GUARDIANS OF NEW ZEALAND SUPERANNUATION

ANNUAL REPORT 2010

NEW ZEALAND SUPERANNUATION FUND

Contents

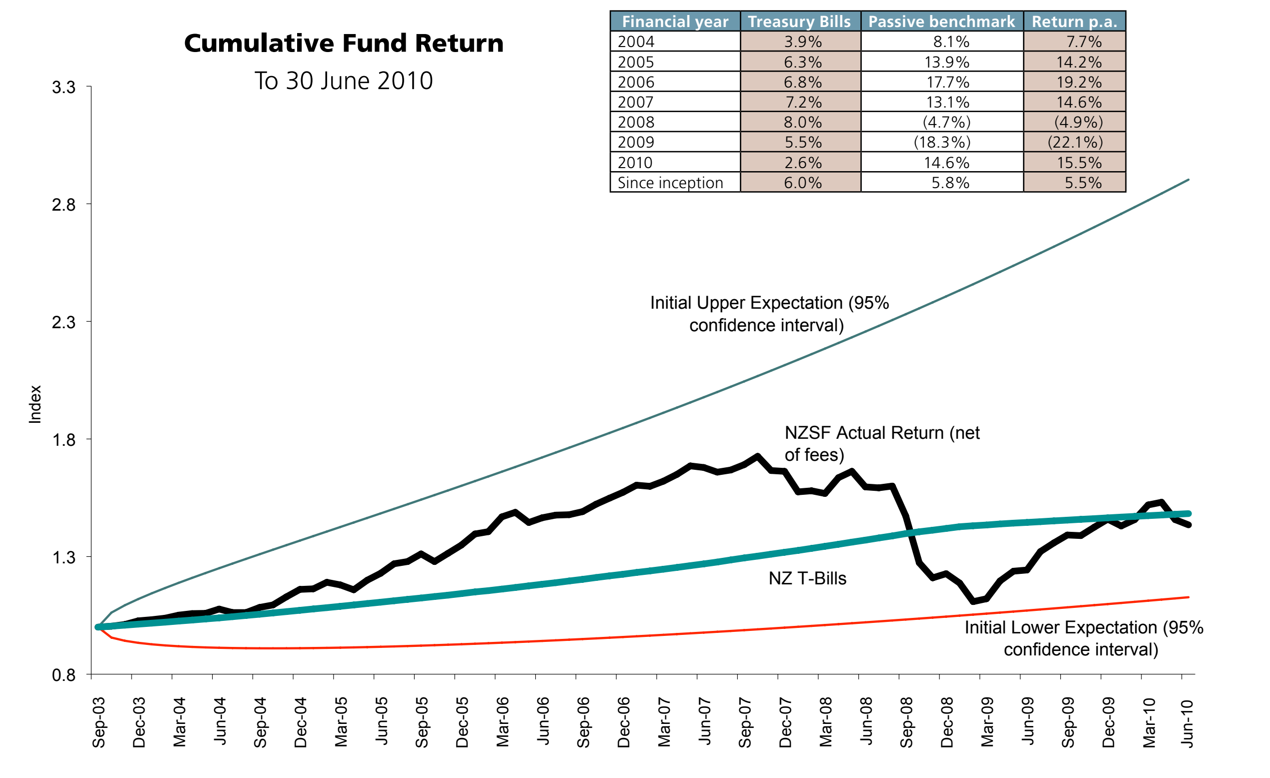
The past 12 months
has seen the Fund,
and its purpose,
benefit from
the focus and
level-headedness
shown by our team
throughout
the Global
Financial Crisis.

– David May
Chairman,
Guardians of New Zealand Superannuation

Performance Summary

FUND SIZE AT 30 JUNE 2010:		$15.63 billion[1]
Returns	**Year to 30 June**	**Since inception**
New Zealand Superannuation Fund	15.5% $2.09 billion	5.5% $2.18 billion
90-Day Treasury Bills	2.6%	6.0%
Passive 'Reference' Portfolio	14.6%	5.8%

Annual performance since inception relative to Treasury Bills



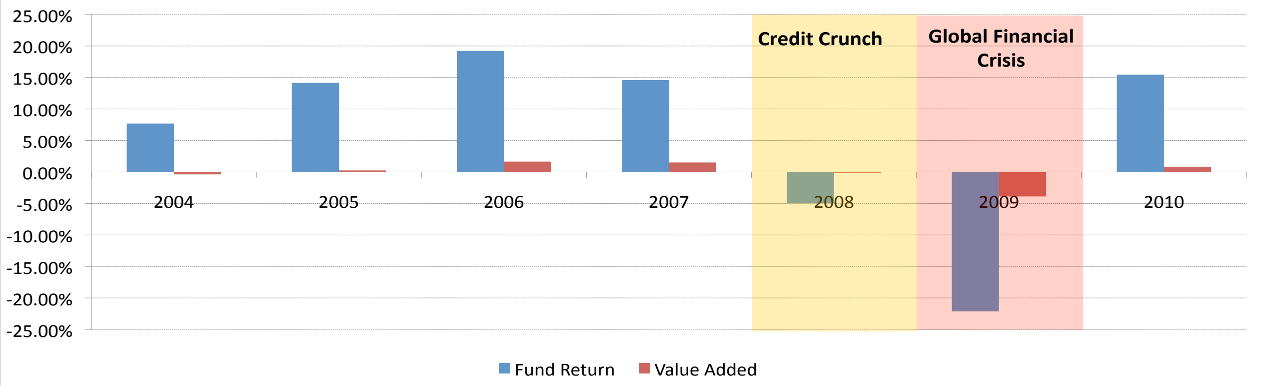
Financial year	Treasury Bills	Passive benchmark	Return p.a.
2004	3.9%	8.1%	7.7%
2005	6.3%	13.9%	14.2%
2006	6.8%	17.7%	19.2%
2007	7.2%	13.1%	14.6%
2008	8.0%	(4.7%)	(4.9%)
2009	5.5%	(18.3%)	(22.1%)
2010	2.6%	14.6%	15.5%
Since inception	6.0%	5.8%	5.5%

1. Excludes provisions for NZ tax

Annual performance since inception relative to passive benchmark

Financial year	Treasury Bills	Passive benchmark	Return p.a.
2004	3.9%	8.1%	7.8%
2005	6.3%	13.9%	14.2%
2006	6.8%	17.6%	19.2%
2007	7.2%	13.1%	14.6%
2008	8.0%	(4.7%)	(4.9%)
2009	5.5%	(18.3%)	(22.1%)
2010	2.6%	14.6%	15.5%
Since inception	6.0%	5.8%	5.5%

Actual Fund Return and Value added



Note: We first introduced this measure at the start of FY2006/7, but to give a fuller picture, we have estimated the passive alternative for earlier years. Value-add is defined as the difference between the Fund return and that of the passive benchmark.

Key Event Summary 2009/10

Reference Portfolio	Page 16
Completion of new investment strategies	Page 19
Value added by active investment	Page 23
Investment in Shell	Page 30
Rated most transparent Sovereign Wealth Fund globally	Page 35
Positive Independent Review of Governance	Page 39

The big picture

The Fund and the Guardians were established by specific legislation for a specific purpose.

Statistics New Zealand predicts that between 2005 and 2050 the number of New Zealanders eligible to retire (aged 65+) is expected to double. The associated cost of providing their retirement income, New Zealand Superannuation (NZS), will more than double because of the additional impact of NZS being indexed to a proportion of the median wage.

This means there will be more people of retirement age than ever before in New Zealand's history and they will make up a larger proportion of the population. Accordingly, there will be fewer 'working-age' people whose productivity can be tapped, through taxation, to fund the greater cost of retirement income. This has significant implications for future Governments' ability to fund other important services.

This is a situation with clear relevance for you, your children and your grandchildren.

How does the establishment of the Fund and the Guardians respond to this?

The establishment of the Fund and the Guardians recognises New Zealand's ageing population as a significant, multigenerational issue. The Fund attempts to address this situation by 'smoothing' the tax burden of the future cost of NZS between generations of New Zealanders. This is achieved by the Guardians investing Government contributions received during the early period of the Fund and, through returns generated over decades of investing, by growing the size of the Fund. At a certain point - currently from 2031 - the Government then begins making withdrawals from the Fund to help to meet the cost, at that time, of NZS.

Partially 'pre-funding' the future cost of NZS in this way means that future Governments do not have to seek as much from future New Zealand taxpayers (or from other sources, such as through raising debt) to meet the cost of NZS when it is increasing most sharply.

In the 2009 Budget the Government decided to reduce contributions to the Fund until the Crown operating balance returns to surplus sufficient to resume contributions. The Treasury has estimated this to be in 2016.

What contribution do the Fund and the Guardians make?

We think of it this way – the **Fund** is a special purpose savings vehicle bringing certainty that some of the future cost of NZS is covered. The Fund is also expected to add to Crown wealth over the long term by earning more for the Government in investment returns than the Government would save in debt servicing i.e. it adds to Crown wealth and improves its ability to meet increased NZS commitments in the future.

We think it is important to state that impact in a way meaningful to all New Zealanders. So we describe the Fund's ultimate outcome as "Reducing the tax burden on future New Zealand taxpayers of the cost of New Zealand Superannuation". We believe that if the Fund improves the Crown's financial position, it will have reduced the tax burden.

The **Guardians** are expected to manage the Fund according to a legislated mandate. The mandate requires us to manage the Fund in a commercial, prudent fashion comprising:

- Best-practice portfolio management
- Maximising return without undue risk
- Without prejudicing New Zealand's reputation in the world community

The mandate drives our work to manage investments, cost, risk, governance and our own capabilities. Ultimately, we will be judged by future taxpayers according to whether we, through the way we have chosen to manage the Fund, have added value to its intended outcome.

Our impact on New Zealand investment markets

To meet our mandate we invest globally. We are careful not to over-invest across the spectrum of New Zealand assets as that would risk driving up prices when we buy and driving them down when we sell. Nevertheless, we are identifying select, attractive opportunities which meet the objectives of a prudent, commercial long-term investor. Where we do invest in New Zealand we aim to:

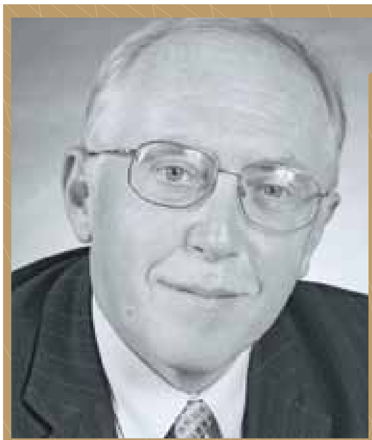
- bring focussed investment experience to local opportunities e.g. through our local infrastructure and Expansion Capital Strategies (see pages 20 and 28);
- bring an almost unique capacity to invest in long-dated productive assets e.g. Kaingaroa timberlands and Shell (see page 30);
- contribute to growing New Zealand's capital markets via – among other things – invseting in new asset classes, leading sound governance practices, and introducing strong relationships to global, world-class sources of capital e.g. through our peer network (see page 12); and
- use the international connections we make through global investment activity, to New Zealand's benefit.

Six things to remember about the Guardians and Fund

1. *We are required to invest the Fund so it makes as much money as possible, without incurring undue risk, for as long a period as possible; and the Government is not scheduled to make withdrawels from the Fund until 2031.*
2. *This means that the asset mix of the Fund is weighted toward growth.*
3. *It also means that we can and do invest in asset classes (e.g. timber) which cannot be realised quickly – they are 'illiquid' – and require a longer-term commitment of capital. This does not suit many investors' portfolios, often because they have high demands for cash (perhaps because they have to pay dividends or must cover the eventuality of investors selling up and leaving their fund).*
4. *We pursue 'atypical' investment options – such as investing in 'illiquid' asset classes – only when we are confident of being rewarded, over time, with superior returns relative to more standard options such as passive investments in fixed interest or equities.*
5. *Having such a portfolio tends to generate short-term volatility – up or down. However it is very important to keep in mind that the purpose of the Fund is long-term and so its success must be measured over time by future taxpayers who will benefit (the oldest of whom is 21 years away from retirement and many of whom have not yet been born). Single-year snapshots have very limited relevance other than as a small contributor to a much larger pattern of returns, which the Fund is only seven years into establishing.*
6. *Finally, we are very aware that the circumstances which make our Fund special relative to many other investors also make it quite difficult to objectively assess its performance and, as important, whether we are adding value to it. Accordingly, we carefully and publicly benchmark both its performance, and our role in that performance.*

If you are interested in further information about the reason why the Fund and Guardians exist, more on the ageing population issue and how the Guardians and Fund are designed to respond to it, there is a significant volume of information on our website **www.nzsuperfund.co.nz.** On the front page of the website you can find our *Introduction to the Guardians and Fund.*

Board Statement
An important 12 months



David May
CHAIRMAN

This financial year has been very different from the one that preceded it. Most obviously, the Fund has benefited from the rebound in global equity markets to present a very different picture to what we reported in the 2009 Annual Report.

But what sits behind that is 12 months of ground work, throughout our organisation, comprising one of our busiest years since the Fund's inception. We have reviewed and bedded in investment beliefs and strategy; welcomed high-quality new people and seen them making positive contributions; recalibrated our underlying investment processes; and revised our approach to using external investment managers.

We have also ensured that we are maximising our position of being a capital provider in these times when confidence is low. We have made direct investments, and investments via third parties, in activities that are normally crowded and competitive but are far less so at present – in particular, global property, infrastructure, and in classes of insurance. Finally, we have exerted considerable effort on developing strong links with like-minded and similarly positioned global funds so that we can learn and potentially coinvest with them.

We expect the work we have done in the past 12 months to make a material contribution toward achieving the Fund's purpose of reducing the tax burden of NZS on future New Zealand taxpayers.

Fund performance

In the 2009 Annual Report we said that, as a long-term investor, we have a higher-than-average tolerance to volatility in investment markets and that our investment strategy and asset allocation had been designed accordingly. We said that the period of severe volatility that characterised the previous financial year was precisely the time for us to stay the course and capitalise on our ability to ride out tough patches without selling undervalued assets. In fact, it was the time to take advantage of the opportunities available to an investor with our perspective and the Fund's characteristics in such conditions.

A year on, it is clear that our focus was held. We did 'lean in' to prevailing market winds and build our exposure to growth assets. We have taken advantage of our long-term investment horizon and tolerance for illiquid assets (i.e. those which are difficult to sell quickly) to make investments outside of listed equities markets, where we believe we will receive active returns sufficient to compensate the Fund for taking on the illiquidity risk.

We began to see the benefits of being able to ride out tough market conditions in the final quarter of the previous financial year. That effect continued through the first three quarters of this financial year. For the year to 30 June 2010 the Fund's return was 15.45%, reflecting the rebound. This represents a 12.85% premium to the risk-free rate (which for the Fund is the return on 90-day New Zealand Treasury Bills) for the year. Certainly the final quarter of this year has seen further volatility, in particular that generated by concern about sovereign debt. Nevertheless, this year's rebound has seen the Fund's total return since inception rise to 5.49% p.a. This remains 0.51% less than the risk-free rate over the same period, but the Fund's return was 2.8% below that mark at the end of the previous financial year.

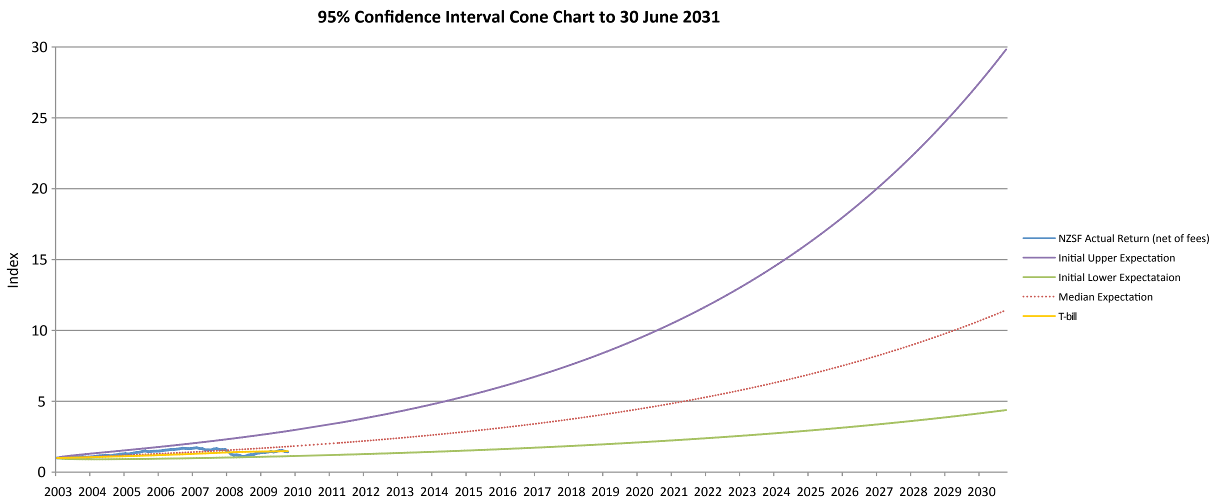
The increase in the size of the Fund in the 2010 financial year best illustrates two key points. First, it supports what the Guardians have repeatedly stressed since the Fund's inception: that a growth portfolio makes short-term performance volatile. Clearly, we prefer short-term volatility to make the Fund go up – as it has for most of this year – rather than down. But the crucial factor is how the Fund performs over time. We must remember that, in September 2010, the Fund will have been invested for less than seven years of the multi-decade, multi-generational job it was established to do.

Second, after poor results during the Global Financial Crisis, the refocus of our active investment strategy once again added value. As well as outperforming Treasury Bills, the Fund outperformed the passively invested alternative benchmark by 0.83% in the past financial year.

Performance in context: Less than seven years invested

Chart shows:

- Median of our range of expected returns over 30 years (dotted)
- Monte Carlo analysis highlights 95% confidence intervals of our returns with our current portfolio
- Impact of Global Financial Crisis (GFC)



Board Statement (continued)

Managing the Fund

It is our job to manage the Fund so that it achieves its purpose. Over the past two financial years we have done considerable ground work. In 2008/09 the work was, primarily, to weather and manage through the GFC. In 2009/10 it has been to build what we learned into our investment processes, to ensure we benefited fully from the recovery.

This is apparent in four important areas: how we assess, access and manage risk within the Fund; what we have done to improve the efficiency of our operations; the development and careful implementation of investment strategies; and the higher degree of transparency we adopt for our management of the Fund. The CEO, Adrian Orr, discusses these matters in further detail under the collective heading of best-practice portfolio management on page 11.

Nor has all of the work been behind the scenes. We have made a number of investments in the period, across a range of asset classes including investment-grade credit, commodities, private equity, forestry, infrastructure, catastrophe insurance and of course our 50% share in the acquisition with Infratil of the New Zealand assets of Shell. On page 26 we set out our second report on our progress against the New Zealand Investment Directive. In that section we also discuss the impact of this on the local market.

"We expect the work we have done in the past 12 months to make a material contribution toward the achievement of the Fund's purpose of reducing the tax burden of New Zealand Superannuation on future New Zealand taxpayers."

Scrutiny

The performance of the Fund and our management of it have, understandably, always been well-scrutinised, but never more than this year. Our Responsible Investment policies and practices, our cost structure, the transparency of how we invest the Fund and why, and our overall governance have all been subject to major reviews by third parties. This is in addition to the usual scrutiny, and commentary, we attract through media coverage of our monthly Fund performance reports and other announcements, our website, the Official Information Act, our annual financial review before the Commerce Committee and the scores of public presentations given in New Zealand and offshore by our management team.

Key among these processes was the second of our required five-yearly reviews. Mercer was appointed by the Minister of Finance to conduct the review, according to terms of reference specified by the Minister. The result was published in November 2009 and we welcomed the conclusions, most of which endorsed our current practices. We have reported this issue on page 49.

We continue to rank well relative to peer funds for our cost structure and performance in implementing the United Nations Principles for Responsible Investment. We continue to be top-rated among global Sovereign Wealth

Funds for transparency – most recently in a study by the Washington, D.C. -based Carnegie Endowment for World Peace.

And we continue to make as much information as possible on our website about how we invest and why, what we're invested in and with whom, and how the Fund is performing; and to present it as simply as possible.

I'd like to note some changes in the Board of the Guardians during the financial year. In September 2009 we farewelled Glen Saunders at the conclusion of his term. In May 2010 we farewelled Bridget Liddell at the conclusion of her second term. We would like to warmly acknowledge the strong contribution Glen and Bridget – who has been with us since our inception – have made to our organisation, in particular to our Responsible Investment programme and to our engagement with peer funds. In November 2009 we welcomed Stephen Moir and Catherine Savage and the Board is already benefiting from their contributions. At the same time, existing Board member David Newman was appointed Deputy Chair of the Guardians, replacing Sir Douglas Graham in that role following Sir Douglas' retirement at the conclusion of the previous financial year. Gavin Walker was appointed to the Guardians' Board effective 1 July 2010. We look forward to working with him.

Finally, I would like to thank my colleagues and the team at the Guardians for their work during the year. The past 12 months has seen the Fund, and its purpose, benefit from the focus and level-headedness shown by our team throughout the Global Financial Crisis. I am confident the organisation will build on its achievements this year and continue to gain from the opportunities available to disciplined, competent long-term investors.

David May

DAVID MAY
Chairman

The Fund outperformed Treasury Bills and it also outperformed the passively invested alternative benchmark.

CEO Statement
How we benchmark what we do

Adrian Orr
CEO

Since March 2009 the global economy has been recovering from the Global Financial Crisis, the darkest points of which involved a near total loss of confidence in financial intermediaries. This brought gridlock to international capital flows, gridlock which was underpinned by a realisation that debt positions in many sectors in many OECD countries had reached unsustainable levels, and correction was needed. When it came, it was brutal.

Since then, increasing savings in many developed economies suggests less spending. As such, global demand remains sluggish. Offsetting this somewhat, however, is the support provided by continued strong levels of economic activity in China and in many other areas of non-Japan Asia, India, and parts of South America. In these countries we are witnessing change of historic proportions where the number of people moving to cities, and being classified as receiving a middle income, is rising at a rate not seen previously. This is hugely positive for economic welfare globally. These trends and economic drivers are now unstoppable, but of course the pace of change and growth will be variable.

So how is this context reflected in the Fund? First in its financial performance, which is discussed in the Board Statement and in further detail later in the report. The key relevance of this has been our ability to ride out the period of poor market performance, retain our focus on the long term and to benefit from recovering markets. In New Zealand the GFC has presented the Fund with a unique opportunity, as many long-term overseas investors have restricted their focus to larger markets.

As one of this country's few, genuine long-term savings vehicles we are able to apply our commercial disciplines to the local market to invest in long-term productive assets that may be unattractive to other investors. By doing so, we can both benefit the Fund and provide stable, long-term investment capacity to attractive sectors of the New Zealand economy.

Another way in which the emerging economic landscape impacts us is the increasing interest taken in our stewardship of the Fund. We understand and welcome scrutiny of our cost control and of the value we add. That is why we strive to make such scrutiny well informed by publicly reporting our returns relative to 90-day Treasury Bills and to a passive alternative. However, that is not the only benchmarking we do. In this section, I will detail how thoroughly we benchmark our management of the Fund.

The logical beginning point for a discussion of how we measure ourselves is our legislation. Taking into account the Fund's long-term purpose, the legislation requires us to manage the Fund in a 'commercial, prudent' fashion which it characterises as:

- Best-practice portfolio management;
- Maximising return without undue risk; and
- Without prejudicing New Zealand's reputation in the world community.

As we have said previously, none of these requirements are defined by the legislation. They are left to us to interpret.

The following sections of this report provide considerable detail on what we have invested in and on the return on those investments over the past 12 months. So, this section focuses on how we benchmark 'best-practice portfolio management'. This is because our portfolio management style dictates how we structure and manage the Fund and, therefore:

- it drives what we invest in and how;
- it drives what impact, if any, our investments have on New Zealand's international reputation either because of what the investments are, how they are managed (or both); and
- it is the foundation of Fund performance.

Portfolio management style is also crucial to any effort to compare funds. We understand that observers seeking to assess the Fund naturally compare with what they know: their own investments e.g. KiwiSaver. However, for any comparison between investment funds to be relevant and useful, the purpose, portfolio, risk appetite, investment horizon and investment style should be as similar as possible.

Unfortunately, it is not easy to find organisations which match the Fund closely in even some, let alone most or all, respects. What the Fund is for and hence how it works are completely different from any retail balanced or growth fund, and from any other Crown Financial Institution. It is also different to most other countries' Sovereign Wealth Funds. So, comparing how we run it, and how it performs, with any of those funds is problematic.

Nevertheless, we ensure that all the important aspects of how we manage the Fund and our own organisation, from our fundamental beliefs about investment onward, are rigorously benchmarked. We internally benchmark what we do against what our peer funds do. We benchmark how we do it. And we also externally benchmark our results i.e. how well we have done what we have chosen to do.

The key relevance of the Fund's performance is that it demonstrates an ability to ride out the period of poor market performance, retain focus on the long term and benefit from recovering markets.

