatment applicable to lessors, or for lessees in contracts classified as finance leases under PBE IPSAS 13.

Impact
Where the group is the lessee in contracts classified as operating leases under its current accounting policy, applying IFRS 16 would result in the group having to recognise a 'right-of-use' asset (that is, the asset that reflects the right to use the leased asset) and a corresponding lease liability (obligation to make lease payments) on its statement of financial position.

Further, applying IFRS 16 would result in the group having to recognise interest expense on the lease liability and depreciation on the 'right-of-use' asset. Due to this, for lease contracts currently classified as operating leases, the total amount of expenses at the beginning of the lease period would be higher than under the current accounting policy of the group.

There is no significant difference where the group is a lessor in the lease arrangement or a lessee in contracts classified as a finance lease under PBE IPSAS 13.

Waiheke Island walking track.
Rocky Bay Te Whau Loop.

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