CEO Statement (continued)

From what we have discovered in the course of our benchmarking work, we are confident that how we have chosen to manage the fund is as good as, or better than, global peer funds. More important, we are confident that it produces results in investment, governance, cost structure, risk management, and organisational capability which are credible relative to our peers.

We note that an important outcome of benchmarking against peers is the relationships it leads to e.g. collaborative research and coinvestment, and staff development. This is what we intend from our relationships, which should further drive organisational improvement and lead to positive economic outcomes for current and future New Zealanders.

How and what we benchmark

First: what does a 'peer' look like?

There are several hundred funds against which we are benchmarked in third-party assessments of cost structure, transparency and other disciplines. However, there are a selection of funds, mainly based in North America and Europe – but increasingly including Asian funds – who we closely monitor and against whom we benchmark ourselves. These are our 'peer' funds. None is exactly like our Fund. However, they all share two important qualities with us: they have a similar risk profile and they actively manage investments.

By 'risk profile' we mean the extent to which the peer fund is able to choose and manage risk in order to generate return. Generally, the longer the investment horizon the more risk can be assumed – with the associated expectation of greater reward – because a 'bad' result in any one year has less overall impact. Having a similar risk profile is important because, given its influence on what returns are sought over what period, it is crucial to the composition of the fund, the challenges it is likely to face and so how that fund is managed.

Having actively managed investments in common is important because it requires skilled intellectual resources to implement (and to monitor). It therefore has a strong influence on a fund's cost structure because such resources can be expensive to recruit or outsource. Accordingly, a fund's management should take on the cost and complexity of active management only when it believes it can generate returns above passive management (an example of 'passive' management would be through an index-tracking fund), or because passive management of a particular desired investment simply isn't available.

Because active management generally carries more risk, often because the assets being actively managed are illiquid (i.e. it is not possible to realise them quickly), the return expectations are commensurately higher. So, funds with active management in common will deal with roughly similar issues relating to managing cost, liquidity and retaining skilled human capital. They will also be further linked through the influence of active management on their risk profiles and portfolios. We will now discuss what we benchmark.

We benchmark what we do

Benchmarking of 'what we do' primarily focuses on our approach to investing. It can be expressed as ensuring that we think about and structure our investments is at least as vigorously considered as it is at other credible, comparable funds doing the same, or similar, things that we do. The main areas we benchmark are shown below:

> ***"This is one of the best-designed and governed institutional investors in the world."***
>
> – Dr. Ashby Monk, Co-director, Oxford Sovereign Wealth Fund Project, Oxford University

What we benchmark	How we benchmark it
• Investment beliefs • Investment approach • Reference portfolio composition • Investment strategies for individual asset classes • Net value added, implementation risk and costs • Investment risk practices	We compare ourselves to peer funds, including by going to speak to them; accessing published research and reviews by external experts. We also use third-party benchmarking. The main tool for this is CEM Benchmarking Inc, which is widely used by global pension funds to compare performance. We use this because CEM looks into what funds do that contribute to their performance relative to peers. For example, CEM's cost benchmarking includes 290 global funds and compares whether costs are reasonable given the investment strategy. We are closely benchmarked against a subset of 20 peers with a similar size and investment approach (see page 33).

CEO Statement (continued)

We benchmark how we do it

Benchmarking of 'how we do it' primarily focuses on internal structures and capabilities. The main areas benchmarked are shown below:

What we benchmark	How we benchmark it
• Governance • Leadership skills • Culture • Custodial capability, contract and cost • Responsible Investment • Transparency • Fund and strategy capabilities • Collaboration with peers	Again, we compare ourselves to peer funds – including face-to-face – and use third-party benchmarks. The third party benchmarks vary. For example, we benchmark custodial capability. (A 'custodian' is the organisation holding a pension fund's assets in safekeeping and which, among many other roles, settles purchases and sales of securities). For custodial benchmarking we use Thomas Murray, a company specialising in global custodian monitoring. They benchmark us against 16 global institutional investors. The 2010 benchmark concluded that the fees we pay for our custodian are competitive. Responsible investment benchmarking meanwhile is based on the UN Principles for Responsible Investment. This survey is completed by 124 global asset owners and 152 global investment managers. Overall we are top quartile (see page 138). Both benchmarks highlight areas for further improvement.

We benchmark whether we are improving

Benchmarking of ‘whether we are improving’ focuses on ensuring we are able to assess our progress on an ongoing basis. This is based mainly on:

What we benchmark

- Measurement of investment and organisational performance
- Our transparency
- Ongoing comparison to peers
- Board and management engagement with external experts
- Continuously reviewing our business model and activities

How we benchmark it

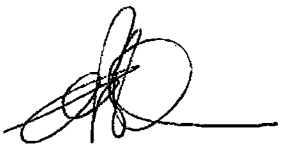
Once more, we compare ourselves to peers, including via a global benchmarking study, and have a strong internal focus on continuous improvement.

For example, internal reporting assesses risk-adjusted after-costs returns and organisational performance across a range of areas, including compliance, risk, communications and people. Crucially, these assessments directly influence performance-based pay.

Our global peer benchmarking study meanwhile continuously assesses peers to benchmark our progress and identify potential improvements. Board and management engagement with peers is an important part of this. Our Board education programme has involved discussions with several large US and Canadian pension funds and university endowments during the year to understand more about how other Boards function. The Board also received presentations from external experts on a range of topics.

A number of third parties benchmark our transparency. Transparency, for us, is a crucial tool because it ensures that New Zealanders and all other interested observers can do their own benchmarking based on easily accessed, simply written and well-structured public information about what we do, how we do it, and how well. We discuss this in more detail on page 34.

Finally, I would like to thank the team and the Board for maintaining discipline, dedication and good spirit through what has been an intense but constructive 12 months. I am fortunate to work with a talented Guardians team, and enjoy and learn from the experience.



Adrian Orr
CEO

Portfolio activity

As discussed in the Board and CEO statements, this year has seen a significant level of activity in structuring and benchmarking the portfolio, designing and finalising investment strategies, making decisions about who to invest with, and ultimately in actually making new investments.

This section deals in detail with each of those areas.

Portfolio structure and benchmarking

During the financial year we instituted the concept of the Reference Portfolio. At the close of the financial year we had not finalised its composition. However, that work has been completed in time for inclusion in this Annual Report and is set out below. Information about the Reference Portfolio has also been disclosed on our website.

What is the Reference Portfolio and why are we using it?

In our 2010 Statement of Intent, which is available on our website, we set out why we regard the Reference Portfolio as important. In essence, it is our best effort at designing a 'shadow' portfolio which is appropriate to the Fund's long-term horizon and associated risk profile, and is capable of achieving the Fund's objectives. The Reference Portfolio is weighted towards growth assets, as is the Fund, but it is comprised of simple, low-cost investments (primarily listed equities and fixed income).

Accordingly it is a crucial benchmark for whether we are adding value to the Fund by pursuing additional, active investment strategies with the expectation of higher reward, but which are more complex and costly, than passive investments (we discuss these strategies in detail, later in this section).

We strongly believe that active investment strategies will, over time, make the Fund larger than it would have been had we not pursued them, and without having incurred undue risk. The Reference Portfolio will test that belief.

It will do so publicly. We will publish the Fund's performance relative to the Reference Portfolio in each Annual Report (many of our private markets assets are valued on an annual basis). This is also consistent with our focus on transparency.

The Reference Portfolio is a crucial benchmark for whether we are adding value to the Fund.

What is in the Reference Portfolio?

The principles underlying the composition of the Reference Portfolio require exposures which are:

- low-cost, simple (i.e. listed asset classes) and passive;
- representative of the investable market;
- appropriate to the risk profile of the Fund; and
- relevant to a New Zealand investor.

The Reference Portfolio is a crucial component of the Fund and therefore had to be designed and implemented carefully, requiring input and review from the Board, Leadership Team and external asset allocation experts. The transition has been a considerable achievement for the team given the complexity and sensitivity of billions of dollars of transactions across equities, bonds, listed property, commodities and foreign currency.

The result is the Reference Portfolio as below:

Asset class	Percentage
Global equities	70%
NZ equities	5%
Global listed property	5%
Total Growth	**80%**
Total Fixed Interest	**20%**
TOTAL PORTFOLIO	**100%**
Net unhedged foreign currency exposure	**0%**

Is the Reference Portfolio 'set and forget'?

No. The structure of the Reference Portfolio is based on our assumptions of what the long-term value of various asset classes should be, regardless of what is actually happening to those values in any given market conditions. This is the appropriate approach for a long-term investment perspective.

The Reference Portfolio's composition can therefore change if:

- our assumptions change about what long-term return-for-risk should be; or
- aspects of the Fund's purpose or endowments (tolerance for illiquidity, long-term investment horizon, New Zealand location and sovereign status) change; or
- market developments mean that a narrower or wider set of representative market exposures can be accessed passively and at low cost.

How does the Reference Portfolio differ from the Passive Benchmark?

The Passive Benchmark continued to be in force throughout the past financial year. The Reference Portfolio takes over in the 2010/11 financial year.

The Passive Benchmark served fundamentally the same purpose as the Reference Portfolio. However, the Reference Portfolio contains only low-cost, simple, passive exposures, selected on the basis of long-term assumptions (as explained in the previous section).

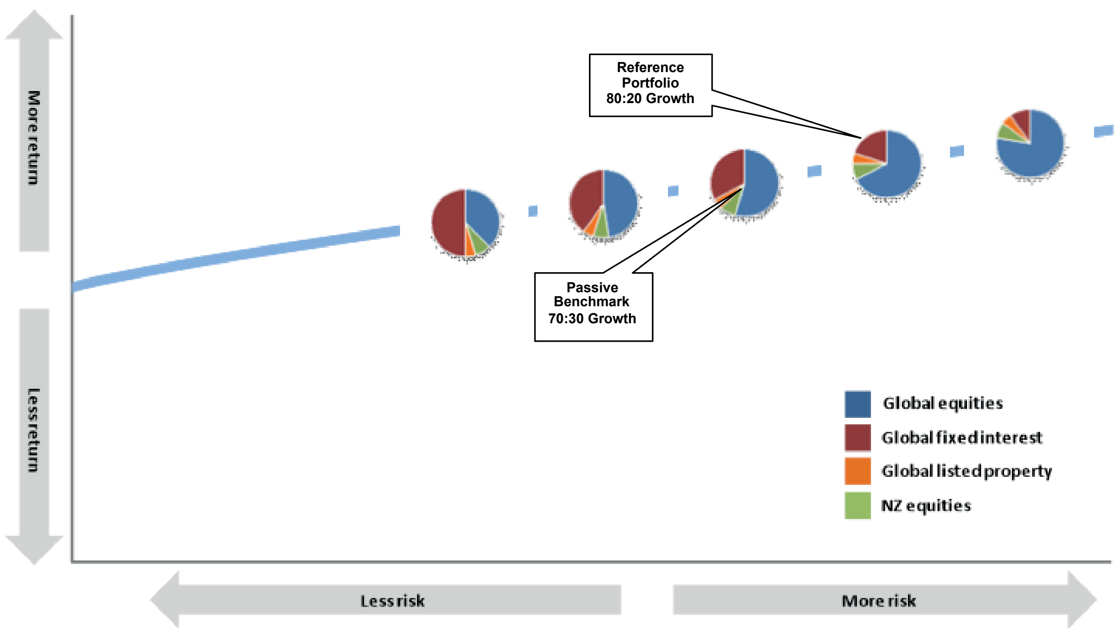
Portfolio activity (continued)

We made a number of other important changes as part of the introduction of the Reference Portfolio:

1. ***The Reference Portfolio incorporates an appropriate degree of financial risk for a long-term investor***

The Reference Portfolio is constructed from our long-term assumptions of asset class risk-return behaviours. Given the Fund's purpose and investment horizon, we have deliberately selected a high exposure to growth assets. This bias toward growth assets will generate a higher long-term return, albeit with more short-term returns volatility. The Reference Portfolio has a similar level of financial risk to our Strategic Asset Allocation established at the commencement of the Fund's investment life. However, it represents a slight increase in risk relative to where the actual Fund was last year in the midst of the Global Financial Crisis.

We do not anticipate changing the level of financial risk in the Reference Portfolio often, indeed only if there is some fundamental change in our view of the long-term risk-return behaviours in underlying assets. What we will do, however, is change the level of financial risk in the actual Fund based on our value-add investment activities.



2. ***There is a smaller 'over-weight' allocation to New Zealand listed equities and to global listed property***

Both New Zealand listed equities and global listed property are represented by a minimum holding of 5% in the Reference Portfolio compared to 7.5% and 12% respectively under the previous Strategic Asset Allocation.

This reflects the low representation of both asset classes (sub-5% in reality) in the market capitalisation of the global investable market. We note that the Fund's actual investments in New Zealand comprise a far broader range of assets than just equities e.g. timber, direct investments, infrastructure and private equity. All of these investments are regarded as active investment activities making the difference between the Reference Portfolio and the Actual Fund.

3. It contains no allocation to commodities or to foreign currency exposure

We do not believe that, based on our equilibrium view, exposure to either asset class will improve the risk-return balance of the Reference Portfolio. It may be that the Fund can gain shorter-term benefits from exposure to these assets classes, however that benefit is better accessed through active investment activity such as Strategic Tilting (again, see the Adding Value section below).

Adding value to the Reference Portfolio

We undertake a range of active investment activities that we believe will add value over and above the returns generated by passive investments in the asset classes contained within the Reference Portfolio. This activity is the difference between the Reference Portfolio and the Actual Fund at any one time.

That we decide to undertake any additional investment activity at all is underpinned by two main factors:

1. fundamentally, our recognition of the reality that good investment opportunities come and go and, to access them, the Fund must be invested dynamically; and
2. the anchoring of the activity to strategies making use of:
    - our investment beliefs relating to asset class strategy and portfolio structure, and to manager and investment selection;
    - the Fund's endowments (see page 17); and
    - our competitive advantages (e.g. we have a competitive advantage in New Zealand markets).

Active investment strategies

There are three broad areas of added-value activity we pursue. Each is delivered via one or more strategies. Each strategy is supported by one or more investment beliefs. We have set out our added-value activities and the strategies (and sub-strategies) that sit under each below:

ACTIVITY	STRATEGIES	DESCRIPTION
Capturing active returns through investing in private markets and/or selecting and investing through active managers.	**Public markets active return**	*This strategy is based on two of our investment beliefs: that managers with true skill in generating excess returns are rare; but that some markets and strategies are particularly conducive to a manager's ability to generate excess returns. The former belief fashions how we evaluate prospective active managers, the latter how we select markets in which we look for them.*

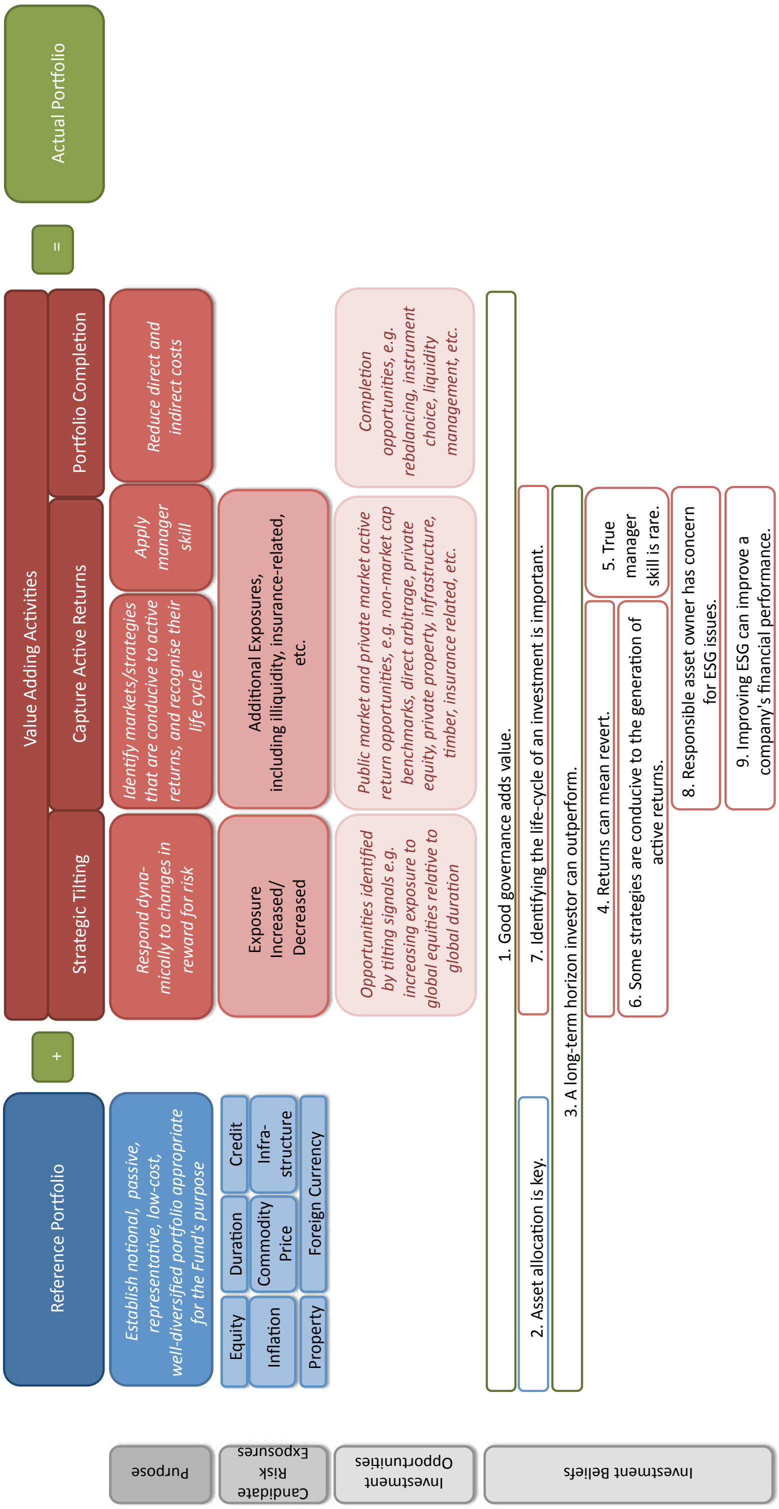
Portfolio activity (continued)

ACTIVITY	STRATEGIES	DESCRIPTION
Capturing Active Returns (continued)	**Infrastructure**	*Infrastructure can provide stable, long-term cashflows that are a good match for our long-term objectives. It can also help hedge the Fund against inflation risks. Our infrastructure strategy plays to our belief that investors with a long horizon can outperform more short-term-focused investors.* **Social Infrastructure** *Social Infrastructure sits within this strategy. We believe there is an opportunity to focus on Public Private Partnership (PPP) projects in social infrastructure, where, typically, the private investor provides the infrastructure and the Government party the service.*
	Timber	*We believe timber is a good investment for long-term investors as it has a low correlation with other asset classes and provides an inflation hedge. Our timber strategy suits our belief that investors with a long horizon can outperform more short-term-focused investors.*
	Private Equity	*We believe there is a potential to generate out-performance in risk-adjusted returns against passive listed equity alternatives through private equity investment in skilled, aligned private equity fund management teams who can access long-term pools of capital. Our private equity strategy suits the same beliefs as our public markets active return strategy and our belief that investors with a long horizon can outperform more short-term-focused investors.* **Sub-strategy** *The New Zealand Expansion Capital Strategy sits within the Private Equity Strategy. We believe there is a significant pool of smaller high-growth companies in New Zealand constrained by a shortage of long-term equity and where there are opportunities to add value by improving governance. This strategy suits the same investment beliefs as our New Zealand direct strategy.*

ACTIVITY	STRATEGIES	DESCRIPTION
Capturing Active Returns (continued)	**Property**	*We believe inefficiencies in global real estate markets create opportunities to generate out-performance in risk-adjusted returns against passive listed alternatives through private equity investment in skilled, aligned private equity style fund management teams. This strategy suits the same beliefs as our private equity strategy.*
	Rural land	*We believe rural land is a sound investment for long-term investors. Income growth in emerging Asia should benefit food producers and be reflected in farmland prices. The sector cannot be accessed passively. Our rural land strategy suits our belief that investors with a long horizon can outperform more short-term-focused investors.*
	New Zealand Direct	*We believe we can take advantage of our long-term investment horizon, sovereign status and NZ domicile to earn meaningful returns for the Fund by making a small number of significant NZ investments. This strategy suits our beliefs about the benefits to long-term investors and that certain markets are more conducive to excess returns.*
Strategic Tilting or swimming against the market tide.	**Strategic Tilting Strategy**	*Strategic tilting is based on our belief that asset class returns are partly predictable over time and tend to revert to their average. We exploit this by first identifying asset class returns that we believe are materially above or below our view of their long-term value and then by increasing or decreasing our portfolio weighting toward those asset classes accordingly.*
Portfolio completion or identifying and reducing the direct or indirect costs of investment.	**Portfolio Completion Strategy**	*Closely managing fees and costs – for example, the costs that accrue to investing or divesting from equities, particularly in small markets – represents added value to the Fund.*

Portfolio activity (continued)

In the below table, we have further illustrated the linkages between value-adding investment activities, risk exposures and our investment beliefs.



Our added value in 2009/10

Passive and value-added returns to 30 June 2010

PASSIVE BENCHMARK RETURN	+/- ADDED-VALUE ACTIVITIES =			ACTUAL PORTFOLIO RETURN	VALUE ADDED (NET OF FEES, BEFORE NZ TAX)
	CAPTURING ACTIVE RETURNS	STRATEGIC TILTING	PORTFOLIO COMPLETION		
14.62%	(0.24)%	0.77%	0.29%	15.45%	0.83% ($113 million)

Key factors in performance

CAPTURING ACTIVE RETURNS

This result comprised the following factors:

- **Active investment managers +0.53%** The ending of severe volatility in global markets saw the Fund's overall stable of investment managers beat their individual investment benchmarks. The main contributors to this were managers of multistrategy (a strategy particularly hard hit during the GFC) and emerging markets mandates
- **Private markets investments relative to public markets indexes –1.12%** This result along with the +0.53% return above illustrates the degree to which listed global markets rebounded following the GFC. When we look at private markets – put very simply, not publicly traded – assets we compare their performance with combinations of publicly listed asset classes we believe have similar risk profiles. The valuations of private markets investments are updated infrequently and lag behind developments in public markets. In last year's environment of rapidly rising public markets we found, inevitably, that the gains on valuations of private markets investments did not keep up with those achieved in public markets. We stress that this is a relative return. Comparison aside, the return for these investments was +12.58% year on year.
- **Using alternative tracking indices +0.26%** In some cases we choose to have index – i.e. passive – exposures that are not exactly the same as those specified in the Strategic Asset Allocation (this will also likely occur post the advent of the Reference Portfolio). This is known as 'benchmark mismatch' and is classed as an active investment activity because we have made a decision to actively deviate. For the past year the main such mismatch was holding credit exposure rather than a broader mix of fixed income that included sovereign fixed income. As economic activity recovered, credit outperformed sovereign bonds.
- **Internally executed arbitrage +0.09%.** Last year we saw a number of instances where the prices of securities or indices were different when the underlying securities were purchased individually or in different ways. For example, in the credit markets physical bonds were priced more cheaply then the equivalent derivatives. Our arbitrage strategy takes positions in the cheaper instrument and sells the more expensive instrument to benefit from an eventual convergence of price.

STRATEGIC TILTING +0.77%

We have explained Strategic Tilting on page 21. In the past year we took advantage of many investors selling equities and Real Estate Investment Trusts (REITs) and raised the Fund's exposure to these asset classes, selling down sovereign fixed-income exposure. Equities and REITs subsequently performed strongly, relative to sovereign fixed income, and produced the stated return.

PORTFOLIO COMPLETION

- **Transition portfolios +0.22%.** We manage within the Fund a small number of portfolios comprising relatively illiquid securities. This situation has generally arisen when we have 'taken back' asset portfolios from terminated external managers. The intention is to slowly sell these portfolios as liquidity allows. Last year, improving liquidity in a number of markets saw valuations rebound strongly for many illiquid securities, hence the return.
- **Using derivative rather than physical exposure to passive investment managers +0.06%**. As part of our Portfolio Completion activities we attempt to add value through the judicious use of derivatives as the pricing can be very attractive compared to that for physical passive exposures. Using derivatives also allows us to minimise fees paid to third parties and other transaction costs.
- Other portfolio completion activities together added **+0.01%.**

Portfolio activity (continued)

Investment activity

In this section we discuss actual investment activity, including manager appointments and individual investments.

Appointments and Terminations

In the 2009 Annual Report we detailed how our experiences during the GFC prompted us to think differently about how we should best use external investment managers to benefit the Fund. The below table shows the managers we used in the year to 30 June 2010 and the outcome of our review of those managers, in showing which managers were appointed and which were terminated during the year. The table on the opposite page shows the investments we made during the year, including some via managers. A full list of every third party we invest with is published on our website under

Structuring the Fund/Who Do We Invest With?

MANAGER	MANDATE
AMP Capital Investors	Property and NZ Equities
AQR Capital Management	Multistrategy equities, active Convertible bonds, active
AXA Rosenberg*	Small-cap global equities, active Long-short global equities, active
Barclays Global Investors*	Large-cap equities, active
CP2	Global infrastructure
Elementum Advisors, LLC**	Catastrophe-linked securities
Global Forest Partners	Global timber
GMO*	Large-cap global equities, active Small-cap global equities, active Multistrategy equities
GMO Renewable Resources	NZ timber
Hancock Timber Resource Group	NZ and US timber
ING (NZ) Ltd*	NZ cash, passive NZ credit, passive
LSV Asset Management Limited	Global equities, active Emerging markets equities, active
Milford Asset Management**	NZ equities, active
Morrison & Co Funds Management Limited	Global infrastructure
Numeric Investors LLC	Multistrategy equities, active US small-cap equities, active
Overlay Asset Management*	Currency overlay
Smartshares Ltd*	NZ equities, passive
State Street Global Advisors**	Large-cap equities, passive
Sterling Johnson Capital Management*	Global small-cap equities, active
Thompson, Siegel & Walmsley, Inc.	US small-cap equities, active
Vanguard Investments Australia Limited	Global credit Global listed property
Western Asset Management**	Global credit, active

* Terminated in year to 30 June 2010 (seven managers)
** Appointed in year to 30 June 2010 (four managers)

New investments/commitments made (including via managers where identified)

Note we have provided three case studies on page 30

DATE	TYPE OF INVESTMENT
July 2009	Investment in global tactical asset allocation fund.
September 2009	Commitment to private equity partnership specialising in mid-large scale firms primarily in developed markets including USA and Europe. Likely industries to include media, financial services, professional services, software and information services.
September 2009	Investment in Australian timber.
October 2009	NZ$100 million commitment to Public Infrastructure Partnerships Fund dedicated to small/medium social infrastructure in New Zealand.
November 2009	Investment in private equity real estate partnership specialising in European commercial real estate.
February 2010	US$125 million investment in portfolio of catastrophe-linked securities. Increased to US$300 million in May 2010. **Via manager (Elementum Advisors, LLC)**
March 2010	Investment in absolute return commodities investment fund.
April 2010	NZ$209.8 million commitment to purchase of downstream NZ assets of Shell. **Via manager (Morrison & Co Funds Management Limited)**
April 2010	Commitment to private equity partnership focussed on US companies in distress or requiring capital.
April 2010	NZ$30 million commitment to fund specialising in providing Expansion Capital to high-growth, undercapitalised New Zealand businesses.
May 2010	Investment in fund specialising in investments in non-performing and sub-performing commercial property loans in Japan.
June 2010	Commitment to fund specialising in commodities - agricultural, energy, base metals, precious metals and soft commodities.
June 2010	Investment in fund specialising in stressed/distressed senior debt obligations of US and European small-cap companies.

Portfolio activity (continued)

New Zealand investment activity

We are required to report annually on our progress on the New Zealand Investment Directive received from the Minister of Finance in 2009. This section of the report meets that requirement.

Through our investment activity we apply focussed investment expertise. We invest in long-dated productive assets which few other investors have the ability to consider (e.g. Shell). We have the ability to build the general capabilities and capacity of the New Zealand businesses we invest in. We have a broader ability to grow New Zealand's capital markets, qualitatively and quantitatively through:

- governance practices including Responsible Investment;
- new asset classes (e.g. NZ retail investors got the opportunity to invest in PPPs via the establishment of a retail feeder fund into the Public Infrastructure Partnerships Fund in which we are a cornerstone investor);
- depth/breadth of investment activities; and
- coinvestment with global best-practice funds (of the sort discussed in the CEO's Statement).

Activity in 2009/10

The following information updates the table from our 2009 Annual Report. It summarises what we have done to seek out, consider and make investments in New Zealand.

Opportunities reviewed to 30 June 2010	New commitments/ investments made to 30 June 2010	Outstanding commitments at 30 June 2010	Commitments under consideration at June 30 2010
41	$240 million	$178 million	1.6% of the Fund

Value of NZ investments at 30 June 2010

We have set out below a snapshot of the value of our investments in New Zealand at 30 June 2010 relative to the beginning of the financial year. At 30 June 2010 our NZ investments represented c17% of the Fund (or about 30% including cash). We note that the table shows valuations of actual investments at the end of the year, it does not include relevant commitments made to invest which have not yet been called (and which total some $178 million as per the above table). Nor does it include debtors' and creditors' balances.

Table of investments in New Zealand		
	1 July 2009	**30 June 2010**
Auckland Airport	191.2m	248.8m
Equities	690.4m	804.9m
Private equity	47.8m	47.3m
Property	292.2m	267.6m
Timber	999.1m	1,026.6m
Shell NZ assets	n/a	209.8m
Swaps/other	12.3m	80.6m
TOTAL INVESTMENTS	2,233.0m	2,685.6m

Portfolio activity (continued)

We have undertaken the following New Zealand-specific investment activities in the past financial year.

NZ Direct

The main activity under this strategy was the completion and approval of the strategy itself. It provides capacity to make a small number of significant investments. We have in place a team focussed on the implementation of this strategy. We have been open in providing information to the market about the nature of the investments we would expect to make under this strategy, including collective, co-operative, and Crown-owned assets. We have had a number of discussions regarding potential investments and have progressed two of these to further due diligence during the final quarter of FY2010.

NZ Expansion Capital

Auckland-based Waterman Capital is the first manager to be appointed under this strategy. We have committed $30 million to the Waterman Fund 2 LP. We expect to make at least one further manager appointment in the 2010/11 year. Waterman is already considering a range of potential investments.

NZ Social Infrastructure

We made a cornerstone investment in the Morrison & Co Public Infrastructure Partnerships (PIP) Fund. We note the establishment – and close – of a retail feeder fund to the PIP Fund, providing the opportunity for retail investors to participate. Since the end of the financial year the PIP Fund has made its first investment – the Melbourne Convention Centre. The PIP Fund's mandate permits Australian investments.

Rural Land

We note that this is not a New Zealand-specific strategy. It is global, however there is clear applicability to New Zealand. We expect to appoint a manager under this strategy in the second half of 2010.

Shell

We made a $210 million investment in the downstream NZ assets of Shell. Since the acquisition was formally completed, there has been a considerable amount of activity at the business. Much of this has involved decoupling the business from Shell's offshore-based systems and processes in order to have a fully self-contained New Zealand operation. We have provided more detail on this asset on page 30.

Note: a Statement of Investment Policies, Standards and Procedures (SIPSP) is published on our website www.nzsuperfund.co.nz.

On behalf of the Board and Management of the Guardians of New Zealand Superannuation we hereby certify to the best of our knowledge that the SIPSP has been complied with throughout the 2009/10 financial year.

David May

DAVID MAY
Chairman
13 September 2010

ADRIAN ORR
Chief Executive Officer
13 September 2010

Investment case studies

Shell NZ

In March 2010 we confirmed a NZ$210 million investment in acquiring Shell's New Zealand downstream assets, in a 50:50 partnership with Infratil Ltd. The investment, managed by Morrison & Co, means that returns from the business will now contribute to reducing the tax burden on future New Zealanders' of the cost of New Zealand Superannuation.

What did we invest in?

The network of downstream assets supplies approximately 30% of New Zealand's fuel and comprises:

- A 17.1% stake in the NZ Refining Company;
- Ownership of and access arrangements to storage terminals and pipelines;
- A marine refuelling business;
- Facilities at Auckland and Christchurch airports;
- Over 220 Shell Service Stations nationwide;
- Nearly 100 truck stops; and
- 25% ownership of Loyalty New Zealand ('Fly Buys').

First shipment of 'Kiwi oil'.

Why did we make this investment?

All investments made by the Guardians must be prudent and commercial and must contribute to the Fund meeting its purpose.

We saw the investment in Shell's downstream NZ assets as consistent with those requirements because the network is a top-quality infrastructure asset, bought at a very attractive price. It is a long-term business and so is a good fit for an investor with a long-term investment horizon; it produces robust, stable, long-term cashflows; it is a market leader; it contributes well to the diversification of the Fund and finally there is significant ability to add value to it over time.

What has happened since the acquisition?

The initial priority for the board and management has been on ensuring that the transition to NZ ownership goes as smoothly as possible. Behind the scenes there has been considerable activity. Much of this has involved decoupling the business from Shell's offshore-based system and processes in order to have a fully self-contained New Zealand operation. However decisions have been made which have already had some positive impacts, including:

- A new Board under Chair Marko Bogoievski and a new management team under CEO Mike Bennetts;
- Implementation of core IT, payroll and management reporting infrastructure;
- Establishment of new supply contracts;
- Creation of 40 jobs including 'in-sourcing' 12 call centre roles;
- Lease signed for a new service station site at Bethlehem, near Tauranga; and
- $2 million investment in a new service station site on Auckland's North Shore.

On 25 June 2010 we saw the arrival of the first full delivery – 690,000 barrels – of 'Kiwi-owned' oil at Marsden Point aboard the *Pacific Leo*, as seen in the picture.

Catastrophe reinsurance

In February 2010 we awarded a mandate to Chicago-based Elementum Advisors, LLC., to invest in natural catastrophe reinsurance products. We made an initial investment of US$125 million which increased to US$300 million in May 2010.

What did we invest in?

Catastrophe bonds (and other insurance-linked securities) are a way for capital markets to provide reinsurance to the insurance industry. Essentially they cover natural catastrophes such as major hurricanes, earthquakes and bushfires in areas where such events present a low but genuine risk.

They exist as a way to spread the risk and the cost of major catastrophic events that are unlikely to occur but which are very expensive when they do.

Our investment is mostly in securities that cover US hurricanes and earthquakes, with some products covering European wind storms and Japanese earthquakes. We have not made similar investments in New Zealand because of organisations such as the Earthquake Commission.

Why did we make this investment?

We invested in catastrophe bonds during the GFC. Investors had become very risk-averse but the risk of natural catastrophes was not affected by the GFC. The GFC enabled us to get an attractive premium for an income stream completely uncorrelated with financial markets.

For an investor, the rationale is the income stream derived from the premiums paid on the policies in the pool. The insurance industry values this back-up insurance, and pays attractive premiums to investors to provide it. Without investors fulfilling this role, insurance for householders in high-risk areas would be more expensive.

Should a relevant catastrophe occur, the bond may be triggered. Triggering depends on the size and severity of the catastrophe. Triggering constitutes a requirement to pay out, but the size of the payment is capped to a maximum agreed by the investor.

Spotlight Activity in third-party funds and manager portfolios

Direct Capital IV minority investment in Bayleys Corporation Limited

In June 2010 Direct Capital completed the second investment from its Direct Capital IV fund, into Bayleys Corporation Limited. The Fund invests in mid-sized private New Zealand companies that typically require further capital to continue growing their business, expand into Australia, or to assist with ownership succession.

Bayleys had seen the recession as an opportunity to grow its business and extend its services but required capital to do so. Coming off the back of a record earnings year, Bayleys had the financial base to grow without taking on a financial partner but, as it wished to grow quickly, taking on a partner made strategic sense.

The growth programme to which Direct Capital's investment will contribute is aimed at increasing the scope and depth of agency services Bayleys provides for its clients throughout New Zealand – particularly in property management, valuation services and funds management.

Value for Money

Our investment decisions are based on expected net return, which requires us to weigh up the certainty of incurring cost against expectations of higher long-term returns.

We continue to make considerable efforts to manage and control the costs of running the Fund given their importance to the Fund's bottom line return. These activities are in line with our investment beliefs, our investment mandate that necessitates we invest on a commercial, prudent basis, and the Government's expressed desire for fiscal prudence.

Over the course of this financial year we have incurred lower overall costs by 12.6 basis points, or NZ$10.6 million over the prior year, as set out on page 54. This is a cost reduction relative to the size of the Fund, and to our budgeted expectations.

Most of our cost control has come from our increased use of direct investment (e.g. choosing to acquire investment exposure through derivatives), in large part facilitated by our increased internal capacity to manage our portfolio completion. In that sense, overall costs have declined as a proportion of Funds, despite a higher headcount at the Guardians.

In broad terms, we manage costs as follows:

First, we only appoint external investment managers and pay base fees when we are confident that a manager is:

- operating in an investment environment conducive to generating investment returns greater than what can be gained through passive exposure (i.e. active returns);
- utilising a sound investment strategy; and
- satisfying our due diligence hurdles.

In this regard, our manager costs will vary, dependent upon our confidence in achieving a net postive return from the use of external active managers.

Second, we only pay manager performance fees when their returns over time are greater than a benchmark hurdle. In this regard, paying performance fees is a good 'problem' for the Fund.

Over the course of this year considerable effort has gone into investigating investment environments that are conducive to excess returns. This has resulted in us terminating some external manager relationships (as outlined on page 24). Again, this experience will vary, dependent upon our success at gaining access to sound active investment opportunities.

Third, we annually benchmark the Fund's cost structure against its identified 'peer' funds. We do this via the CEM Benchmarking Survey, which compares the Fund's cost structure for the five years ended 31 December 2009. At the time of writing this Annual Report, we only had a draft CEM survey for the calendar 2009 year. The draft covered 321 global funds, with assets totalling approximately $US6 trillion. Twenty funds from Australia, Canada, Europe and the United States were assessed by the draft survey as being in our peer group, selected on the basis of broadly comparable fund size and investment activity.

The draft concludes that our total costs are slightly below our peer group, and the Fund's investment performance is consistent with the same peer group. We caution that these results need to be finalised. A full analysis of the CEM comparison will be made available in due course.

The Fund's Reference Portfolio also enables us to compare our value-add from actively investing. We discuss our value-add performance against the passive alternative (i.e., the Reference Portfolio) on page 23 of this Report. In short, our value-add returned to positive territory for the year (0.85bps). This follows a significant negative outcome during the GFC, almost solely due to our external multi-strategy managers. This is the group of managers that we have focussed on the most change over the past 12 months (again, as outlined on page 24).

Transparency

We are conscious that the ultimate beneficiaries of the Fund are future New Zealand taxpayers. We also acknowledge that internationally we represent New Zealand and that this is reflected in our statutory duty to manage the Fund and invest it so as not to prejudice New Zealand's reputation in the world community. We believe that the best way for others to judge whether we are actually doing this to be as open as possible about what we do, why, and the outcomes. External judgement of our activities can then be based on facts. Accordingly, transparency is crucial to the preservation of our reputation and we believe that the degree of our transparency is best judged by third parties.

We implement this belief in a number of ways:

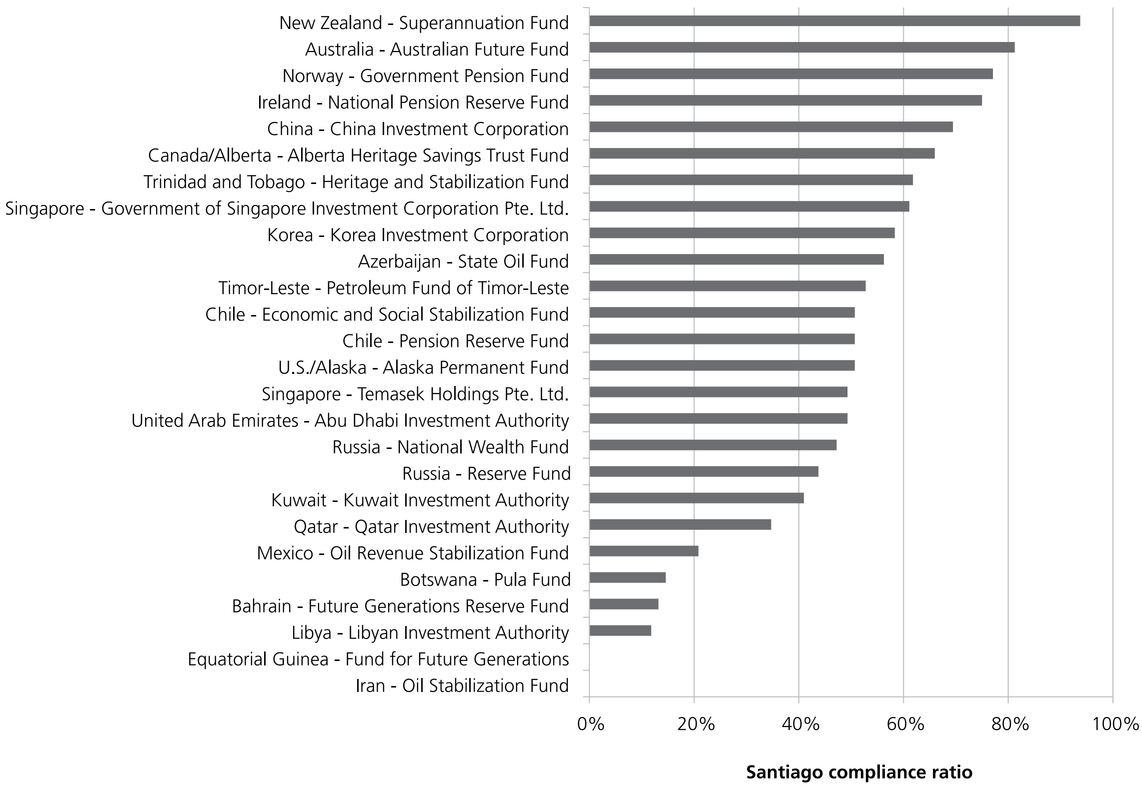
1. Our website is a comprehensive store of information about why the Guardians and Fund exist, how we make investment decisions, why we make them that way, what we have invest in, who we invest with, and how the Fund performs. We have tried to make the site easy to navigate and to use simple language to aid understanding. We welcome your feedback on this point, via the website.
2. We publish independent reviews of all aspects of our management and governance of the Fund. This year alone we have published:
    a. a full copy of the independent review of our governance of the Fund done by Mercer at the request of the Minister of Finance (see page 39). The review, which is required every five years, is available on our website together with our recommendation-by-recommendation response.
    b. a copy of the assessment by the Office of the Auditor General (OAG), of our progress on recommendations in the OAG's 2008 review of our governance and management of the Fund. The assessment concluded that the OAG was satisfied that we were committed to implementing the recommendations. It is available on our website.
    c. our performance in the CEM survey comparing the Fund's total cost structure to peers is on page 33 of this report.
    d. our performance, as assessed by the secretariat of the United Nations Principles for Responsible Investment, in implementing the principles is on our website and discussed further on page 138.
3. We monitor our performance in transparency surveys. Currently, there are not many such surveys and only one which is done regularly: the Linaburg-Maduell Transparency Index published by the San Francisco-based Sovereign Wealth Fund Institute on its website www.swfinstitute.org. The survey records a mark out of 10 and is based on the Institute's view of what an average person would expect to find out, easily, about a particular Sovereign Wealth Fund (SWF) from the Fund itself. The Guardians have rated 10/10 since the inception of the index and we intend to stay that way.
4. We also publish how we are rated by other such mechanisms, as we become aware of them (and if we regard them as relevant and credible). In May 2010 one such survey was published by the Washington-based Carnegie Endowment for World Peace. It was based on the Institute's assessment of each of the 26 signatory SWF's implementation of the Santiago Principles (see below) and we were rated a clear first among all such funds.

We are aware that third-party surveys are not perfect indicators of transparency. We are also aware that the comparative nature of such surveys is problematic, as the purpose and – most important – the nature of the beneficiaries of our peer SWFs is the key determinant of what is desirable and appropriate for each to disclose.

However, for a Fund with our purpose and with current and future New Zealanders as our stakeholders and beneficiaries, a high degree of transparency verified as such by third parties is important.

Note: We annually review and publish our implementation of the Santiago Principles, a set of best practice behaviours.

Figure 1. Santiago Compliance Index as of March 2010



The Guardians (along with other top performers in the survey): "...provides sufficient and detailed information about its policy objectives, governance arrangements, funding and withdrawal arrangements, financial positions, and overall investment policy, including information about non-financial and non-economic considerations that might drive investment behaviour."

– Sven Behrendt, Carnegie Endowment for World Peace

Responsible Investment

What is Responsible Investment?

Like many institutional investors, we invest with a long-term focus. We recognise that environmental, social, and governance (ESG) issues are long-term factors that can be highly relevant to investment performance. ESG issues present regulatory, market, reputational, and operational risks and opportunities which shareholders should consider to fully understand the companies in which they invest.

Responsible investment (RI) is, therefore, the 'integration of ESG considerations into investment management practices in the belief that these factors can have an impact on financial performance[1]'.

Our Beliefs

We believe ESG analysis should be integrated into traditional investment analysis across asset classes, and mainstreamed into the investment process.

We see an opportunity in developing the investment strategy for the Fund, to systematically consider ESG issues, with the objective to better manage long-term risks and maximise investment opportunities. This aligns with our two core RI beliefs:

1. responsible asset owners who exercise best-practice portfolio management should have concern for environmental, social, and governance (ESG) issues of companies; and
2. improving ESG factors can improve the long-term financial performance of a company.

We have adopted the UN Global Compact principles as a benchmark for expected standards of corporate behaviour. We have adopted the UN Principles for Responsible Investment (UNPRI) as an internationally accepted framework for investors to manage ESG issues in a manner consistent with improving long-term investment returns. These ESG standards and beliefs form the basis of our RI policy.

1. Mercer Investment Consulting

How we integrate ESG

Having identified the importance of integrating ESG considerations into investment analysis and the investment process, how do we actually go about it? Broadly, we do this in five ways:

Beliefs, policies, standards and procedures	Our investment beliefs, policies, standards and procedures, underpin all of our investments across investment selection, due diligence, execution, management, monitoring and reporting. We have already discussed above our core RI beliefs which are integrated within this investment process.
Engagement	This takes two forms: a. engagement with investee companies on ESG issues, either directly with the company ourselves or – more likely, given our size – in collaboration with other investors with a similar ESG focus. This can be achieved by voting at company meetings or partnering with other UNPRI signatories; and b. engagement with regulators on frameworks relevant to ESG and investment issues.
Portfolio Monitoring and Exclusions	Monitoring the Fund for any companies that are in breach of ESG standards and monitoring our exclusions.
Communication	This takes two forms: a. through reporting the outcomes of our Responsible Investment activity on our website and via our Annual Reports; and b. through benchmarking every aspect of what we do in our Responsible Investment programme through the UNPRI signatory assessment. We make the assessment public and have set targets for our performance relative to other signatories in our 2010 Statement of Intent.
Collaboration	Through understanding, sharing and learning best practice. Participation in initiatives and organisations such as the Climate Disclosure Project, the UNPRI, the Investor Group on Climate Change, the Responsible Investment Association of Australasia and the collaboration initiative we lead here with New Zealand Crown Financial Institutions.

For a full report on how we have integrated ESG in 2009/10, see our Responsible Investment Report on page 132.

Reporting against the 2009/10 Statement of Intent

In this section we report on our progress against the expectations and goals we set out in the Statement of Intent (SOI) for 2009/10 – in particular, in the Forecast Statement of Service Performance from that document.

Fund Performance

We are legally required to outline our expectations of the performance of the Fund over each financial year. As we have said many times, predicting short-term financial markets returns with any useful accuracy over such a near-term horizon is impossible. At best we can use our modelling techniques to provide a range of likely outcomes and outline the mid-point of this range.

This is the basis on which we estimated our return for 2009/10 in the 2009 SOI. In that document we estimated that the mid-point of our estimated range for the Fund return over the next 10 years, after costs but before tax, would be 10.7% p.a. The actual return for 2009/10 was 15.45%.

However, like the previous financial year, this year's performance compared to our forecast illustrates the challenges – and relevance – of short-term predictions. Of more relevance is how this year's return fits into the overall performance of the Fund since inception. That is illustrated in the graphs on pages 2 and 3.

Statement of Service Performance

In the 2009 SOI we set out a number of key financial and non-financial outputs relating to asset allocation, portfolio management, value-add through active management and third-party evaluations of our governance of the Fund by parties including the UNPRI, the five-yearly Independent Review and the Generally Accepted Principles and Practices (GAPP) for Sovereign Wealth Funds.

These are ongoing measurement criteria and will, naturally, be reported on in each Annual Report. In this document they are covered on the following pages:

Output	Relevant Benchmark	Relevant Target	Comment
Determining an optimal mix of market exposure	NZ 90-day Treasury Bills	Treasury Bills + 2.5% p.a.	The Fund outperformed T-Bills by 12.85% for the year. Since inception Fund performance is 0.52% below T-Bills, see page 2 (and also page 7 to set performance in context as the Fund is less than seven years' invested)
Best-practice portfolio management	% return on index matching Strategic Asset Allocation (SAA)	Match index	The Fund outperformed the passive alternative by 0.83% for the year. Since inception Fund performance is 0.28% below the passive alternative. See page 3.
Adding value through active management	Zero net of all fees	+0.50% p.a. relative to passive benchmark	The Fund outperformed the passive alternative by 0.83% for the year. See page 23 for an analysis of active management activity.
UNPRI rating	Peer comparison	Top quartile Australasia, top half globally	Top quartile for five out of seven categories Asia/ Pacific, top half for five out of seven globally (all five top quartile). See page 138 for global scores.
Peer evaluation	Five-year performance Auditor General feedback	Positive	See information on our peer review approach pages 12-15. Also see page 34 for information about the progress report from the Office of the Auditor General (OAG), relating to our implementation of the recommendation in the OAG's 2008 review of our governance and management of the Fund.

Output	**Relevant Benchmark**	**Relevant Target**	**Comment**
Independent Review	n/a	Positive	See below table.
GAPP	GAPP Assessment	Meet all principles	Assessed as most GAPP-compliant SWF by Carnegie Endowment for World Peace. (See page 34).
Independent studies	Best practice as determined by study	Top quartile or equivalent	See Linaburg-Maduell Transparency Index on page 34. See also the draft conclusions from the CEM survey of our cost-effectiveness on page 33. The Carnegie survey also meets the criteria for this output (see page 34).

Within the broader set of criteria we identified four projects with particular relevance for this financial year.

Project	Relevant Benchmark	Relevant Target	Comment for 2009/10
Review of Strategic Asset Allocation	NZ 90-day Treasury bills	+ 2.5% p.a.	Review substantially complete by end of 30 June 2010. Expected to be complete and consequent new asset allocation implemented by 30 September 2010. Key outcome is creation of Reference Portfolio. (See page 16).
Implementation of Strategic Tilting	Zero net of all fees	+ 0.10% p.a. (element of 0.85% p.a.)	Strategic tilting implemented. Contribution to Fund return for 2009/10 0.77% (see page 23).
Focus on cost efficiency, including embedding of Treasury unit	Zero net of all fees	Contribution to + 0.50% p.a.	Treasury unit completed as part of completion of broader portfolio completion strategy aimed at identifying and avoiding or mitigating cost. Contribution of portfolio completion to Fund return for 2009/10 0.29% (see page 23).
Independent Review commissioned by Minister of Finance	n/a	Positive review	In 2009 Mercer was appointed by the Minister of Finance to conduct the second of the required five-yearly reviews of our governance of the Fund. The terms of reference of the review was specified by the Minister. The review report was published in November 2009 (including on our website) and we welcomed the conclusions, most of which endorsed our current practices. We also published to the website our initial response to each recommendation. In parallel with the writing of this report we have updated those responses. They are available on our website **www.nzsuperfund.co.nz** under *Performance/ Independent Reviews.*

Governance

In this section we report on how the Guardians observed each of the Securities' Commission's corporate governance principles in the year to 30 June 2010.

PRINCIPLE 1 Directors should observe and foster high ethical standards

The Board has adopted a Board Charter incorporating Codes of Conduct for Board members. The Charter is available on our website under *Who We Are/Our Board.*

We also have Codes of Conduct. The Codes provide Board members and employees with clear expectations of ethical standards expected at the Guardians. The Codes of Conduct address:

- professional conduct and duties of Board members and employees;
- conflicts of interests;
- confidentiality;
- securities markets legal obligations;
- use of Guardians' information and assets;
- receipt of gifts and entertainment;
- political participation; and
- whistle blowing.

A copy of the Code of Conduct for employees is available on our website under *Who We Are/Our Management.*

For Board members, actual or potential conflicts of interest are managed in accordance with the requirements of the Guardians' governing legislation. Codes are reviewed regularly as part of the Guardians' Legislative Compliance Framework.

PRINCIPLE 2 There should be a balance of independence, skills, knowledge, experience, and perspectives among directors so that the Board works effectively

The skills and attributes required to be a Board member are set out in the Act. Board members are chosen for their experience, training, and expertise in the management of financial investments, as well as their mix of complementary skills.

Board members are appointed by the Governor-General on the recommendation of the Minister of Finance. The Minister's recommendation follows nominations from an independent nominating committee established by the Minister. On receiving those nominations, the Minister consults with representatives of other political parties in Parliament before recommending the Governor-General appoint a person to the Board.

The Board must comprise of at least five, but no more than seven, members. Each Board member is appointed for a term of up to five years and is eligible to be reappointed. The first Board members were appointed in August 2002.

The Board composition at 30 June 2010 with details of individual Board members' background is set out in the table below. We note that Glen Saunders left the Board at the end of his term in September 2009 and Bridget Liddell left the Board at the end of her second term in June 2010. David Newman was appointed Deputy Chair in November 2009. Catherine Savage and Stephen Moir joined the Board in November 2009. Gavin Walker joined the Board in July 2010.

Name	**DAVID MAY, Chairman**
Term of office	Appointed August 2002 for five years and reappointed September 2007 for five years.
External directorships	Deputy Chairman, Government Superannuation Fund Authority and Director of Southern Cross Medical Care Society and Annuitas Management Limited.
Skills, experience, and expertise	David has 35 years' experience in the financial services, superannuation, and insurance industries, including 27 years with Colonial Group, most recently as Managing Director of Colonial Life NZ Ltd (1995–2000).
Standing Board committee membership	Chairman of the Employee Policy and Remuneration Committee and member of the Responsible Investment Committee[1].

Name	**DAVID NEWMAN, Deputy Chairman**
Term of office	Appointed September 2004 for five years and reappointed November 2009 until September 2011.
External directorships	Chairman of Infratil Limited and its subsidiary Wellington International Airport Limited and a Director of Infratil Airports Europe Limited. David is also Chairman of Loyalty New Zealand Limited, operator of Fly Buys loyalty card programme, and of the Centre for Biodiversity and Restoration Ecology at Victoria University of Wellington.
Skills, experience, and expertise	David was previously Chief Executive Officer of the Institute of Directors in New Zealand. Prior to this, David spent 22 years with BP, culminating in four years as Chief Executive and Managing Director of BP New Zealand Limited.
Standing Board committee membership	Chairman of the Audit Committee[2].

Name	**MARK TUME**
Term of office	Appointed April 2006 for five years.
External directorships	Director of the New Zealand Railways Corporation (KiwiRail), Infratil Limited and the The New Zealand Refining Company.
Skills, experience, and expertise	Over his 20-year career, Mark has held a variety of senior roles within the finance sector, in areas such as investment banking, capital markets, asset and liability management, and risk control. He was a former President of the New Zealand Financial Markets Association, and ACC's External Maori Reference Group.
Standing Board committee membership	Member of the Audit Committee[2].

1. See page 44 regarding the Responsible Investment Committee.
2. See page 44 regarding the Audit Committee

Governance (continued)

Name	JOHN EVANS
Term of office	Appointed December 2006 for five years.
External directorships	Managing Director of PGE Australasia Pty, an actuarial company specialising in the application of quantitative techniques to investment business. John holds a number of other directorships, including Emerging Leaders Investment Ltd, and is actively involved with various committees at Fiducian Portfolio Services, a specialist financial services organisation.
Skills, experience, and expertise	John is also Associate Professor in Actuarial Studies at the University of New South Wales and Deputy Director of the Centre for Pensions and Superannuation
Standing Board committee membership	Member of the Audit Committee[2].

Name	CATHERINE SAVAGE
Term of office	Appointed November 2009 for five years.
External directorships	Managing Director of CMS Capital Limited, Director of Todd Family Office Limited, Comrad Holdings, NZX Incognito and Pathfinder Asset Management. Chairman of the National Provident Fund.
Skills, experience and expertise	Catherine was Treasurer of the National Gas Corporation from 1991-1993 prior to moving to AMP Capital Investors (NZ) Ltd where she worked in various senior management roles to 2000 when she became the Managing Director - AMP's youngest and only female country manager.
Standing Board committee membership	Member of the Employee Policy and Remuneration Committee.

Name	STEPHEN MOIR
Term of office	Appointed November 2009 for five years.
External directorships	Stephen is a non-executive director of the Bank of New Zealand and a member of the NZX Discipline Panel.
Skills, experience, and expertise	Stephen has more than 25 years of experience in financial services, including being the General Manager of the Westpac Institutional Bank from 1998-2001, preceded by senior positions with Credit Suisse in Singapore, Citibank in Singapore, Bangkok and Sydney.
Standing Board committee membership	Member of the Audit Committee[2] until August 2010. Member of the Employee Policy and the Remuneration Committee from August 2010.

1. See page 44 regarding the Responsible Investment Committee.
2. See page 44 regarding the Audit Committee

Name	**GAVIN WALKER**
Term of office	Appointed July 2010 for three years.
External directorships	Gavin is a Director of Lion Nathan National Foods (formerly Lion Nathan Ltd) since 2000 and in 2010 became a director of ASB Bank and Sovereign Insurance.
Skills, experience and expertise	Gavin has extensive experience in investment banking and funds management including being CEO of the Banker's Trust in both New Zealand and Australia. He is a past chairman of the Foreign Direct Investment Advisory Board and a past director of BT Investment Management Limited, the Southern Cross Building Society and of Goodman Fielder Limited. Gavin has a BCA from Victoria University. He is a member of the New Zealand and Australian Institutes of Directors and the Institute of Financial Professionals.
Standing Board committee membership	Member of the Audit Committee[2] from August 2010.

Board members who left the Board during the financial year

Name	**BRIDGET LIDDELL, CFA**
Term of office	Appointed August 2002 for three years and reappointed June 2005 for five years ending May 2010.
External directorships	Chairman of the US Beachhead Programme, a programme run by New Zealand Trade and Enterprise to assist New Zealand companies with entry to the US market, and a Director of the New Zealand Institute, a privately funded non-partisan think-tank, and of BioVittoria, a New Zealand biotechnology company.
Skills, experience, and expertise	Before moving to the US in 2003, Bridget was Chief Executive Officer of University of Auckland Development Ltd. Bridget has been a Director of several New Zealand companies, including Sky City Entertainment Group, Fisher & Paykel Appliances Holdings Ltd, and Uniservices Ltd. Bridget has held senior executive positions at Carter Holt Harvey and was a Director of CS First Boston NZ Limited.
Standing Board committee membership	Member of the Responsible Investment Committee[1] and Employee Policy and Remuneration Committee.

Name	**GLEN SAUNDERS**
Term of office	Appointed September 2004 for five years ending September 2009.
External directorships	Board member of UNRPI, a non-executive Director of Sustainable Investment Research Institute Pty Ltd, and a Director of Prometheus Finance Ltd.
Skills, experience, and expertise	A consultant, investment banker, and qualified accountant, Glen was previously UK Managing Director of Netherlands-based bank, Triodos. He is a former Director of the Wind Fund plc and the Local Investment Fund, a public-private partnership funding community-based initiatives in the UK. Glen has also served as Non-Executive Director of the Western Partnership for Sustainable Development and the Earth Centre Advisory Board.
Standing Board committee membership	Chairman of the Responsible Investment Committee[1] and a member of the Employee Policy and Remuneration Committee.

Governance (continued)

The Guardians' governing legislation and the Board Charter define Board responsibilities, responsibility of individual Board members, as well as matters reserved for the Board and matters delegated to management. The Board Charter and the Guardians' governing legislation is available on our website.

While the day-to-day responsibility for the operation of the business is delegated to the executive, there are a number of matters which, either because it is required by law or because the Board has decided it is in the interests of the Guardians to do so, are decided only by the Board as a whole.

The Board makes considerable efforts to keep up to date with investment markets and with global best practice. External experts regularly address the Board on emerging economic themes and risks and on the developments in, and changing return expectations from, the many different sectors of the investment markets.

Board members visit and review global peer funds to compare investment strategies and governance and organisational issues. Every year independent experts are invited to the Board strategy day to assist in the review of strategies and plans and to suggest where they can be improved, in the light of developing best global practice. Periodically, the Board uses an external independent adviser to review the collective and individual performance of the Board and to make suggestions on areas for improvement.

PRINCIPLE 3 The Board should use committees where this would enhance its effectiveness in key areas while retaining board responsibility

The Board had three standing Board committees during the 2009/10 financial year:

- **Audit Committee:** Oversees financial reporting, internal and external audit, operational and legislative risk, compliance (including tax compliance), and other governance systems. In August 2010 the Audit and Risk Committee was renamed the Audit Committee and the terms of reference changed to concentrate its oversight on legislative and operational risk, with the full Board focussing on investment and strategic risk.
- **Responsible Investment Committee:** Oversees the implementation of the ethical investment policy (under Section 61(d) of the Act) and the policy for the exercise of voting rights (under Section 61(i) of the Act). In light of embedding these policies in the business of the Guardians, the Committee was disestablished in October 2009 with the Board directly overseeing the observance of these policies.
- **Employee Policy and Remuneration Committee:** Oversees the development and operations of employment and remuneration policies.

The roles and responsibilities of the Board committees are set out in the respective Committee's Terms of Reference. Copies of the Terms of Reference are available on the our website. Minutes of the meetings of each committee are provided to the Board. In addition, all Board members are able to attend any Committee meeting.

In addition, from time to time, the Board may establish specific sub-committees to address a particular matter or for a particular purpose. This allows the Board to function effectively and to apply its conflicts of interest procedures.

The Board committees meet either quarterly or are convened as necessary. Each committee is entitled to the resources and information it requires to operate effectively. The Chief Executive Officer and senior executives are invited to attend committee meetings as necessary.

The Board met 9 times during FY 2009/10, and its standing committees held nine meetings. The table below reflects the number of meetings attended by each Board member relative to the total meetings that Board member could have attended.

Meeting Type	Board	Audit Committee[2]	Responsible Investment Committee[1]	Employee Policy and Remuneration Committee
Number of meetings	9	4	1	4
David May	8/9	2/0	1/1	4/4
Stephen Moir	6/6	2/2		
Bridget Liddell	7/8		1/1	2/2
David Newman	9/9	4/4		
Mark Tume	9/9	4/4		
Glen Saunders	n/a		1/1	2/2
Catherine Savage	6/6			2/2
John Evans	9/9	4/4		

Note that Glen Saunders and Bridget Liddell left the board during the financial year and Catherine Savage and Stephen Moir joined the Board in the financial year. Gavin Walker joined the Board on the first day of the 2010/11 financial year.

PRINCIPLE 4 The Board should demand integrity both in financial reporting and in the timeliness and balance of disclosures on entity affairs

As a Crown entity the Guardians must meet all its obligations in respect of the Guardians and the Fund under the Act, the Crown Entities Act 2004, and the Public Finance Act 1989, including tabling the Annual Report in the House of Representatives. The Annual Report is available to the public in hard copy and on our website. The financial statements for the Guardians are signed by the Chairman of the Board and another Board Member. The Financial Statements for the Fund are signed by the Chairman of the Board and the Chief Executive Officer

The Guardians are required by the Crown Entities Act 2004 to prepare a Statement of Intent. The Statement of Intent for the five years from 2010 to 2015 was tabled in the House on 24 May 2010. The Guardians also report quarterly to the Minister with a written report on progress of the Fund and the Guardians.

1. See page 44 regarding the Responsible Investment Committee
2. See page 44 regarding the Audit Committee

Governance (continued)

PRINCIPLE 5 The remuneration of directors and executives should be transparent, fair, and reasonable

The remuneration of Board members is set by the Minister of Finance operating in accordance with the Fees Framework for Members of Statutory and Other Bodies Appointed by the Crown.

Members' remuneration is disclosed in Note 12(c) to the Guardians' financial statements.

The objective of the staff remuneration strategy is to provide competitive remuneration aimed at attracting and retaining competent people, and aligning rewards with achievement of financial and non-financial targets. Staff remuneration comprises base or fixed remuneration and a long-term incentive scheme based on the achievement of organisation and financial performance targets.

Further details concerning staff remuneration are disclosed in Note 13 to the Guardians' financial statements. We also note a proposed new discretionary bonus scheme applying from 1 July 2010 onward, this is outlined on page 52.

PRINCIPLE 6 The Board should regularly verify that the entity has appropriate processes that identify and manage potential and relevant risks

The Board is responsible for reviewing and approving the Guardians' risk management strategy. The Board delegates day-to-day management of risk to the Chief Executive Officer and, as appropriate, other staff. Inherent in this delegation is the belief that responsibility for managing risks at the Guardians is the domain of the relevant business unit.

The Audit Committee reviews the reports of management and the external and internal auditors on the effectiveness of systems for internal control, financial reporting, and operational and legislative risk management. The committee reports to the Board on changes to the risk management framework and to risk records overseen by the Audit Committee. To assist in discharging this responsibility, the Board has in place a number of strategies designed to safeguard the Fund's and Guardians' assets and interests and ensure the integrity of reporting.

PRINCIPLE 7 The Board should ensure the quality and independence of the external audit process

The Audit Committee is responsible for overseeing the external audit of the Guardians and the Fund. Accordingly, it monitors developments in the areas of audit, and threats to audit independence, to ensure its policies and practices are consistent with emerging best practice in these areas.

The external auditors are not permitted to perform non-audit work assignments.

The Auditor-General appoints the external auditors of the Guardians and the Fund. The external auditor is Brent Penrose of Ernst & Young.

PRINCIPLE 8 The Board should foster constructive relationships with shareholders that encourage them to engage with the entity

The Guardians is a Crown entity and its assets, and the assets of the Fund, form part of the Crown's assets. The Guardians are accountable to Parliament, through the Minister of Finance, for those assets. The Guardians' Statement of Intent for the five years from 2010 - 2015 is published on our website and will be reported against in the Annual Report next year. The Guardians report to the Minister on the Fund at those intervals that the Minister may require and currently the Guardians provide a quarterly written report on the Fund's progress.

Under the governing legislation, the Minister may give directions regarding the Crown's expectations as to the Fund's performance, including its expectations as to risk and return. However, the Minister may not give any direction that is inconsistent with the duty to invest the Fund on a prudent, commercial basis. The Guardians must have regard to any such direction and must notify the Minister how it proposes to do this, as well as report the direction in the Annual Report. Any direction given by the Minister must be tabled in Parliament. We received a direction in May 2009 but have received no directions in the current financial year.

The Act and the Crown Entities Act 2004 provide more information on the role and responsibilities of the Minister and are available on our website.

PRINCIPLE 9 The Board should respect the interests of stakeholders within the context of the entity's ownership type and its fundamental purpose

The Guardians published its Statement of Intent under the Crown Entities Act 2004 in May 2010. This set out the broad parameters of work for the five years from 2010 to 2015 and a detailed plan for FY2010/11.

Objectives set out in the Statement of Intent for the 2009-10 financial year are reported against on pages 38 - 39 of this report.

Governance (continued)

Adrian Orr

Neil Williams

Matt Whineray

Management Team

To ensure high-quality decision-making, our management team operates through a series of internal executive committees. These committees include the:

- Leadership Team: dealing with the business operations of the Guardians;
- Investment Committee: advising on the investment decisions of the Guardians; and
- Risk and Portfolio Monitoring Committee: advising on the performance of the Fund and the Guardians' service providers.

In planning for growth, we have refined our organisational structure to support the overall business strategy. In particular, we have designed the structure to deliver:

- alignment to the Guardians' strategies and mandate;
- focus on driving performance and accountability;
- clarity around processes within the organisation;
- additional capability;
- support of clear governance;
- leverage of economies of scale and skill across the Guardians; and
- assurance the cost of doing business is managed appropriately.

Below are brief profiles of the Leadership Team.

Adrian Orr, Chief Executive Officer: Responsible for general management of the Guardians under delegation from the Board. Adrian joined the Guardians in February 2007 from the Reserve Bank of New Zealand where he was Deputy Governor and Head of Financial Stability. Adrian has held the position of Chief Economist at Westpac Banking Corporation, Chief Manager of the Economics Department of the Reserve Bank of New Zealand, and Chief Economist at the National Bank of New Zealand. He also worked at The Treasury and at the OECD.

Neil Williams, General Manager Asset Allocation: Responsible for investment in listed markets and for the overall Fund investment completion (i.e. the use of derivatives, cash management and rebalancing). Neil joined the Guardians in May 2008 from UBS Global Asset Management in London where he was Global Head of Asset Allocation and a Managing Director in Global Investment Solutions. Neil was previously Chief Global Strategist, Executive Director for Goldman Sachs International (London).

Matt Whineray, General Manager Investments: Responsible for investment activity in alternative assets and the appointment of investment managers. Matt joined the Guardians in May 2008 from Credit Suisse (Hong Kong) where he was Head of Financial Sponsor Coverage for non-Japan Asia. Prior to this, Matt was a Managing Director of First NZ Capital and a Vice President at Credit Suisse First Boston (New York). Matt began his career as a Barrister and Solicitor with Russell McVeagh.

Tim Mitchell, General Manager Corporate Strategy: Responsible for the Guardians' overall strategy in best-practice activities, including best-practice portfolio management, responsible investment, legal, and communications. Tim joined the Guardians in April 2003. He was previously a consultant to the Board with responsibility for establishing the Guardians' infrastructure and policies. Prior to that, Tim was a principal advisor at The Treasury. Before moving into the public sector, he spent seven years with Colonial First State Investment Managers, most recently as Chief Investment Officer.

Mark Fennell, General Manager Operations: Responsible for developing and overseeing investment operations and information technology. Mark joined the Guardians in July 2007 from The Warehouse Group where he was the Company Secretary and Chief Risk Manager. Mark also has significant public sector experience, working in a senior finance position for the Ministry of External Relations and Trade and for State Owned Enterprises (Forestry Corporation and NZ Railways Corporation).

Stewart Brooks, General Manager Finance: Responsible for financial control, tax, and internal and external audit. Stewart joined the Guardians in August 2003 from Sterling Grace Portfolio Management Group, where he was Group Company Secretary. Stewart was previously Financial Controller for Motorola Cellular and worked in private equities for seven years. Prior to this, he worked for a computer multinational in the UK.

Janet Gallagher, General Manager Human Resources: Responsible for people, performance and culture. Janet joined the Guardians in May 2007 after eight years managing her own HR consultancy business. Previously Janet held senior HR positions with Lion Nathan, NZI Life and New Zealand Dairy Foods.

Tim Mitchell

Mark Fennell

Stewart Brooks

Janet Gallagher

Our team

We recognise the benefits to our organisation of having a breadth of skills and experience among our employees. We also recognise the benefits of being able to recruit, retain and develop high-quality people. To us this means our people must enjoy and feel safe in their workplace; trust the processes and procedures around their development, recognition, promotion and exit; and be enthused about and professionally satisfied by their roles.

If we can consistently achieve this for our people we believe that we will succeed in achieving our long term business goals, and continue to improve our Good Employer and Equal Employment Opportunity practices.

EEO STATISTICS

Diversification is a business enabler. It is one means of avoiding drift into 'group-think' in important decision making. Accordingly, in 2009, we developed our company culture charter and one of the key behaviours identified was the need for independent thinking and rigorous, respectful critique as part of our decision making processes.

To retain good people, we will need to ensure that we continue to allow for a variety of career paths and speeds for our employees. The basis for this is to encourage our employees to see how their long term plans could fit with a career at the Guardians. Making role models more visible and accessible, mentoring schemes and networking groups are all positive and 'do-able' initiatives we will make available to facilitate long-term career thinking and ultimately talent retention at the Guardians.

As part of regular reporting requirements, the Guardians' monitor and report on the profile of their workforce. As at 30 June 2010, the workplace profile for the Guardians is detailed as follows:

Headcount (FTE)	**64**	
Full-time (FTE)	59	
Part-time (FTE)	5	
Gender		
Women	20	27%
Men	44	73%
Senior Management*		
Women	11	37%
Men	19	63%
Age		
Under 20	0	0%
20 – 29	3	5%
30 - 39	33	51%
40 – 49	23	36%
50 – 59	5	8%
Over 60	0	0%
Undeclared	0	0%

1. Organisational restructure

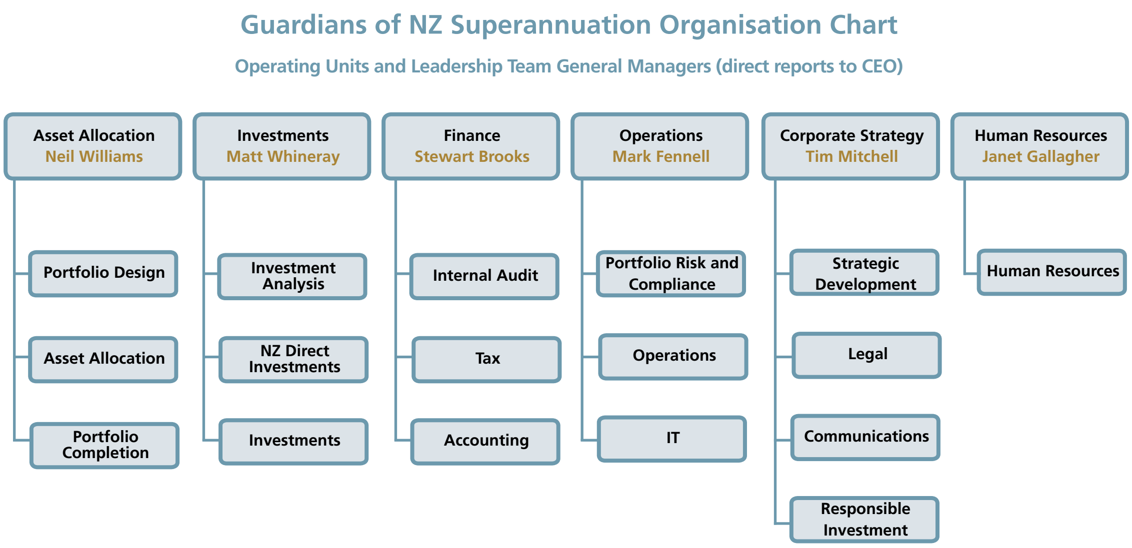
During the year we restructured our investment functions to better allocate responsibility for asset allocation and investment. Whereas previously we had three teams; Portfolio Research, Private Markets and Public Markets we now have two – Asset Allocation and Investments.

The Asset Allocation team is responsible for assessing the risk profile of the Fund and deciding how it should be accessed; passively or via active management. The Investments team identifies and assesses the best possible investment opportunities within the parameters set by the Asset Allocation team.

* Senior management includes General Managers, Heads of Departments and Senior Investment Analysts.

Our great team (continued)

The new structure is as per the below chart.



2. Talent Management

The challenge for our organisation, like many others, is the competition for talent – in particular since the GFC. We seek employees with high intelligence and high emotional intelligence, as do many other employers, many of whom can offer benefits that we cannot.

Having a team built on such people is a competitive advantage. They enable our growth. Accordingly talent management is a key objective for our 2010-15 Strategic Plan – as set out in our 2010 Statement of Intent. We believe the design and successful implementation of the plan will contribute significantly to our other strategic objectives, such as:

(a) building a high performance culture;

(b) developing a learning organisation;

(c) adding value to our employer of choice branding; and

(d) contributing to our team diversity management (as discussed above).

3. New discretionary bonus scheme

Fitting in with the restructure discussed at point 1, and consistent with one of our five key strategic objectives for the 2010/11 financial year, we also completed the design of a proposed new discretionary bonus programme. The proposed new programme, which applies from 1 July 2010, is designed to better reflect each employee's responsibilities while also giving them greater control over the outcome.

It also embeds clear commonality of performance objectives within teams and across teams so that each employee's objectives are directly relevant to their manager's objectives and that relevance continues all the way up to the Chief Executive. All objectives are also very clearly derived from our organisational Strategic Plan.

The proposed new scheme involves three pools; Investments (for the GMs of Asset Allocation and Investments and their teams), the Leadership Team (non-investment GMs) and Support (Operations, Finance, Corporate Strategy and Human Resources).

We will report on the outcome of the proposed new programme from the 2011 Annual Report onward.

4. Harassment and Bullying Prevention

We are committed to preventing harassment and bullying in the workplace. Zero tolerance policies have been developed in conjunction with clear guidelines for the management of harassment complaints. Other activities include regular feedback sessions reviewed by Human Resources and the availability of relevant policies and the employee Code of Conduct to all employees

5. Safe and Healthy Environment

The development of sound occupational health and safety policies and procedures is an integral part of our ongoing commitment to the health and well-being of our employees. Key activities in place include:

- A third-party audit of our Workplace Health and Safety Management;
- An Employee Wellness Programme involving outside speakers on health and fitness, stress management and other topics;
- Staff participation on the Health and Safety Committee;
- First aid, civil defence, building warden training;
- Fire evacuation training;
- The annual review of health and safety practices as per our independent health and safety audit;
- Ergonomic assessments included in employee induction programmes; and
- Fresh fruit made available to all employees as healthy snack alternative.

Overview of Financial Statements

Headline Results

- A $2.0 billion increase in the Fund's net asset position compared to the prior year
- A net return of 15.45% on the Fund's assets
- A 12.6 basis point or NZ$10.6 million decrease in overall expenses[2]

FUND SIZE AT 30 JUNE 2010:		$15.63 billion[1]
Returns	**Year to 30 June**	**Since inception**
New Zealand Superannuation Fund	15.5%	5.5%
90-Day Treasury Bills	2.6%	6.0%
Passive 'Reference' Portfolio	14.6%	5.8%

Fund Revenue

The 2009/10 financial year saw a welcome recovery from the previous year, dominated by the GFC.

The increase in returns primarily reflects the broad-based recovery in global and domestic asset prices, especially those priced in liquid publicly traded markets. These include listed equity, fixed interest, property, and commodities. It also includes fair value accounting for the Fund's life settlements and catastrophe bond holdings, as well as for the Fund's private market holdings.

The Fund accounts also reflect its increased revenue from rising use of derivatives to gain investment exposure. The choice of derivative exposure rather than holding the actual physical securities comes down to our assessment of the most cost-effective means of accessing investments. The use of derivatives resulted in an increase in interest income over the year (as a proportion of total income), as we have managed large cash holdings for the Fund's collateral and liquidity management purposes.

Meanwhile, the Fund's timber holdings increased in fair value, reflecting higher timber prices. In addition, the Fund's domestic timber managers increased their harvesting and sales activity, in response to both stronger prices internationally and the increasing maturity of some of the Fund's major timber holdings.

We received less 'Use of Money Interest' income due to our reduced pre-payment of tax, resulting from the previous year's losses. We also ceased our securities lending operation.

Fund Expenses

The Guardians and Fund expenses are separate accounts. Both are funded from the Fund (with all returns net of all costs), although the Board of the Guardians costs are funded through annual appropriation from Parliament. Despite this, we include all costs in the expenses analysis graph presented below.

Our overall expenses decreased[2] over the year. This reduction reflects the refocus of our active management strategy by increased direct derivative exposure rather than through physical holdings, and the reduced use of external managers.

1. Excludes provisions for NZ tax

In terms of the other major drivers:

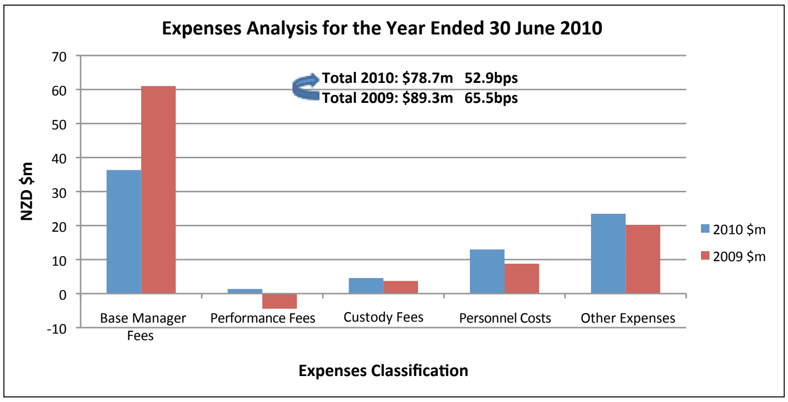
- Performance fees have increased due to the improved performance of our external managers, adding to a positive net return to the Fund's performance;
- Custody fees have increased in line with the size of the Fund; and
- Other expenses (which includes brokerage, depreciation, amortisation, trading, and audit and advisor costs) rose only marginally despite the increase in total Fund size and activity. These costs were constrained overall due to lower advisor costs, given the increase in internal capacity at the Guardians.

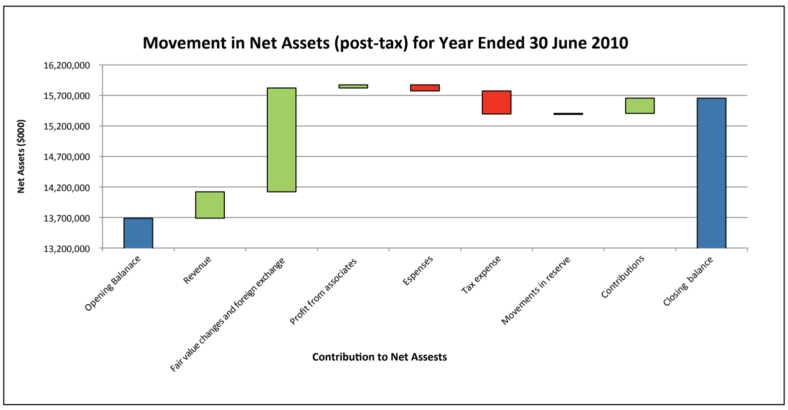
The Fund also incurred a tax expense of $378 million for the year. The tax bill was largely driven by the increase in fair value gains on our investments. A full discussion of the Fund's tax expenses is included in the Fund's financial statements.

Change in Net Assets under Management

The Fund's net asset position increased $2.0 billion over the financial year. This increase comprised primarily a $250 million Crown contribution, gains on our net investments, and tax accruals.

The figures below highlight both changes in our expense analysis (including those of the Board) and our net asset movements.





[2] To reconcile the expenses discussed in this section with the expenses disclosed in the accounts (at note 2), please note that the graph does not include timber expenses, losses on land revaluation and on the sale of land related to forestry holdings. While for accounting purposes they must be treated as an expense, economically they form part of the net return of the Fund.

Financial Statements

Contents

Statement of Responsibility

The Board and management of the Guardians of New Zealand Superannuation accept responsibility for the preparation of the annual financial statements of the New Zealand Superannuation Fund and Group and the judgements used in them.

The Board and management of the Guardians of New Zealand Superannuation accept responsibility for establishing and maintaining a system of internal control designed to provide reasonable assurance as to the integrity and reliability of financial and non-financial reporting of the New Zealand Superannuation Fund and Group.

In the opinion of the Board and management of the Guardians of New Zealand Superannuation, the annual financial statements for the year ended 30 June 2010 fairly reflect the financial position, operations, and cash flows of the New Zealand Superannuation Fund and Group.

DAVID MAY
Chairman
13 September 2010

ADRIAN ORR
Chief Executive Officer
13 September 2010

Statement of Comprehensive Income

For the year ended 30 June 2010

		GROUP ACTUAL		BUDGET
		2010	2009	2010
	Note	NZ$000	NZ$000	NZ$000
Interest income	2(a)	164,303	114,356	97,575
Dividend income		218,288	232,890	264,787
Timber sales	4	43,758	18,767	26,260
Fair value changes in investments at fair value through profit or loss	3	1,492,632	(4,261,761)	949,077
Net foreign exchange gain		196,768	669,107	-
Fair value changes in timber investments – forests	4	11,618	(33,204)	47,876
Share of profit of investments accounted for using the equity method	7(f)	51,510	144,200	89,488
Other income		6,603	18,365	7,635
NET OPERATING INCOME/(LOSS)		**2,185,480**	**(3,097,280)**	**1,482,698**
Operating expenses	2(b)	99,499	103,946	131,628
PROFIT/(LOSS) FOR THE YEAR BEFORE INCOME TAX EXPENSE		**2,085,981**	**(3,201,226)**	**1,351,070**
Income tax expense/(credit)	6	378,202	(408,140)	306,864
PROFIT/(LOSS) FOR THE YEAR AFTER INCOME TAX EXPENSE		**1,707,779**	**(2,793,086)**	**1,044,206**
Other comprehensive income				
Net fair value gains on available-for-sale financial assets		3,866	-	-
Gain/(loss) on revaluation of land		(282)	3,194	-
Translation of foreign operations		9,193	22,294	-
Income tax on items of other comprehensive income		(2,754)	1,584	-
OTHER COMPREHENSIVE INCOME FOR THE YEAR, NET OF TAX		**10,023**	**27,072**	**-**
TOTAL COMPREHENSIVE INCOME FOR THE YEAR		**1,717,802**	**(2,766,014)**	**1,044,206**

The attached notes form part of and should be read in conjunction with these financial statements.

Statement of Financial Position

As at 30 June 2010

	Note	GROUP ACTUAL 2010 NZ$000	GROUP ACTUAL 2009 NZ$000	BUDGET 2010 NZ$000
ASSETS				
Cash and cash equivalents	19	1,942,798	1,060,920	422,907
Trade and other receivables	8	584,352	536,580	71,792
Other assets	9	63	59	-
Investments				
Investments – derivative financial instrument assets	7	604,342	1,073,820	51,816
Investments – other financial assets	7	12,465,339	10,213,968	12,759,148
Investments accounted for using the equity method	7	856,585	837,648	871,857
Timber investments – forests	7	147,016	138,988	415,622
Total investments		**14,073,282**	**12,264,424**	**14,098,443**
Taxation receivable		69,277	-	-
Deferred tax asset	6	-	371,490	613,276
Property, plant, and equipment	10	47,929	50,517	48,621
Intangible assets	11	702	255	-
TOTAL ASSETS		**16,718,403**	**14,284,245**	**15,255,039**
LIABILITIES				
Trade and other payables	12	492,617	411,036	646,805
Investments – derivative financial instrument liabilities	7	530,048	149,923	-
Taxation payable		-	33,434	21,894
Provisions	13	3,306	1,943	17,090
Deferred tax liability	6	36,721	-	-
TOTAL LIABILITIES		**1,062,692**	**596,336**	**685,789**
NET ASSETS		**15,655,711**	**13,687,909**	**14,569,250**
PUBLIC EQUITY				
Retained surplus/(deficit)		761,895	(945,884)	(396,659)
Foreign currency translation reserve		-	(6,435)	59,760
Available-for-sale reserve		3,866	-	-
Land revaluation reserve		7,871	8,149	24,070
Contributed capital	15	14,882,079	14,632,079	14,882,079
TOTAL PUBLIC EQUITY		**15,655,711**	**13,687,909**	**14,569,250**

The attached notes form part of and should be read in conjunction with these financial statements.

Statement of Changes in Public Equity

For the year ended 30 June 2010

	Notes	FOREIGN CURRENCY TRANSLATION RESERVE NZ$000	LAND REVALUATION RESERVE NZ$000	AVAILABLE-FOR-SALE RESERVE NZ$000	CONTRIBUTED CAPITAL NZ$000	RETAINED SURPLUS/ DEFICIT NZ$000	TOTAL NZ$000
Balance at 1 July 2008		**(21,097)**	**24,071**	**-**	**12,390,079**	**1,818,870**	**14,211,923**
Loss for the year						(2,793,086)	(2,793,086)
Other comprehensive income		22,294	(25,138)	-		28,332	25,488
Income tax on items of other comprehensive income		(7,632)	9,216	-		-	1,584
Total comprehensive income for the year		14,662	(15,922)	-	-	(2,764,754)	(2,766,014)
Fund capital contributions from the Crown					2,242,000		2,242,000
Capital contributions from the Crown in respect of funding the net cost of New Zealand superannuation entitlements	15				7,744,149		7,744,149
Capital withdrawals by the Crown in respect of funding the net cost of New Zealand superannuation entitlements	15				(7,744,149)		(7,744,149)
Balance at 30 June 2009		**(6,435)**	**8,149**	**-**	**14,632,079**	**(945,884)**	**13,687,909**
Profit for the year						1,707,779	1,707,779
Other comprehensive income		9,193	(282)	3,866			12,777
Income tax on items of other comprehensive income		(2,758)	4	-			(2,754)
Total comprehensive income for the year		6,435	(278)	3,866	-	1,707,779	1,717,802
Fund capital contributions from the Crown					250,000		250,000
Capital contributions from the Crown in respect of funding the net cost of New Zealand superannuation entitlements	15				8,289,830		8,289,830
Capital withdrawals by the Crown in respect of funding the net cost of New Zealand superannuation entitlements	15				(8,289,830)		(8,289,830)
Balance at 30 June 2010		**-**	**7,871**	**3,866**	**14,882,079**	**761,895**	**15,655,711**

The attached notes form part of and should be read in conjunction with these financial statements.

Statement of Cash Flows

For the year ended 30 June 2010

	Note	GROUP ACTUAL 2010 NZ$000	GROUP ACTUAL 2009 NZ$000	BUDGET 2010 NZ$000
CASH FLOWS FROM OPERATING ACTIVITIES				
Cash was provided from:				
Proceeds from sale of investments		19,109,963	15,388,512	12,879,063
Proceeds from sale of timber investments – forest		3,670	120,955	-
Proceeds from sale of associates		32,573	-	-
Dividends received		210,837	229,301	264,787
Interest received		137,496	138,743	97,575
Receipts from customers		41,847	21,124	33,895
Miscellaneous income		1,696	5,138	-
Income taxation received		-	162,494	-
Total cash inflow from operating activities		**19,538,082**	**16,066,267**	**13,275,320**
Cash was applied to:				
Purchases of investments		(18,700,288)	(17,290,235)	(13,499,583)
Purchases of timber investments – forest		(447)	-	-
Purchases of associates		-	(182,503)	-
Managers' fees		(40,704)	(61,770)	(72,028)
Payments to suppliers		(52,255)	(66,859)	(56,881)
Income taxation paid		(65,415)	-	-
Goods and Services Tax		(1,444)	(65)	-
Total cash outflow from operating activities		**(18,860,553)**	**(17,601,432)**	**(13,628,492)**
NET CASH PROVIDED BY/(USED IN) OPERATING ACTIVITIES	19(e)	**677,529**	**(1,535,165)**	**(353,172)**
CASH FLOWS FROM INVESTING ACTIVITIES				
Cash was provided from:				
Proceeds from sale of property, plant, and equipment		1	58,165	-
Total cash inflow from investing activities		**1**	**58,165**	**-**
Cash was applied to:				
Purchases of property, plant, and equipment		(488)	(1,308)	-
Purchases of intangible asset		(941)	(224)	-
Total cash outflow from investing activities		**(1,429)**	**(1,532)**	**-**
NET CASH PROVIDED BY/(USED IN) INVESTING ACTIVITIES		**(1,428)**	**56,633**	**-**
CASH FLOWS FROM FINANCING ACTIVITIES				
Cash was provided from:				
Capital contributions from the Crown		250,000	2,242,000	250,000
NET CASH PROVIDED BY/(USED IN) FINANCING ACTIVITIES		**250,000**	**2,242,000**	**250,000**
Net increase/(decrease) in cash and cash equivalents		**926,101**	**763,468**	**(103,172)**
Cash and cash equivalents at the beginning of the financial year		1,060,920	324,103	526,079
Effects of exchange rate changes on the balance of cash held in foreign currencies		(44,223)	(26,651)	-
CASH AND CASH EQUIVALENTS AT THE END OF THE FINANCIAL YEAR	19(a)	**1,942,798**	**1,060,920**	**422,907**

The attached notes form part of and should be read in conjunction with these financial statements.

Notes to the Financial Statements

For the year ended 30 June 2010

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

GENERAL INFORMATION

These are the financial statements of the New Zealand Superannuation Fund (Fund) and its subsidiaries (Group), a fund created under Section 37 of the New Zealand Superannuation and Retirement Income Act 2001 (Act). This Act commenced on 11 October 2001.

The consolidated financial statements comprise the Fund and its subsidiaries.

The Fund is managed and administered by the Guardians of New Zealand Superannuation (Guardians). The Guardians were established as a Crown entity by Section 48 of the Act and became operative from 30 August 2002.

Under section 43 of the Act, the Crown is required to make capital contributions to the Fund for investment based on a percentage of GDP as set out in the Act. Capital contributions are made by the Crown into the Fund on a fortnightly basis for the purpose of investment, and funding the net cost of New Zealand superannuation entitlements. Under section 44 of the Act, the Crown is entitled to contribute lesser amounts than calculated using the formula under section 43 of the Act.

The Fund is domiciled in New Zealand and the address of its principal place of business is set out in the Corporate Directory on page 142.

STATEMENT OF COMPLIANCE

The Fund is a profit-oriented entity. The financial statements have been prepared in accordance with Generally Accepted Accounting Practice in New Zealand (NZ GAAP). They comply with the New Zealand Equivalents to International Financial Reporting Standards (NZ IFRS), as appropriate for profit-oriented entities. The financial statements also comply with International Financial Reporting Standards (IFRS).

The financial statements for the year ended 30 June 2010 were authorised for issue in accordance with a resolution of the Board of Guardians of New Zealand Superannuation on 13 September 2010.

BASIS OF PREPARATION

The financial statements have been prepared in accordance with the Act.

The financial statements have been prepared on a fair value basis, except for certain items as detailed in the policies below.

The financial statements are presented in New Zealand dollars and all values are rounded to the nearest thousand dollars (NZ$000).

Accounting policies are selected and applied in a manner which ensures that the resulting financial information satisfies the concepts of relevance and reliability, thereby ensuring that the substance of the underlying transactions or other events is reported.

The budget was approved by the Board of Guardians of New Zealand Superannuation for the year. The budget figures are unaudited.

Notes to the Financial Statements (continued)

For the year ended 30 June 2010

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Standards and interpretations that have recently been issued or amended but are not yet effective have not been adopted for the annual reporting period ended 30 June 2010. The standards and interpretations applicable to the Fund are outlined in the table below.

REFERENCE	TITLE	SUMMARY	APPLICATION DATE OF STANDARD*	IMPACT ON FINANCIAL STATEMENTS	APPLICATION DATE FOR GROUP*
NZ IAS 24	Related Party Disclosures (Revised 2009)	The amendments simplify the definition of a related party and provide a partial exemption from the disclosure requirements for government-related entities.	1 January 2011	The amendments will have an impact on the Group's related party disclosures. It is expected that the number of disclosures will reduce on adoption of the revised standard.	1 July 2011
NZ IFRS 9	Financial Instruments	This standard is part of the IASB's project to replace IAS 39 Financial Instruments: Recognition and Measurement. The standard applies to financial assets, their classification and measurement. All financial assets are required to be classified on the basis of the entity's business model for managing the financial assets and the contractual cash flow characteristics of the financial asset. Financial assets are initially measured at fair value plus, in the case of a financial asset not at fair value through profit or loss, particular transaction costs and subsequently measured at amortised cost or fair value.	1 January 2013	NZ IFRS 9 will affect the classification and measurement of the Group's financial assets.	1 July 2013

* Designates the beginning of the applicable annual reporting period.

All accounting policies have been consistently applied by the Group with those of the previous financial year except as follows:

The Group has adopted the following amendments as of 1 July 2009:

IAS 1 (Revised 2007) Presentation of Financial Statements

The International Accounting Standards Board (IASB) issued a revised version of IAS 1 Presentation of Financial Statements (IAS 1R), which is effective for periods beginning on or after 1 January 2009. The revised standard is intended to improve the users' ability to analyse and compare the information given in the consolidated financial statements. The Board have determined that this does not have any material financial impact on the consolidated financial statements of the Group. However, adoption of IAS 1R impacts the presentation of the consolidated financial statements of the Group. As permitted under IAS 1R, the Board have chosen to present one single statement of comprehensive income.

Amendments to IFRS 7 Financial Instruments: Disclosures about Financial Instruments

The IASB issued amendments to IFRS 7 Financial Instruments: Disclosures (IFRS 7) in March 2009, which are effective for periods beginning on or after 1 July 2009. The Board have determined the amendments will not have any material financial impact on the consolidated financial statements of the Group. However, the adoption of the amendments to IFRS 7 does impact the presentation of the consolidated financial statements of the Group. The amendment to IFRS 7 requires fair value measurements to be disclosed by the source of inputs, using a three-level hierarchy:

1) Quoted prices (unadjusted) in active markets for identical assets or liabilities (Level 1)
2) Inputs other than quoted prices included in Level 1 that are observable for the asset or liability, either directly (as prices) or indirectly (derived from prices) (Level 2)
3) Inputs for the asset or liability that are not based on observable market data (unobservable inputs) (Level 3)

Notes to the Financial Statements (continued)

For the year ended 30 June 2010

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

In addition, the amendment revises the specified minimum liquidity risk disclosures including the contractual maturity of non derivative financial liabilities, and a description of how this is managed.

In the first year of application, comparative information is not required and has not been presented.

The following particular accounting policies which materially affect the measurement of comprehensive income and financial position have been applied:

(a) Capital contributions

(i) Fund capital contributions

The Crown is required to make capital contributions to the Fund in accordance with Sections 42 to 44 inclusive of the Act. Capital contributions are made by the Crown to the Fund for investment and for the purpose of contribution to the net cost of paying superannuation entitlements after 2020. These capital contributions are recorded in the statement of changes in public equity.

(ii) Superannuation entitlement payments

The Minister of Finance, under Section 45 of the Act, must ensure that sufficient money is transferred to the Fund in each year to meet the net cost of superannuation entitlements. These transfers are treated as capital contributions from the Crown in respect of funding the net cost of superannuation entitlements and are offset by capital withdrawals and recorded in the statement of changes in public equity.

(b) Capital withdrawals

(i) Fund capital withdrawals

In terms of Section 47 of the Act no withdrawals of Fund capital contributions are permitted prior to 30 June 2020.

(ii) Superannuation entitlement payments

The net cost of superannuation entitlements is treated as capital withdrawals by the Crown in respect of funding the net cost of superannuation entitlements and is recorded in the statement of changes in public equity. These amounts equate to the associated capital contributions.

The payment of superannuation entitlements is an expense of the Crown and is recorded separately in the Crown's financial statements.

(c) Income tax

In accordance with Section 76 of the Act the Group is treated as if it is a body corporate for tax purposes and is therefore subject to income tax on any income derived from investments, and that income is treated as income of the Group under the Income Tax Act 2007.

The income tax expense recognised for the year is based on the accounting surplus, adjusted for permanent differences between accounting and tax rules together with the movement in deferred tax for the year.

Current tax is calculated by reference to the amount of taxes payable or recoverable in respect of the taxable profit or tax loss for the year. It is calculated using tax rates and tax laws that have been enacted or substantively enacted at balance date. Current tax for current and prior periods is recognised as a liability (or asset) to the extent that it is unpaid (or refundable).

Deferred income tax is provided on all temporary differences at balance date between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes.

Deferred income tax liabilities are recognised for all taxable temporary differences:

(i) except for a deferred income tax liability arising from the initial recognition of goodwill;

(ii) except where the deferred income tax liability arises from the initial recognition of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss; and

(iii) in respect of taxable temporary differences associated with investments in subsidiaries, associates, and interests in joint ventures, except where the timing of the reversal of the temporary differences can be controlled and it is probable that the temporary differences will not reverse in the foreseeable future.

Notes to the Financial Statements (continued)

For the year ended 30 June 2010

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

(c) Income tax (continued)

Deferred income tax assets are recognised for all deductible temporary differences, carry-forward of unused tax assets, and unused tax losses, to the extent that it is probable that taxable profit will be available against which the deductible temporary differences, and the carry-forward of unused tax assets, and unused tax losses can be utilised:

(i) except where the deferred income tax asset relating to the deductible temporary difference arises from the initial recognition of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss; and

(ii) in respect of deductible temporary differences associated with investments in subsidiaries, associates, and interests in joint ventures, except that deferred tax assets are only recognised to the extent that it is probable that the temporary differences will reverse in the foreseeable future and taxable profit will be available against which the temporary differences can be utilised.

The carrying amount of deferred income tax assets is reviewed at each balance sheet date and reduced to the extent that it is no longer probable that sufficient taxable profit will be available to allow all or part of the deferred income tax asset to be utilised.

Deferred income tax assets and liabilities are measured at the tax rates that are expected to apply to the year when the asset is realised or the liability is settled, based on tax rates (and tax laws) that have been enacted or substantively enacted at balance date. The measurement of deferred tax liabilities and assets reflects the tax consequences that would follow from the manner in which the Group expects, at the reporting date, to recover or settle the carrying amount of its assets and liabilities.

Deferred tax assets and liabilities are offset when they relate to income taxes levied by the same taxation authority and the Group intends to settle its current tax assets and liabilities on a net basis.

Income tax relating to items of other comprehensive income are recognised in the statement of comprehensive income.

(d) Financial instruments

The Group is party to financial instruments as part of its normal operations. These financial instruments include cash and cash equivalents, derivatives, investments, receivables, and payables. All financial instruments are recognised in the statement of financial position and all revenues and expenses in relation to financial instruments are recognised in the statement of comprehensive income.

Financial assets and financial liabilities are recognised in the statement of financial position when the Group becomes a party to the contractual provisions of the instrument. Purchases or sales of financial instruments that require delivery within the time frame generally established by regulation or convention in the marketplace are recognised on the trade date, i.e., the date that the Group commits to purchase or sell the instrument. Derivatives are recognised on a trade date basis. The Group offsets financial assets and financial liabilities when the Group has a legally enforceable right to set off the recognised amounts and interests and intends to settle on a net basis.

(e) Investments

Investments are represented by the following:	**KEY**
- Financial instruments at fair value through profit or loss (either designated at fair value through profit or loss or held for trading):	
- Equities	i)
- Fixed interest securities	ii)
- Derivatives	iii)
- Collective investment funds	iv)
- Certain private equity investments	v)
- Unlisted unit trusts	vi)
- Insurance-linked investments	vii)
- Available-for-sale financial instruments: certain private equity investments	viii)
- Loans and receivables: unlisted debt instruments	ix)
- Investments accounted for using the equity method (refer accounting policies (h) and (i))	
- Timber investments – forests (refer accounting policy (j))	

Notes to the Financial Statements (continued)

For the year ended 30 June 2010

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

(e) Investments (continued)

Financial instruments at fair value through profit or loss

Initial recording

Financial instrument investments at fair value through profit or loss are initially recognised at fair value on a trade date basis. Transaction costs, for example trading commission, are expensed immediately in the statement of comprehensive income.

Subsequent measurement

Subsequent to initial recognition, these investments are recorded at fair value and are classified into the category "at fair value through profit or loss". The Guardians manage and evaluate the performance of these investments on a fair value basis in accordance with the Fund's investment strategy and information about the investments is provided internally on this basis to the Guardians' key management personnel. Changes in fair value are recognised in profit or loss in the statement of comprehensive income.

Interest earned is accrued in income according to the terms of the contract, while dividend income is recorded when the right to payment has been established.

Determination of fair value

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

i) Listed equities are valued at the last quoted bid price on the relevant exchange as of the close of business at balance date.

ii) Highly liquid fixed interest securities are valued at the last quoted bid price by a reputable pricing vendor or broker as of the close of business at balance date. Where the market for fixed interest securities is illiquid, prices are determined by a reputable pricing vendor who uses models to value these securities. The models can utilise a variety of inputs including loan level data, prepayment and default assumptions and benchmark prices for similar securities. Because of the inherent uncertainty of valuation, it is possible that those values estimated for the illiquid securities may differ from those values that would have been used had a ready market for those securities existed and those differences may be significant.

iii) Fair value for derivatives is outlined under "Derivatives" below.

iv) Investments in collective investment funds (unlisted investment funds) are valued at the last price of the unit or security as provided by the administrators at balance date. The price is based on the fair value of the underlying net assets or securities of the relevant collective investment fund.

v) Certain private equity investments (unlisted investment funds and unlisted equity investments), which are designated at fair value through profit or loss, are valued at the last price of the unit or security as provided by the investment managers or administrators at balance date. The price is based on the fair value of underlying net assets of the private equity investment. Fair value is determined using a variety of methods, including independent valuations, valuation models based on the price of recent investments, earnings multiples, or discounted cash flows. Certain private equity investments are classified as available for sale. The accounting policy for these investments is outlined under viii).

vi) Investments in unlisted unit trusts are valued at the last bid price of the unit or security as provided by the administrators at balance date. The price is based on the fair value of the underlying net assets or securities of the relevant unlisted unit trust.

vii) Insurance-linked investments which are catastrophe bonds are valued using prices provided by reputable pricing vendors or brokers.

Available-for-sale financial instruments

viii) Certain private equity investments that do not have a quoted market price in an active market and whose fair value cannot be reliably measured using the valuation methods outlined in v) above are classified as available-for-sale and are measured at cost less impairment. Transaction costs are included in the cost of the investment. Management has determined that fair value for these investments cannot be reliably measured where the entity's financial statements have not been prepared under either IFRS or a recognised and reliable accounting basis such as US GAAP. Subsequently, where the fair value of these investments becomes able to be reliably measured, then the investment will be measured at fair value with gains or losses being recognised in other comprehensive income (reserves) until the investment is derecognised or until the investment is determined to be impaired, at which time the cumulative gain or loss previously reported in reserves is reclassified to profit or loss.

Notes to the Financial Statements (continued)

For the year ended 30 June 2010

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

(e) Investments (continued)

Loans and receivables

ix) Unlisted debt instruments including fixed and floating rate notes and redeemable preference shares are non-derivative financial assets with fixed or determinable payments that are not quoted on an active market. Such assets are carried at amortised cost using the effective interest rate method. Gains and losses are recognised in profit or loss when the loans and receivables are derecognised or impaired.

Derivatives

The Group enters into a variety of derivative financial instruments to manage its exposure to foreign currency risk, and achieve exposure to assets and asset classes. The use of derivatives is governed by the Fund's Statement of Investment Policies, Standards and Procedures as approved by the Guardians, which provides written principles on the use of derivatives by the Group.

The fair value of forward foreign exchange contracts is calculated by reference to current forward exchange rates for contracts with similar maturity profiles.

The fair value of cross currency swaps is determined using a discounted cash flow model.

The fair value of asset swaps is determined using a model, with the key inputs being interest rates and the pricing of inflation futures.

The fair value of credit default swaps is determined using a discounted cash flow model which incorporates default rate and credit spread assumptions for the reference entity or index.

The fair value of futures contracts is calculated as being the present value of the difference between the contract price and the closing price reported on the primary exchange of the futures contract.

The fair value of index swaps (commodity, equity, real estate and longevity contingent swaps) is provided by the counterparty and is calculated by reference to the movement in the underlying index or basket of securities or other contracts. Index swaps are settled net in cash.

The fair value of insurance-linked swaps is calculated using a model which incorporates the premium paid or received and a price provided by reputable pricing vendors or brokers. Premiums are recognised based on a risk dissipation schedule, derived from third party catastrophe models.

The fair value of exchange-traded insurance-linked options is the closing price as reported by the primary exchange of the contract.

The fair value of options are calculated using a Black-Scholes option valuation model.

(f) Securities lending

Securities lending transactions are collateralised by securities or cash. The transfer of the securities to counterparties is only reflected on the statement of financial position if the risks and rewards of ownership are also transferred. Collateral advanced by the borrower in the form of readily marketable securities (non-cash) is held in escrow by a third-party agent. Recourse to those securities is only available in the event of default by the borrower, and as such the non-cash collateral is not recognised in the statement of financial position. Collateral advanced by the borrower in the form of cash is recognised in the statement of financial position as an asset, along with a corresponding liability to repay the cash collateral to the borrower, once the securities have been returned.

(g) Consolidation of subsidiaries

Subsidiaries are those entities that are controlled by the Fund.

The Group's financial statements incorporate the financial statements of the Fund and its subsidiaries, which have been consolidated. The results of any subsidiaries that become or cease to be part of the Group during the year are consolidated from the date that control commenced or until the date that control ceased.

All inter-entity transactions, balances, and unrealised profits are eliminated on consolidation.

The acquisition of subsidiaries is accounted for using the acquisition method of accounting. The acquisition method of accounting involves recognising at acquisition date, separately from goodwill, the identifiable assets acquired, the liabilities assumed and any non-controlling interest in the acquiree. The identifiable assets acquired and the liabilities assumed are measured at their acquisition date fair values.

The difference between the above items and the fair value of the consideration (including the fair value of any pre-existing investment in the acquiree) is goodwill or a discount on acquisition.

Notes to the Financial Statements (continued)

For the year ended 30 June 2010

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

(h) Investments in associates

An associate is an entity over which the Fund is in a position to exercise significant influence, but not control or joint control, through participation in the financial and operating policy decisions of the entity.

At inception, certain of the Fund's associates are designated at fair value through profit or loss under NZ IAS 39 Financial Instruments: Recognition and Measurement (in accordance with paragraph 1 of NZ IAS 28 Investments in Associates). All other associates are equity accounted in accordance with NZ IAS 28 Investments in Associates. The designation is made with reference to how the Guardians intend to manage the investment and the extent to which the Guardians will be involved in the management of the investment.

The results of associates which are accounted for under NZ IAS 28 Investments in Associates are incorporated in the financial statements using the equity method of accounting, except where the investment is classified as held for sale, in which case it is accounted for in accordance with NZ IFRS 5 Non-current Assets Held for Sale and Discontinued Operations. Under the equity method, investments in associates are carried at cost as adjusted for post-acquisition changes in the Fund's share of the net assets of the associate, less any impairment in the value of individual investments. Losses of an associate in excess of the Fund's interest in that associate are not recognised, unless the Fund has incurred legal or constructive obligations or made payments on behalf of the associate.

(i) Investments in joint ventures

A joint venture is a contractual arrangement whereby the Guardians and other parties undertake an economic activity that is subject to joint control, which is when the strategic financial and operating policy decisions relating to the activities of the joint venture require the unanimous consent of the parties sharing control.

At inception, certain of the Fund's joint ventures are designated at fair value through profit or loss under NZ IAS 39 Financial Instruments: Recognition and Measurement (in accordance with paragraph 1 of NZ IAS 31 Interests in Joint Ventures). All other joint ventures are equity accounted in accordance with NZ IAS 31 Interests in Joint Ventures. The designation is made with reference to how the Guardians intend to manage the investment and the extent to which the Guardians will be involved in the management of the investment.

The results of joint ventures which are accounted for under NZ IAS 31 Interests in Joint Ventures are incorporated in the financial statements using the equity method of accounting, except where the investment is classified as held for sale, in which case it is accounted for in accordance with NZ IFRS 5 Non-current Assets Held for Sale and Discontinued Operations. Under the equity method, investments in joint ventures are carried at cost as adjusted for post-acquisition changes in the Fund's share of the net assets of the joint venture, less any impairment in the value of individual investments. Losses of a joint venture in excess of the Fund's interest in that joint venture are not recognised, unless the Fund has incurred legal or constructive obligations or made payments on behalf of the joint venture.

(j) Timber investments – forests

Forest assets are predominantly standing trees. These are recognised in the statement of financial position at fair value less estimated point of sale costs. The costs to establish and maintain the forest assets are included in the statement of comprehensive income together with the change in fair value for each accounting period.

The valuation of forest assets is based on discounted cash-flow models. The annual harvest from forecast tree growth is multiplied by expected wood prices and the costs associated with forest management, harvesting, and distribution are then deducted to derive annual cash flows.

The fair value of the forest assets are measured as the present value of cash flows from one growth cycle based on productive forest land, taking into consideration environmental, operational, and market restrictions. Forests are valued separately from the underlying freehold land. Further details on the valuation basis is set out in note 7(g).

(k) Receivables

Short-term receivables are initially recorded at fair value, then subsequently at amortised cost using the effective interest rate less any impairment.

Notes to the Financial Statements (continued)

For the year ended 30 June 2010

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

(l) Property, plant, and equipment

Initial recording

All items of property, plant, and equipment are initially recognised at cost. Cost includes the value of consideration exchanged, or fair value in the case of donated or subsidised assets, and those costs directly attributable to bringing the item to working condition for its intended use.

Subsequent measurement

Subsequent to initial recognition, leasehold improvements, plant, and equipment are stated at cost less accumulated depreciation and any impairment in value.

Land is measured at fair value. Fair value is determined on the basis of an independent valuation prepared by external valuation experts, based on discounted cash flows or capitalisation of net income (as appropriate).

Any revaluation increase arising on the revaluation of land is credited to the asset revaluation reserve, except to the extent that it reverses a revaluation decrease for the same asset previously recognised as an expense in profit or loss, in which case the increase is credited to the statement of comprehensive income to the extent of the decrease previously charged.

A decrease in carrying amount arising on the revaluation of land is charged as an expense in profit or loss to the extent that it exceeds the balance, if any, held in the asset revaluation reserve relating to a previous revaluation of that asset.

Independent valuations of land are performed with sufficient regularity (at least every three years) to ensure that the carrying amount does not differ materially from the asset's fair value at balance date.

Disposal

An item of property, plant, and equipment is derecognised upon disposal or when no future economic benefits are expected to arise from the continued use of the asset.

Upon disposal, any revaluation reserve relating to the particular asset being sold is transferred to retained earnings.

Any gain or loss arising on derecognition of the asset (calculated as the difference between the net disposal proceeds and the carrying amount of an item) is included in profit or loss in the year the item is derecognised.

Impairment

All items of property, plant, and equipment are assessed for indicators of impairment at each balance date.

Where the carrying amount is assessed to be greater than its recoverable amount, the item is written down to its recoverable amount. The write down is recognised in the statement of comprehensive income unless it relates to land in which case it is treated as a revaluation decrease.

Where an impairment loss subsequently reverses, the carrying amount of the item is increased to the revised estimate of its recoverable amount, but only to the extent that the increased carrying amount does not exceed the carrying amount that would have been determined had no impairment loss been recognised for the item in prior years. A reversal of an impairment loss is recognised in the statement of comprehensive income immediately unless it relates to land, in which case it is treated as a revaluation increase.

Recoverable amount is the greater of fair value less costs to sell and value in use. It is determined for an individual asset, unless the asset's value in use cannot be estimated to be close to its fair value less costs to sell and it does not generate cash inflows that are largely independent of those from other assets or groups of assets, in which case, the recoverable amount is determined for the cash generating unit to which the asset belongs.

In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset.

Notes to the Financial Statements (continued)

For the year ended 30 June 2010

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

(m) Depreciation

Depreciation is provided on a straight line basis at a rate which will write off the cost of the assets to their estimated residual value over their useful lives.

The useful lives and associated depreciation rates of major classes of assets have been estimated as follows:

Land improvements	15-50 years
Office equipment	3 years
Computer equipment	3 years
Office fitout	2-6 years

The cost of office fitout is capitalised and depreciated over the unexpired period of the lease (held by the Guardians) or the estimated remaining useful lives of the improvements, whichever is shorter.

(n) Intangible assets

Software and licences are finite life intangibles and are recorded at cost less accumulated amortisation and impairment. Amortisation is charged on a straight line basis over their estimated useful lives of 3 years. The estimated useful life and amortisation method is reviewed at the end of each annual reporting period.

(o) Payables

Short-term payables are not interest bearing. They are initially recognised at fair value and subsequently at amortised cost.

(p) Provisions

Provisions are recognised when the Group has a present obligation as a result of a past event, the future sacrifice of economic benefits is probable, and the amount of the provision can be measured reliably.

The amount recognised as a provision is the best estimate of the consideration required to settle the present obligation at reporting date, taking into account the risks and uncertainties surrounding the obligation. Where a provision is measured using the cash flows estimated to settle the present obligation, its carrying amount is the present value of those cash flows.

When some or all of the economic benefits required to settle a provision are expected to be recovered from a third party, the receivable is recognised as an asset if it is virtually certain that recovery will be received and the amount of the receivable can be measured reliably.

(q) Income recognition

Revenue is recognised to the extent that it is probable that the economic benefits will flow to the Group and the revenue can be reliably measured. The following specific recognition criteria must also be met before revenue is recognised:

For financial instruments measured at fair value, interest income is recognised on an accruals basis, either daily or on a yield to maturity basis. Interest earned on cash balances is accrued at the effective interest rate.

Dividend income is recognised when the shareholder's rights to receive payment has been established, normally the ex-dividend date. Where the Group has elected to receive dividends in the form of additional shares rather than cash, the amount of the cash dividend foregone is recognised as income. Any excess in the value of shares received over the amount of cash dividend foregone is recognised as a gain in the statement of comprehensive income.

Revenue from the sale of goods is recognised when the Group has transferred to the buyer the significant risks and rewards of ownership of the goods.

Securities lending fees are recognised as earned.

(r) Foreign currency transactions

Transactions denominated in a foreign currency are converted to New Zealand dollars at the exchange rate in effect at the date of the transaction.

Monetary assets and liabilities denominated in foreign currency at balance date are translated at the rate of exchange ruling as at that date. The resulting exchange differences are recognised separately in the statement of comprehensive income.

Notes to the Financial Statements (continued)

For the year ended 30 June 2010

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

(s) Translation of the financial statements of independent foreign operations

Assets and liabilities of foreign operations with functional currencies other than New Zealand dollars are translated at the closing rate. Revenue and expense items are translated at a weighted average of exchange rates over the year, as a surrogate for the spot rates at transaction dates. Exchange differences arising from the foregoing are taken to the foreign currency translation reserve and recognised in the statement of changes in public equity.

Goodwill and fair value adjustments arising on the acquisition of a foreign operation are treated as assets and liabilities of the foreign operation and translated at exchange rates prevailing at the reporting date.

On disposal of an independent foreign operation, the accumulated amount of the exchange differences taken to the foreign currency translation reserve that relate to the foreign operation is transferred out of the foreign currency translation reserve and recognised as income or expense in the statement of comprehensive income.

(t) Statement of cash flows

The following are the definitions of the terms used in the statement of cash flows:

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

Investing activities are those activities relating to the acquisition, holding, and disposal of property, plant and equipment and intangible assets.

Financing activities are those activities relating to capital contributions and to payments of superannuation entitlements (from 2020). As the current funding by the Crown of superannuation entitlements flows directly from the Treasury to the Ministry of Social Development it is not considered cash flow of the Group and is accordingly not recorded in the statement of cash flows.

Cash and cash equivalents

Cash and cash equivalents includes cash balances on hand, held in bank accounts, demand deposits, and other highly liquid investments with an original maturity of three months or less.

(u) Goods and Services Tax (GST)

Revenues, expenses, assets, and liabilities are recognised exclusive of GST, with the exception of receivables and payables which are stated with GST included. Where GST is irrecoverable as an input tax, then it is recognised as part of the related asset or expense.

Cash flows are included in the cash flow statement on a gross basis. The GST component of cash flows arising from investing and financing activities which is recoverable from, or payable to, the taxation authority is classified as operating cash flows.

(v) Changes in accounting policies

There have been no changes in accounting policies. The accounting policies have been applied consistently throughout these financial statements.

(w) Significant estimates and judgements

In preparing these financial statements, estimates and judgements have been made concerning the future. These estimates and judgements may differ from the subsequent actual results. Estimates and judgements are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances. The estimates and judgements that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities are detailed within the following accounting policies and notes:

- Note 1(e) Investments. In particular: fixed interest securities where the market is illiquid; private equity funds; unlisted unit trusts; derivatives.
- Note 1 (j) Timber investments – forests
- Note 1 (l) Property, plant, and equipment – valuation of land
- Note 7 Investments
- Note 10 Property, plant, and equipment
- Note 20 Financial instruments

Notes to the Financial Statements (continued)

For the year ended 30 June 2010

	GROUP ACTUAL 2010 NZ$000	GROUP ACTUAL 2009 NZ$000
2. PROFIT/(LOSS) FROM OPERATIONS		
(A) INTEREST INCOME		
New Zealand fixed interest – Crown	-	6,000
New Zealand fixed interest – State-Owned Entities	108	242
New Zealand fixed interest – Local Bodies	740	1,507
New Zealand fixed interest – Other	10,328	9,382
New Zealand fixed interest – Total	11,176	17,131
Global fixed interest	125,601	61,472
Other interest	27,526	35,753
Total interest income	**164,303**	**114,356**
(B) OPERATING EXPENSE		
Profit/(loss) before income tax has been arrived at after charging/(crediting):		
Timber harvesting and operating expenses (note 4)	19,758	7,649
Depreciation of property, plant, and equipment (note 10)	920	676
Loss on disposal of property, plant, and equipment	33	7,546
Loss on disposal of intangible asset	16	-
Loss on revaluation of property, plant, and equipment	1,561	-
Amortisation of intangible assets (note 11)	478	156
Managers' fees – base	36,322	61,015
Managers' fees – performance (note 13)	1,363	(4,446)
Custody fees	4,569	3,721
Auditors' remuneration (note 5)	283	279
Reimbursement of Guardians' expenses	15,973	11,635
Trade expenses	8,511	9,354
Other expenses	9,712	6,361
	99,499	**103,946**
3. FAIR VALUE CHANGES IN INVESTMENTS AT FAIR VALUE THROUGH PROFIT OR LOSS		
Financial assets or liabilities designated at fair value through profit or loss	1,591,322	(3,191,361)
Financial assets or liabilities held for trading recognised at fair value through profit or loss	(98,690)	(1,070,400)
	1,492,632	**(4,261,761)**
4. TIMBER OPERATIONS		
Timber sales	43,758	18,767
Harvesting and operating expenses	(19,758)	(7,649)
Depreciation – land improvements (note 10)	(531)	(380)
Net trading result	**23,469**	**10,738**
Fair value changes in timber investments – forests	9,842	(33,204)
Gain on disposal of timber investments – forests	1,776	-
Loss on disposal of property, plant, and equipment	-	(7,546)
Timber net surplus/(loss) (excluding managers' fees)	**35,087**	**(30,012)**

Notes to the Financial Statements (continued)

For the year ended 30 June 2010

	GROUP ACTUAL 2010 NZ$000	GROUP ACTUAL 2009 NZ$000
5. REMUNERATION OF AUDITORS		
Auditor of the parent entity		
Audit of the financial statements – Attest	269	265
Audit of Fund subsidiaries	2	2
Audit of Guardians subsidiaries	12	12
	283	**279**

The auditor of the Fund and its subsidiaries and the Guardians' subsidiaries is Brent Penrose of Ernst & Young, on behalf of the Auditor-General.

	GROUP ACTUAL 2010 NZ$000	GROUP ACTUAL 2009 NZ$000
6. INCOME TAXES		
Income tax expense		
Current tax – current year	6,869	6,133
Current tax – prior year	(34,249)	(2,569)
Deferred tax – current year	495,649	(413,476)
Deferred tax – prior year	(90,067)	1,772
Income tax expense/(credit)	**378,202**	**(408,140)**
Profit/(loss) for the year before income tax	2,085,981	(3,201,226)
Income tax calculated at 30%	625,794	(960,367)
Fair Dividend Regime	(112,090)	467,848
PIE Regime	(834)	81,045
Imputation credits	(10,422)	(9,926)
Reduction in tax rate to 28%	(7,017)	-
Foreign tax credits unable to be claimed	6,633	6,360
Prior period adjustment	(124,317)	(797)
Other items	455	7,697
Income tax expense/(credit)	**378,202**	**(408,140)**
Deferred tax assets are attributed to the following		
New Zealand income tax losses	63,667	459,777
Unrealised loss on non-portfolio grey list FIF's	4,560	-
Other	1,441	236
Set off against deferred tax liability	(69,668)	(88,523)
Balance at the end of the year	**-**	**371,490**
Movements		
Balance at the beginning of the year	371,490	-
Prior year adjustments	91,134	-
Other	124	30
(Credited)/charged to profit or loss	(481,603)	371,460
Set off against deferred tax asset	18,855	-
Balance at the end of the year	**-**	**371,490**

Notes to the Financial Statements (continued)

For the year ended 30 June 2010

	GROUP ACTUAL 2010 NZ$000	2009 NZ$000
6. INCOME TAXES (continued)		
Deferred tax liabilities are attributed to the following		
Timber investments – forest revaluation	(103,005)	(84,960)
Accrued Foreign Dividend Payments	-	(310)
Amounts recognised directly in equity	(2,309)	(2,313)
Other	(1,075)	(940)
Set off against deferred tax asset	69,668	88,523
Balance at the end of the year	**(36,721)**	**-**
Movements		
Balance at the beginning of the year	-	(41,828)
Prior year adjustments	(1,066)	(1,772)
Amount recognised directly in foreign currency translation reserve	(2,758)	(7,633)
Amount recognised directly in land revaluation reserve	4	9,217
Other	-	30
Set off against deferred tax asset	(18,855)	-
(Credited)/charged to profit or loss	(14,046)	41,986
Balance at the end of the year	**(36,721)**	**-**

With effect from 1 July 2011, the applicable statutory tax rate for the Group will change from 30% to 28%. Deferred tax has been provided at 30% for temporary differences which are expected to reverse prior to 1 July 2011 and has been provided at 28% for temporary differences expected to reverse after 30 June 2011 in accordance with NZ IAS 12 Income Taxes. This has reduced tax expense by $7,017,000 in the current income year.

A deferred tax asset of $63,667,000 has been recognised in relation to New Zealand income tax losses based on a history of making taxable profits and forecasted future taxable profits which will be able to be offset using these tax losses.

The prior period adjustment of $124,317,000 (including cash refunds of $34,249,000) relates primarily to the New Zealand tax classification of offshore investments in certain foreign investment funds for the 2007, 2008 and 2009 income years. In particular there were certain investments in which the Group held an interest exceeding 10% and used the fair dividend rate method to compute its foreign investment fund income. This treatment has been corrected in the current year and prior year tax returns have been amended where necessary.

Notes to the Financial Statements (continued)

For the year ended 30 June 2010

	GROUP ACTUAL 2010 NZ$000	GROUP ACTUAL 2009 NZ$000
7. INVESTMENTS		
(A) INVESTMENTS BY ASSET TYPE		
Financial assets		
Derivative financial instrument assets:		
Forward foreign exchange contracts	348,963	905,839
Cross currency swaps	101,619	12,223
Asset swaps	301	3,904
Real estate swaps	-	40,937
Longevity contingent swaps	108,913	85,366
Futures contracts	-	-
Equity swaps	39	25,551
Commodity swaps	2,084	-
Credit default swaps	35,368	-
Insurance-linked swaps	7,055	-
Total derivative financial instrument assets	**604,342**	**1,073,820**
Other financial assets:		
New Zealand equities – State-Owned Entities	11,052	3,463
New Zealand equities – Other	1,042,653	878,725
Global equities	4,645,336	4,394,326
Total equities	**5,699,041**	**5,276,514**
New Zealand fixed interest – Crown	199,045	-
New Zealand fixed interest – State-Owned Entities	20,954	2,837
New Zealand fixed interest – Local Bodies	2,204	16,854
New Zealand fixed interest – Other	169,957	134,548
Global fixed interest	3,690,534	2,087,773
Total fixed interest	**4,082,694**	**2,242,012**
Collective investment funds	1,650,283	1,961,459
Insurance-linked investments – catastrophe bonds	187,896	-
Floating rate notes	122,250	-
Private equity	398,060	226,416
Redeemable preference shares	57,500	-
Unlisted unit trusts	267,615	507,567
Total other financial assets	**12,465,339**	**10,213,968**
Total financial assets	**13,069,681**	**11,287,788**
Investments accounted for using the equity method (refer note 7(f))	**856,585**	**837,648**
Non-financial assets – timber investments – forests (refer note 7(g))		
New Zealand timber investments – forests	147,016	138,988
Total timber investments- forests	**147,016**	**138,988**
Total investments	**14,073,282**	**12,264,424**

Notes to the Financial Statements (continued)

For the year ended 30 June 2010

	GROUP ACTUAL	
	2010 NZ$000	2009 NZ$000
7. INVESTMENTS (continued)		
(A) INVESTMENTS BY ASSET TYPE (continued)		
Financial liabilities		
Derivative financial instrument liabilities:		
Forward foreign exchange contracts	178,242	95,994
Cross currency swaps	21,739	-
Asset swaps	88,193	169
Equity swaps	194,286	37,114
Credit default swaps	38,610	-
Commodity swaps	-	16,646
Insurance-linked options	814	-
Insurance-linked swaps	8,164	-
Total derivative financial instrument liabilities	**530,048**	**149,923**
Net investments	**13,543,234**	**12,114,501**

(B) RESTRICTIONS

During the year the Group participated in a securities lending program which was subsequently wound up by 30 June 2010. Credit risk associated with the securities lending program was mitigated by requiring the borrower to provide daily collateral in the form of cash or readily marketable securities (non-cash) of greater market value than the securities loaned. As at 30 June 2009, the Group's global equities investments included loaned securities with a fair value of $278,283,000. The fair value of non-cash collateral held (by a third-party agent) in respect of these loans was $556,000. This was not recognised in the Group's financial statements as the non-cash collateral is not able to be sold or repledged. In 2009, cash collateral received in respect of securities lent was invested in the collective investment fund referred to in note 7(d). The obligation to repay collateral to borrowers at 30 June 2009 of $293,379,000 disclosed in note 12 was funded out of cash, in the normal course of business.

(C) FAIR VALUES

The basis of the fair value determination is set out in the statement of accounting policies.

(D) ILLIQUID SECURITIES

During the prior year the Group redeemed its interests in a collective investment fund which was principally used to generate returns from cash collateral provided by borrowers in the Group's securities lending program. The Group received a transfer of a pro rata share of the assets of the collective investment fund. In addition to cash, the assets received were asset-backed securities, medium-term notes, and corporate bonds. During the current year some of these assets have either matured or have been sold in the normal course of business. The fair value of the remaining securities is $90,631,000 (2009:$164,686,000), which is included in the global fixed interest asset category. Securities with a fair value of $3,712,000 (2009:$9,120,000) are currently past due, and this fact is reflected in their valuation. Securities with a fair value of $9,853,000 (2009:$6,450,000) have had their terms renegotiated and are no longer past due. In addition to the securities received, the Group received a pro-rata share of a capital support agreement as disclosed in note 8.

Notes to the Financial Statements (continued)

For the year ended 30 June 2010

7. INVESTMENTS (continued)

(E) INVESTMENTS IN SUBSIDIARIES

NAME OF SUBSIDIARY	NOTE	BALANCE DATE	COUNTRY OF INCORPORATION	OWNERSHIP INTEREST 2010 %	2009 %
CNI Timber Operating Company Limited	(i)	30 June	New Zealand	0%	0%
Separate Account NZ0001 of Horseshoe Re Limited	(ii)	31 December	Bermuda	100%	0%
Separate Account NZ0002 of Horseshoe Re Limited	(ii)	31 December	Bermuda	100%	0%

(i) All of the shares in CNI Timber Operating Company Limited are legally owned by the Guardians. However, beneficial ownership of the shares remains with the Fund, and as such this company has been consolidated into these financial statements. Section 59 of the Act restricts the Fund from taking an enduring controlling interest in any other entity. From time to time, opportunities to purchase privately traded assets carry associated obligations to take over operating entities specific to that asset. There is a need to balance the benefit to the Fund of progressing with the transaction against the restriction on taking control of the operating entity. The acquisition of CNI Timber Operating Company Limited arose during the purchase of timberland estate. The Group has been restructured so that legal ownership of this entity sits with the Guardians. However, due to certain performance guarantee contracts that exist within the company which have not been transferred, the beneficial ownership of the shares has been retained by the Fund.

(ii) During the year, the Fund established two separate accounts (NZ0001 and NZ0002) in a Bermudan segregated account company, Horseshoe Re Limited. Horseshoe Re Limited acting for, and for the benefit of, the separate accounts enters into agreements relating to the Fund's investments in insurance-linked products. Section 59 of the Act restricts the Fund from taking an enduring controlling interest in any other entity. As a matter of Bermudan law, a segregated account is not a "legal person" and has no existence separate from the segregated account company. In addition, the Fund does not control the segregated account company. Therefore even though the separate accounts have been consolidated into these financial statements they are not "entities" for the purposes of section 59 of the Act and accordingly the interest held does not constitute a breach of that section.

The Fund holds investments in a number of entities where it's ownership interest exceeds 50%. The Fund has no power to govern the financial and operating policies of these entities, and therefore does not have control. As such, investments in these entities have been designated as at fair value through profit or loss in accordance with NZ IAS 39 Financial Instruments: Recognition and Measurement.

(F) INVESTMENTS ACCOUNTED FOR USING THE EQUITY METHOD

	GROUP ACTUAL 2010 NZ$000	2009 NZ$000
Investments in associates	**856,585**	**837,648**

NAME OF ENTITY	BALANCE DATE	COUNTRY OF INCORPORATION	OWNERSHIP INTEREST 2010 %	2009 %
Kaingaroa Timberlands Partnership	30 June	New Zealand	40%	40%

	GROUP ACTUAL 2010 NZ$000	2009 NZ$000
Associate		
Carrying amount at start of year	837,648	510,228
Acquisition of associate	-	195,714
Share of recognised revenues and expenses	51,510	144,200
Return of capital	(32,573)	(12,494)
Carrying amount at end of year	**856,585**	**837,648**
Goodwill at the start of the year	-	-
Goodwill at the end of the year	-	-

Notes to the Financial Statements (continued)

For the year ended 30 June 2010

	GROUP ACTUAL	
	2010 NZ$000	2009 NZ$000
7. INVESTMENTS (continued)		
(F) INVESTMENTS ACCOUNTED FOR USING THE EQUITY METHOD (continued)		
Summarised financial information of associate company:		
Current assets	81,245	50,546
Non-current assets	2,151,989	2,046,732
	2,233,234	**2,097,278**
Current liabilities	30,991	13,495
Non-current liabilities	-	-
	30,991	**13,495**
Net assets	**2,202,243**	**2,083,783**
Revenue	191,103	266,810
Net profit	158,323	137,634
Share of associate's profit	51,510	144,200

(G) NON-FINANCIAL ASSETS – TIMBER INVESTMENTS – FORESTS

Timber investments – forests are accounted for under NZ IAS 41 Agriculture, and carried at fair value less estimated point of sale costs. Timber investments – land is accounted for under NZ IAS 16 Property, Plant and Equipment, and is carried at fair value with revaluations reflected in reserves.

	GROUP ACTUAL	
	2010 NZ$000	2009 NZ$000
Gross carrying amount – forests		
Carrying amount at start of year	138,988	259,630
Additions	447	731
Disposals	(1,893)	(88,169)
Fair value changes in timber investments – forests	9,842	(33,204)
Other changes	(368)	-
Carrying amount at end of year	**147,016**	**138,988**

At 30 June 2010, the Group's forests measured approximately 15,065 hectares (2009: 16,200 hectares). During the year ended 30 June 2010, the Group harvested 0.51 million m3 (2009: 0.3 million m3). Average estate age increased slightly from 16 years to 16.1 years.

The forests have been measured at fair value based on a net present value or discounted cash flow approach. The following methodology and assumptions were applied:

An estate-based approach was employed whereby the net cash flows for each geographically distinct area was forecast and discounted to provide a forest value. These cash flows reflect management's future harvesting and silvicultural intentions for the forest.

Notes to the Financial Statements (continued)

For the year ended 30 June 2010

7. INVESTMENTS (continued)

(G) NON-FINANCIAL ASSETS – TIMBER INVESTMENTS – FORESTS (continued)

(a) The forests have been valued on the basis of a going concern and captures the value of the existing crop on a single rotation basis.

(b) Notional land rental costs have been included for freehold land based on current government valuations.

(c) The net present value is calculated using a pre-tax discount rate of 8.6 – 9.5% (2009: 8.55 – 9.5%).

(d) The cash flows do not take into account income tax.

(e) No allowance for inflation has been provided.

(f) The impact of movement in prices is estimated by adjusting the starting prices for price forecasting by the quarter-on-quarter movement in market prices and maintaining a consistent price path to the long-run averages by grade category.

(g) Costs are current average costs. No allowance has been made for cost improvements in future operations.

(h) The net change in value arising from harvest, growth, and change in prices by log grade category is taken as the change in fair market value of the crop and is included in profit or loss in the statement of comprehensive income.

(i) Estimated point of sale costs of 1% have been deducted from the fair valuation.

Forest financial risk management strategy

The Group has procedures in place to minimise damage to forest assets from climatic risks, pests and diseases, nutrient deficiencies and imbalances, fire, and flood risk. As a member of the New Zealand Forest Owners Association the Group subscribes to the annual national forest health surveillance programme. This programme helps early detection of any exotic disease or pest incursion, data to meet New Zealand's international forest reporting requirements and forest health management information.

In addition, pest and disease populations are constantly monitored through annual region-specific surveys, site or species specific pest surveys and visual assessment by contractors. This information is then used to determine where to carry out control operations.

New Zealand forests have historically experienced low forest loss due to fire as a result of both climatic conditions and management regimes directed toward active fire risk reduction. The Group owns a number of fire fighting resources and these are located around the districts as defined by risk factors at any given point in time.

Emissions trading scheme

The New Zealand Emissions Trading Scheme (ETS) was established by the passing of the Climate Change Response Act 2002. The legal requirements relating to forestry in the ETS are set out in the Climate Change (Forestry Sector) Regulations 2008.

Participants in the ETS have three core obligations:

(1) monitor their emissions and/or removals of greenhouse gases;

(2) report these to the Government by periodically filing an emissions return;

(3) surrender units to cover their reported emissions, or to claim units for their removals.

The primary unit of trade in the ETS is the New Zealand Unit (NZU). One NZU represents one tonne of carbon dioxide (CO2) either released to the atmosphere (emissions) or removed from the atmosphere (removals).

The forestry sector became a participant in the ETS from 1 January 2008. Participation in the ETS is mandatory for owners of pre-1990 forest land, while owners of post-1989 forest land may opt into the ETS voluntarily.

Post-1989 forest land is exotic or indigenous forest that is established after 31 December 1989 on land that was not forest land on 31 December 1989.

Pre-1990 forest land is an area of forest land covered by predominantly exotic forest species that was established on or before 31 December 1989 and that remained forest land on 31 December 2007.

The Group owns approximately 6,300ha of pre-1990 forest land for which participation in the ETS is mandatory. The Group also owns approximately 4,500 ha of post-1989 forest land for which participation in the ETS is voluntary. The Group has yet to decide whether it will opt-in to the ETS for its post-1989 forests.

Notes to the Financial Statements (continued)

For the year ended 30 June 2010

7. INVESTMENTS (continued)

(G) NON-FINANCIAL ASSETS – TIMBER INVESTMENTS – FORESTS (continued)

Owners of pre-1990 forest land will receive a free allocation of NZU's in partial compensation for the loss in value of their land as a result of the introduction of the ETS. The free allocation is likely to be finalised in the next financial year with the NZU's being received in two tranches. The first tranche of 38% of the Group's overall entitlement will be transferred by 31 December 2012, with the second tranche of 62% to be received after 31 December 2012.

It is estimated that the Group will receive approximately 245,700 NZU's as part of the free allocation.

As a result of carbon sequestered from 1 January 2008 to 30 June 2010, the Group would receive approximately 295,000 NZU's should it opt-in to the ETS for its post-1989 forests.

The current price of NZU's is uncertain, as the market is not yet fully established but indications are that NZU's are currently trading at approximately NZ $18 per NZU.

(H) INVESTMENTS IN JOINT VENTURES

Investments in joint ventures that have been designated as at fair value through profit or loss are classified as private equity investments.

			OWNERSHIP INTEREST	
	BALANCE	COUNTRY OF	2010	2009
JOINTLY CONTROLLED ENTITIES DESIGNATED AT FAIR VALUE	DATE	INCORPORATION	%	%
Aotea Energy Holdings Limited	31 March	New Zealand	50%	0%

The Fund's share of the capital commitments of joint ventures is $9,715,000 (2009: $nil).

	GROUP ACTUAL	
	2010	2009
	NZ$000	NZ$000
8. TRADE AND OTHER RECEIVABLES		
Trade receivables	4,973	2,889
Allowance for doubtful debts	-	-
	4,973	**2,889**
Accrued interest	62,602	28,657
Dividends receivable	19,907	18,254
Unsettled sales	475,955	447,614
GST receivable	207	183
Capital support agreements receivable	20,708	38,983
	584,352	**536,580**

Trade receivables have standard 30 day terms.

The timing and amount of expected cashflows for accrued interest, dividends receivable, and unsettled sales are certain as they are based on contractual terms and corporate actions. All receivables are expected to be settled within one year.

No allowance has been made for irrecoverable amounts as the Group has assessed that there is no evidence of impairment.

The capital support agreements receivable relates to the Group's investment of securities lending cash collateral in a collective investment fund in the prior year. A number of letters of credit were issued by Bank of America N.A. for the benefit of the collective investment fund. In the prior year, the Group redeemed its interests in the collective investment fund. As part of the redemption arrangements any non-transferrable assets, including a proportionate share of the benefits of the capital support agreements are held on trust by the collective investment fund for the Group. During the year a portion of the capital support agreements receivable was recovered. The Group's remaining proportionate share of the proceeds of the letters of credit is expected to be recovered when the capital support is drawn upon by the collective investment fund which is expected to be in the year ending 30 June 2011. The fair value of the Group's proportionate share of the capital support agreements receivable is $20,708,000 (2009: $38,983,000).

Notes to the Financial Statements (continued)

For the year ended 30 June 2010

	GROUP ACTUAL 2010 NZ$000	GROUP ACTUAL 2009 NZ$000
9. OTHER ASSETS		
Prepayments	63	59
	63	**59**

GROUP ACTUAL	LAND AND LAND IMPROVEMENTS NZ$000	OFFICE EQUIPMENT NZ$000	COMPUTER EQUIPMENT NZ$000	OFFICE FITOUT NZ$000	TOTAL NZ$000
10. PROPERTY, PLANT, AND EQUIPMENT					
Gross carrying amount					
Balance at 1 July 2008	100,485	323	235	1,223	102,266
Additions	587	-	231	302	1,120
Disposals	(65,934)	-	-	-	(65,934)
Net revaluation increments/(decrements)	3,188	-	-	6	3,194
Foreign exchange gain/(loss) on translation	11,427	-	-	-	11,427
Balance at 30 June 2009	**49,753**	**323**	**466**	**1,531**	**52,073**
Additions	59	-	161	14	234
Disposals	-	(16)	(28)	(19)	(63)
Net revaluation increments/(decrements)	(1,888)	-	-	20	(1,868)
Balance at 30 June 2010	**47,924**	**307**	**599**	**1,546**	**50,376**
Accumulated depreciation					
Balance at 1 July 2008	614	60	96	110	880
Depreciation expense	380	46	113	137	676
Balance at 30 June 2009	**994**	**106**	**209**	**247**	**1,556**
Depreciation expense	531	41	199	149	920
Depreciation recovered	-	(4)	(22)	(3)	(29)
Balance at 30 June 2010	**1,525**	**143**	**386**	**393**	**2,447**
Net book value					
As at 30 June 2009	48,759	217	257	1,284	50,517
As at 30 June 2010	**46,399**	**164**	**213**	**1,153**	**47,929**

Land as part of the New Zealand timber investments was valued by Telfer Young (Northland) Ltd, an independent registered valuer. The valuer uses New Zealand Valuation and Property Standards as a reference, to determine the fair value of the land. Fair value is the amount for which the assets could be exchanged between a knowledgeable willing buyer and a knowledgeable willing seller in an arm's length transaction as at the valuation date. Fair value is determined by direct reference to recent market transactions for land of comparable size and location as that held by the Group.

The valuations were obtained as at 30 June 2010. The revaluation surplus has been taken to the land revaluation reserve.

Carrying amount that would have been recognised under the cost model $40,176,000 (2009: $40,610,000).

Notes to the Financial Statements (continued)

For the year ended 30 June 2010

	GROUP ACTUAL	
	2010 NZ$000	2009 NZ$000
11. INTANGIBLE ASSETS		
Gross carrying amount		
Opening balance	477	253
Additions – Computer software	941	224
Disposals – Computer software	(75)	-
Closing balance	**1,343**	**477**
Accumulated amortisation		
Opening balance	222	66
Amortisation expense	478	156
Amortisation recovered	(59)	-
Closing balance	**641**	**222**
Net book value	**702**	**255**
12. TRADE AND OTHER PAYABLES		
Trade payables	3,725	2,566
Accrued expenses	11,226	23,071
Unsettled purchases	475,722	90,983
Related party payable to Guardians	1,944	1,037
Collateral repayable to borrowers in the securities lending program	-	293,379
	492,617	**411,036**

The average credit period on purchases is 30 days. No interest is charged on overdue balances. The Group has financial risk management policies in place to ensure that all payables are paid within the credit time frame.

The timing and amount of expected cash flows for unsettled purchases are certain as they are based on contractual terms and corporate actions. All payables are expected to be settled within one year.

Collateral is recognised as a payable when borrowers have provided cash collateral which can be sold or repledged by the Group. The collateral is repayable to borrowers on the return of loaned securities. The loan terms are generally no longer than one year.

	GROUP ACTUAL	
	2010 NZ$000	2009 NZ$000
13. PROVISION FOR PERFORMANCE-BASED FEES		
Balance brought forward	1,943	40,185
New provision during the year	1,379	1,943
Unused provision released during the year	(16)	(6,389)
Paid out during the year	-	(33,796)
Closing provision	**3,306**	**1,943**
Represented by:		
Current	2,343	-
Non-current	963	1,943
	3,306	**1,943**

Investment managers earn performance-based fees once agreed hurdles are reached. The payout of the current year fee is capped, with the remainder of the fee being held by the Group for possible payout in future periods. Poor performance in the following years may lead to a reduction in the entitlement that is being held. Thus the amount and timing of the eventual payout is uncertain.

Notes to the Financial Statements (continued)

For the year ended 30 June 2010

14. AMOUNTS EXPECTED TO BE RECOVERED OR SETTLED AFTER MORE THAN TWELVE MONTHS

The Group's statement of financial position is presented on a liquidity basis. Accordingly, certain line items combine amounts expected to be recovered or settled no more than twelve months after balance date and amounts expected to be recovered or settled more than twelve months after balance date. The following table sets out the amounts expected to be recovered or settled after more than twelve months:

	GROUP ACTUAL	
	2010 NZ$000	2009 NZ$000
ASSETS		
Trade and other receivables	-	38,983
Investments		
Investments – derivative financial instrument assets	232,175	101,493
Investments – other financial assets	845,425	733,983
Investments accounted for using the equity method	856,585	837,648
Timber investments – forest	147,016	138,988
Total investments	**2,081,201**	**1,812,112**
Deferred tax asset	-	371,490
Property, plant, and equipment	47,929	50,517
Intangible assets	702	255
Total assets	**2,129,832**	**2,273,357**
LIABILITIES		
Investments – derivative financial instrument liabilities	133,491	4,766
Provisions	963	1,943
Deferred tax liability	36,721	-
Total liabilities	**171,175**	**6,709**
Net assets	**1,958,657**	**2,266,648**

15. MANAGEMENT OF FUND CAPITAL AND RESERVES

OBJECTIVES, POLICIES, AND PROCESSES FOR MANAGING THE FUND'S CAPITAL

The Fund's "capital" comprises the investments and all other assets of the Fund less any liabilities.

FUNDING – INVESTMENT CAPITAL

The Fund is the property of the Crown. Its purpose is to build a portfolio of financial assets to help reduce the impact of providing retirement income, in the form of New Zealand superannuation, to an ageing population. The Crown is required to make capital contributions to the Fund in accordance with Sections 42 to 44 inclusive of the Act. The Government announced in the 2009 Budget a reduction in contributions to the Fund. Full capital contributions are projected to resume from 2020 under current Treasury modelling, however this may change based on future Fiscal and Economic Updates.

FUNDING – NET COST OF SUPERANNUATION ENTITLEMENTS

Under Section 45 of the Act, the Minister of Finance must ensure that sufficient money is transferred into the Fund in each financial year to meet the net cost of the superannuation entitlements that are payable out of the Fund. As no capital withdrawals are permitted from the Fund in any financial year commencing before 1 July 2020, the Minister of Finance is obliged to provide funding to meet ongoing superannuation entitlements in addition to the capital contributions paid under Section 42 of the Act. The Treasury, through the New Zealand Debt Management Office, has facilitated the flow of funding for superannuation entitlements from the Minister of Finance to the Ministry of Social Development on behalf of the Fund. The Guardians have had no control over these transfers, with The Treasury acting as agent for the Fund.

Notes to the Financial Statements (continued)

For the year ended 30 June 2010

15. MANAGEMENT OF FUND CAPITAL AND RESERVES (continued)

MANAGEMENT OF THE FUND'S CAPITAL

The Fund is a profit-oriented entity, managed by the Guardians. The Guardians' mandate is to invest the Fund on a prudent, commercial basis, and in doing so, ensure that the Fund is managed and administered in a manner consistent with best-practice portfolio management, maximising return without undue risk to the Fund as a whole, and avoiding prejudice to New Zealand's reputation as a responsible member of the world community. The Fund invests the contributions from the Crown, in accordance with the Statement of Investments Policies, Standards and Procedures, which is available at www.nzsuperfund.co.nz

The Guardians review the Fund's investment policies and strategic asset allocation on a regular basis to ensure it is efficient over the longer term.

The Guardians have determined investment policies and a strategic asset allocation (SAA) that, in their view and on the basis of professional advice received, best meets their statutory obligation to maximise the return to the Fund without undue risk and best meets the Guardians' investment objective for the Fund. This is reviewed from time-to-time.

The SAA highlights target levels for asset classes. It does not reflect the Fund's current holdings. The difference between the Fund's current and target holdings is made up through the use of proxies, whereby any differences for the private market holdings are made up of offsetting holdings of other, more readily accessible assets such as listed equities and fixed interest. The table below shows the target weights and ranges (before proxies) as at 30 June 2010. These have not changed since the prior year.

	30 JUNE 2010 %	RANGES %
SECTOR		
Global large cap equities	32.0	
Global small cap equities	5.5	
New Zealand equities	7.5	
Emerging market equities	3.0	
Property	10.0	
Private markets:		
Private equity	5.0	0-10
Infrastructure	5.0	0-15
Other private markets	5.0	0-10
Timber	5.0	0-10
Total private markets	20.0	
Commodities	5.0	
Fixed interest	17.0	
Total portfolio	**100.0**	
Net unhedged foreign currency exposure	10.0	

NATURE AND PURPOSE OF RESERVES

Land revaluation reserve

The land revaluation reserve is used to record increases and decreases in the fair value of land and land improvements.

Available-for-sale reserve

This reserve records movements in the fair value of available-for-sale financial assets.

Foreign currency translation reserve

The foreign currency translation reserve is used to record exchange differences arising from the translation of the financial statements of foreign subsidiaries.

Notes to the Financial Statements (continued)

For the year ended 30 June 2010

16. COMMITMENTS AND CONTINGENT LIABILITIES

At year end, the Group had commitments to private equity funds totalling $663,800,000 (2009: $430,560,000), of which $215,939,000 has been called and paid (2009: $172,099,000). Capital called as at balance date but not yet paid amounted to $9,583,000 (2009: $5,638,000). The Group also had other commitments of $648,887,000 (2009: $663,826,000), of which $244,906,000 has been called upon (2009: $173,118,000). These commitments are denominated in the foreign currency of the respective fund, and have been translated at the year-end rate.

The Group has a contingent liability in respect of it's pre-1990 forests which are part of the New Zealand Emissions Trading Scheme. Should the Group harvest, and not re-plant, all of it's pre-1990 forests, it would have a liability under the ETS of approximately $85,482,000 determined at 30 June 2010 (2009: $89,118,000). The amount and timing of any liability is uncertain and is dependent on the intention of the Group with respect to re-establishing forests after harvesting, and the price of carbon at the time of emission.

17. RELATED PARTY DISCLOSURES

(A) PARENT ENTITIES

The Fund is managed and administered by the Guardians which in turn are a wholly owned entity of the Crown. Both the Guardians and the Crown produce financial statements which are available to the public.

(B) EQUITY INTERESTS IN RELATED PARTIES

Details of the interests held in subsidiaries, associates and joint ventures are disclosed in notes 7(e), 7(f) and 7(h) (respectively) to the financial statements.

(C) TRANSACTIONS WITH RELATED PARTIES

The Guardians have paid expenses relating to the Group, as it is required to do under the Act. A portion of these expenses is reimbursed by the Fund as is entitled under the Act. These expenses are included in the financial statements of the Guardians. The amount of the reimbursement to the Guardians for the financial year was $15,973,000 (2009: $11,635,000).

The Group and the New Zealand Debt Management Office (NZDMO) are consolidated into the Crown financial statements. The Group transacts with the NZDMO for a portion of its foreign exchange contracts and cross currency swaps. The rates at which the Group transacts are negotiated with the NZDMO. The fair value of outstanding contracts at year end was an asset of $250,526,000 (2009: asset $767,317,000). Gains on contracts with the NZDMO recognised in the statement of comprehensive income for the year were $827,554,000 (2009: losses $812,671,000). All other transactions with government entities are on an arm's length basis.

The Group has invested a proportion of its assets in fixed income securities and equities issued by the Government, Crown Entities, and State-Owned Entities. These are detailed in note 7. The income earned from these investments is detailed in note 2.

18. SUBSEQUENT EVENTS

There were no reportable events subsequent to year end.

19. NOTES TO THE STATEMENT OF CASH FLOWS

(A) RECONCILIATION OF CASH AND CASH EQUIVALENTS

For the purposes of the statement of cash flows, cash and cash equivalents includes cash balances on hand, held in bank accounts, demand deposits, and other highly liquid investments. Cash and cash equivalents at the end of the financial year as shown in the statement of cash flows is reconciled to the related items in the statement of financial position as follows:

	GROUP ACTUAL	
	2010 NZ$000	2009 NZ$000
Cash and cash equivalents	1,942,798	1,060,920

At balance date, cash of $228,993,000 (2009: $809,439,000) had been allocated and was held by Investment Managers awaiting investment.

Notes to the Financial Statements (continued)

For the year ended 30 June 2010

19. NOTES TO THE STATEMENT OF CASH FLOWS (continued)

(B) FUTURES MARGIN ACCOUNTS

$58,964,000 of cash balances (2009: $112,872,000) are held in separate bank accounts lodged with the relevant futures exchange. These funds have been pledged as collateral for potential margin callls on futures of $nil (2009: $nil) held by the Group.

(C) COLLATERAL PLEDGED

The cash balance pledged as collateral to meet obligations under Credit Support Agreements for derivative positions is $202,178,000 (2009: $nil). The counterparties are not permitted to sell or repledge the collateral cash balances. The pledged assets will be returned to the Group when the underlying transaction is terminated, but in the event of default the counterparty is entitled to apply the collateral in order to settle the liability.

(D) COLLATERAL RECEIVED

The cash balance received as collateral to meet obligations under Credit Support Agreements for derivative positions is $93,288,000 (2009: $72,106,000). The Group is not permitted to sell or repledge the collateral cash balances. The pledged assets will be returned to the counterparties when the underlying transaction is terminated, but in the event of default the Group is entitled to apply the collateral in order to settle the liability.

(E) RECONCILIATION OF PROFIT/(LOSS) FOR THE YEAR TO NET CASH FLOWS FROM OPERATING ACTIVITIES

	GROUP ACTUAL	
	2010 NZ$000	2009 NZ$000
Profit/(loss) for the year after income tax expense	1,707,779	(2,793,086)
Add/(deduct) non-cash items:		
Share of profit of investments accounted for using the equity method	(51,510)	(144,200)
Depreciation and amortisation of non-current assets	1,398	832
Fair value changes in timber investments – forests	(9,842)	33,204
Unrealised fair value changes in investments	(1,492,632)	4,261,761
Net foreign exchange (gain)/loss	(196,768)	(669,107)
Other non-cash items	14,226	4,533
Add items classified as investing activities:		
Loss on disposal of property, plant, and equipment	33	7,546
Changes in net assets and liabilities:		
(Increase)/decrease in assets:		
Trade and other receivables	(47,772)	(320,725)
Other assets	(4)	2
Increase/(decrease) in current tax balances	(102,711)	158,741
Increase/(decrease) in liabilities:		
Trade and other payables	81,581	183,745
Provisions	1,363	(38,242)
Increase/(decrease) in deferred tax balances	408,211	(413,318)
Add/(deduct) changes in net assets and liabilities related to operating cash flows not included in net profit/(loss):		
Unsettled sales	28,341	295,498
Capital support agreements receivable	(18,275)	38,983
Unsettled purchases	(384,739)	115,318
Collateral repayable to borrowers in the securities lending program	293,379	(293,379)
Add/(deduct) net operating cashflows not included in net profit/(loss)	445,471	(1,963,271)
Net cash provided by/(used in) operating activities	**677,529**	**(1,535,165)**

Notes to the Financial Statements (continued)

For the year ended 30 June 2010

20. FINANCIAL INSTRUMENTS

(A) FINANCIAL ASSETS AND FINANCIAL LIABILITIES BY MEASUREMENT BASIS

Key: H4T: At fair value through profit or loss – Held for trading
Designated at FVTPL: Designated at fair value through profit and loss
L&R: Loans and receivables at amortised cost
A4S: Available for sale
Other: Amortised cost/cost/or equity accounted

	H4T NZ$000	DESIGNATED AT FVTPL NZ$000	L&R NZ$000	A4S NZ$000	OTHER NZ$000	TOTAL NZ$000
2010						
Financial assets						
Cash and cash equivalents					1,942,798	1,942,798
Trade and other receivables			584,352			584,352
Investments						
Investments – derivative financial instrument assets						
Forward foreign exchange contracts	348,963					348,963
Cross currency swaps	101,619					101,619
Asset swaps	301					301
Longevity contingent swaps	108,913					108,913
Futures contracts	-					-
Equity swaps	39					39
Commodity swaps	2,084					2,084
Credit default swaps	35,368					35,368
Insurance-linked swaps	7,055					7,055
	604,342	-	-	-	-	604,342
Investments – other financial assets:						
Equities						
New Zealand equities – State-Owned Entities		11,052				11,052
New Zealand equities – Other		1,042,653				1,042,653
Global equities		4,645,336				4,645,336
Total equities	-	5,699,041	-	-	-	5,699,041
Fixed interest						
New Zealand fixed interest – Crown		199,045				199,045
New Zealand fixed interest – State-Owned Entities		20,954				20,954
New Zealand fixed interest – Local Bodies		2,204				2,204
New Zealand fixed interest – Other		169,957				169,957
Global fixed interest		3,656,116	34,418			3,690,534
Total fixed interest	-	4,048,276	34,418	-	-	4,082,694
Collective investment funds		1,650,283				1,650,283
Insurance-linked investments – catastrophe bonds		187,896				187,896
Floating rate notes			122,250			122,250
Private equity		347,911		50,149		398,060
Redeemable preference shares			57,500			57,500
Unlisted unit trusts		267,615				267,615
	-	2,453,705	179,750	50,149	-	2,683,604
Investments accounted for using the equity method					856,585	856,585
Total investments	604,342	12,201,022	214,168	50,149	856,585	13,926,266
Total financial assets	**604,342**	**12,201,022**	**798,520**	**50,149**	**2,799,383**	**16,453,416**

Notes to the Financial Statements (continued)

For the year ended 30 June 2010

20. FINANCIAL INSTRUMENTS (continued)

(A) FINANCIAL ASSETS AND FINANCIAL LIABILITIES BY MEASUREMENT BASIS (continued)

	H4T NZ$000	DESIGNATED AT FVTPL NZ$000	L&R NZ$000	A4S NZ$000	OTHER NZ$000	TOTAL NZ$000
2010 (continued)						
Financial liabilities						
Trade and other payables					492,617	492,617
Derivative financial instrument liabilities:						
Forward foreign exchange contracts	178,242					178,242
Cross currency swaps	21,739					21,739
Asset swaps	88,193					88,193
Equity swaps	194,286					194,286
Credit default swaps	38,610					38,610
Insurance-linked options	814					814
Insurance-linked swaps	8,164					8,164
Total derivative financial instrument liabilities	530,048	-	-	-	-	530,048
Provisions					3,306	3,306
Total financial liabilities	**530,048**	**-**	**-**	**-**	**495,923**	**1,025,971**

Notes to the Financial Statements (continued)

For the year ended 30 June 2010

20. FINANCIAL INSTRUMENTS (continued)

(A) FINANCIAL ASSETS AND FINANCIAL LIABILITIES BY MEASUREMENT BASIS (continued)

	H4T NZ$000	DESIGNATED AT FVTPL NZ$000	L&R NZ$000	A4S NZ$000	OTHER NZ$000	TOTAL NZ$000
2009						
Financial assets						
Cash and cash equivalents					1,060,920	1,060,920
Trade and other receivables			536,580			536,580
Investments						
Investments – derivative financial instrument assets						
Forward foreign exchange contracts	905,839					905,839
Cross currency swaps	12,223					12,223
Asset swaps	3,904					3,904
Real estate swaps	40,937					40,937
Longevity contingent swaps	85,366					85,366
Equity swaps	25,551					25,551
	1,073,820	-	-	-	-	1,073,820
Investments – other financial assets:						
Equities						
New Zealand equities – State-Owned Entities		3,463				3,463
New Zealand equities – Other		878,725				878,725
Global equities		4,394,326				4,394,326
Total equities	-	5,276,514	-	-	-	5,276,514
Fixed interest						
New Zealand fixed interest – State-Owned Entities		2,837				2,837
New Zealand fixed interest – Local Bodies		16,854				16,854
New Zealand fixed interest – Other		134,548				134,548
Global fixed interest		2,087,773				2,087,773
Total fixed interest	-	2,242,012	-	-	-	2,242,012
Collective investment funds		1,961,459				1,961,459
Private equity		188,116		38,300		226,416
Global unit trusts		507,567				507,567
	-	2,657,142	-	38,300	-	2,695,442
Investments accounted for using the equity method					837,648	837,648
Total investments	1,073,820	10,175,668	-	38,300	837,648	12,125,436
Total financial assets	**1,073,820**	**10,175,668**	**536,580**	**38,300**	**1,898,568**	**13,722,936**
Financial liabilities						
Trade and other payables					411,036	411,036
Derivative financial instrument liabilities						
Forward foreign exchange contracts	95,994					95,994
Asset swaps	169					169
Equity swaps	37,114					37,114
Commodity swaps	16,646					16,646
Total derivative financial instrument liabilities	149,923	-	-	-	-	149,923
Provisions					1,943	1,943
Total financial liabilities	**149,923**	**-**	**-**	**-**	**412,979**	**562,902**

Notes to the Financial Statements (continued)

For the year ended 30 June 2010

20. FINANCIAL INSTRUMENTS (continued)

(B) FAIR VALUE

The Group uses various methods in estimating the fair value of a financial instrument. The methods comprise:

Level 1 – the fair value is calculated using quoted prices in active markets.

Level 2 – the fair value is estimated using inputs other than quoted prices included in Level 1 that are observable for the asset or liability, either directly (as prices) or indirectly (derived from prices).

Level 3 – the fair value is estimated using inputs for the asset or liability that are not based on observable market data.

The fair value of the financial instruments as well as the methods used to estimate fair value are summarised in the table below.

	NOTES	QUOTED MARKET PRICE (LEVEL 1) NZ$000	VALUATION TECHNIQUE – MARKET OBSERVABLE INPUTS (LEVEL 2) NZ$000	VALUATION TECHNIQUE – NON MARKET OBSERVABLE INPUTS (LEVEL 3) NZ$000	TOTAL NZ$000
2010					
Financial assets					
Investments					
Investments – derivative financial instrument assets					
Forward foreign exchange contracts			348,963		348,963
Cross currency swaps			101,619		101,619
Asset swaps			301		301
Longevity contingent swaps	(i)			108,913	108,913
Futures contracts			-		-
Equity swaps			39		39
Commodity swaps			2,084		2,084
Credit default swaps			35,368		35,368
Insurance-linked swaps			7,055		7,055
		-	495,429	108,913	604,342
Investments – other financial assets:					
Equities					
New Zealand equities – State-Owned Entities		11,052			11,052
New Zealand equities – Other		1,042,653			1,042,653
Global equities	(ii)	4,634,780		10,556	4,645,336
Total equities		5,688,485	-	10,556	5,699,041
Fixed interest					
New Zealand fixed interest – Crown			199,045		199,045
New Zealand fixed interest – State-Owned Entities			20,954		20,954
New Zealand fixed interest – Local Bodies			2,204		2,204
New Zealand fixed interest – Other			169,957		169,957
Global fixed interest	(iii)		3,632,230	23,886	3,656,116
Total fixed interest		-	4,024,390	23,886	4,048,276
Collective investment funds			1,650,283		1,650,283
Insurance-linked investments – catastrophe bonds			187,896		187,896
Private equity	(iv)			398,060	398,060
Unlisted unit trusts	(iv)			267,615	267,615
		-	1,838,179	665,675	2,503,854
Total financial assets at fair value		**5,688,485**	**6,357,998**	**809,030**	**12,855,513**

Notes to the Financial Statements (continued)

For the year ended 30 June 2010

20. FINANCIAL INSTRUMENTS (continued)

(B) FAIR VALUE (continued)

	NOTES	QUOTED MARKET PRICE (LEVEL 1) NZ$000	VALUATION TECHNIQUE – MARKET OBSERVABLE INPUTS (LEVEL 2) NZ$000	VALUATION TECHNIQUE – NON MARKET OBSERVABLE INPUTS (LEVEL 3) NZ$000	TOTAL NZ$000
2010 (continued)					
Financial liabilities					
Derivative financial instrument liabilities					
Forward foreign exchange contracts			178,242		178,242
Cross currency swaps			21,739		21,739
Asset swaps			88,193		88,193
Equity swaps			194,286		194,286
Credit default swaps			38,610		38,610
Insurance-linked swaps			8,164		8,164
Insurance-linked options		814			814
Total financial liabilities at fair value		**814**	**529,234**	**-**	**530,048**

(i) The fair value of longevity contingent swaps is provided by the counterparty, and is calculated by reference to movements in the underlying basket of contracts. The price provided by the counterparties is a non-binding bid price based on a valuation model which uses a discount rate. If reasonably possible alternative discount rates were applied, the fair value of the swap would increase by $11,206,000 or decrease by $7,437,000.

(ii) The fair value of listed equities is determined based on the last quoted bid price on the relevant exchange as of the close of business at balance date. In some instances, where the market on which the security is traded is not highly liquid, the price is determined using non-binding broker quotes. These securities have been classified as Level 3. A reasonably likely movement in the fair value in a one year period has been determined to be 26% based on internal risk modelling, which would increase or decrease the fair value of these securities by $2,740,000.

(iii) For Level 3 fixed interest securities where the market is illiquid (largely mortgage and asset-backed securities), prices are determined by a reputable pricing vendor or broker who uses models to value these securities. The models can utilise a variety of inputs including loan level data, prepayment and default assumptions and benchmark prices for similar securities. The Group does not have access to the underlying valuation models to disclose sensitivities to assumptions. However, a reasonably likely movement in the fair value in a one year period has been determined to be 50 basis points based on internal risk modelling. A 50 basis point movement would increase or decrease the fair value of these securities by $119,000.

(iv) The fair value of private equity funds, unlisted equity investments and unlisted unit trusts are provided by the investment manager or administrators. The price is based on the underlying net assets of the investment. Fair value is determined using a variety of methods, including independent valuations, valuation models based on the price of recent investments, earnings multiples, or discounted cash flows. The Group does not have access to the underlying valuation models to disclose sensitivities to assumptions. However a reasonably likely movement in the fair value in a one year period has been determined to be 25% for private equity funds, 19% for private timber funds and 16% for private infrastructure funds based on internal risk modelling. Applying these movements would increase or decrease the fair value of these investments by $116,785,000.

Transfers between categories

There were no significant transfers between Level 1 and Level 2 during the year.

Notes to the Financial Statements (continued)

For the year ended 30 June 2010

20. FINANCIAL INSTRUMENTS (continued)

(B) FAIR VALUE (continued)

Reconciliation of Level 3 fair value movements

The following table shows a reconciliation of all movements in the fair value of financial instruments categorised within Level 3 between the beginning and the end of the reporting period.

	2010 NZ$000
Opening balance	726,239
Gains and losses – profit or loss	10,406
Gains and losses – other comprehensive income	3,866
Purchases	247,496
Sales	(62,139)
Settlements	(28,068)
Transfers from other categories	574
Transfers to other categories	(89,344)
Closing balance	**809,030**
Total gain or loss stated in the table above for assets held at the end of the period:	
– Profit/(loss)	(16,613)
– Other comprehensive income	3,778

(C) FINANCIAL RISK MANAGEMENT OBJECTIVES

Through its activities the Group is exposed to the financial risks of market risk, credit risk, and liquidity risk.

The Guardians have established investment policies, standards, and procedures to manage the Group's exposure to financial risks. The Guardians manage the risks by adopting an appropriate risk profile that is commensurate with the return objective and time horizon of the Fund, avoiding concentration of risk by ensuring there is adequate diversification between and within asset classes and geographically; careful selection and monitoring of managers to ensure the Guardians have sufficient conviction that each manager will maximise the probability that return expectations for each asset class will be met and to ensure that there are no unintended biases away from the intended investment strategy; and rigorous measurement and management of market and manager risk.

Management monitors and manages the financial risks relating to the Group's operations through internal risk reports which analyse exposures by degree and magnitude of risks. These risks include market risk (which includes currency risk, interest rate risk, commodity risk, and equity price risk), credit risk, and liquidity risk. Management report regularly to the Board of the Guardians, and the Audit Committee.

Strategic Asset Allocation

	TARGET 2010 %	ACTUAL 2010 %	TARGET 2009 %	ACTUAL 2009 %
Sector				
Global large cap equities	32.0	35.3	32.0	35.1
Global small cap equities	5.5	6.2	5.5	6.3
New Zealand equities	7.5	6.3	7.5	6.3
Emerging market equities	3.0	3.6	3.0	3.6
Private markets	20.0	18.7	20.0	16.9
Property	10.0	9.2	10.0	10.9
Fixed interest	17.0	16.9	17.0	16.2
Commodities	5.0	4.6	5.0	4.7
Cash, collateral and foreign currency hedges	0.0	(0.8)	0.0	0.0
Total	**100.0**	**100.0**	**100.0**	**100.0**

Notes to the Financial Statements (continued)

For the year ended 30 June 2010

20. FINANCIAL INSTRUMENTS (continued)

(C) FINANCIAL RISK MANAGEMENT OBJECTIVES (continued)

Derivatives

The use of derivatives is governed by the Group's investment policies which provide written principles on the use of financial derivatives. Compliance with policies and exposure limits is reviewed by the Guardians on a continuous basis.

Derivatives may be used to manage risk or hedge against movements in interest rates, values, or prices in relation to permitted investments and movements in foreign currency exposures held within the Group; to achieve or reduce exposure to assets, all or part of any asset class and foreign currency; and to achieve transactional efficiency or reduce the transactional cost of achieving required exposures.

(D) SIGNIFICANT ACCOUNTING POLICIES

Details of the significant accounting policies and methods adopted, including the criteria for recognition, and the basis of measurement applied in respect of each class of financial asset, financial liability, and equity instrument are disclosed in note 1 to the financial statements.

(E) MARKET RISK

The market risks that the Group is primarily exposed to are: equity price risk, both globally and in New Zealand; interest rate risk (primarily to changes in New Zealand and United States interest rates); currency risk (primarily to changes in the New Zealand dollar versus the US dollar); and commodity price risk (primarily to changes in commodity price indices).

Market risk is managed for the Group as a whole as noted above under financial risk management objectives, policies, and processes. Market risk is further managed by requiring investment managers to manage their portfolios by tracking a benchmark index, within a defined tolerance for tracking error. The tolerance for tracking error imposes certain restrictions on the manager. Those restrictions will include limits on percentage weight of any particular company in the portfolio relative to its benchmark weight; limits on aggregate investment in companies not represented in the benchmark; limits on investment in any individual company not represented in the benchmark; limits on the maximum investment in any individual company; duration limits relative to the duration of the benchmark; and maximum limits on exposure to single entities.

(i) Equity price risk

The Group is exposed to changes in the price of equities listed on both New Zealand and international stock exchanges, as well as derivatives or unlisted equities where value is determined with reference to an equity market index, or comparable transactions in a listed equity market. The following table details the Group's sensitivity to a change of price with all other variables held constant. The percentages used represent management's assessment of a reasonably possible change in equity prices.

	%	PROFIT AFTER TAX (NZ$000)		OTHER COMPREHENSIVE INCOME NET OF TAX (NZ$000)	
		Increase	Decrease	Increase	Decrease
30 June 2010					
New Zealand equities	18%	185,409	(185,409)	-	-
Global large cap equities	16%	704,994	(704,994)	-	-
Global small cap equities	20%	98,011	(98,011)	-	-
Emerging markets equities	26%	135,532	(135,532)	-	-
Private equity	25%	68,494	(68,494)	5,254	(5,254)
30 June 2009					
New Zealand equities	19%	167,551	(167,551)	-	-
Global large cap equities	15%	662,262	(662,262)	-	-
Global small cap equities	18%	80,675	(80,675)	-	-
Emerging markets equities	27%	101,771	(101,771)	-	-
Private equity	25%	40,011	(40,011)	-	-

Notes to the Financial Statements (continued)

For the year ended 30 June 2010

20. FINANCIAL INSTRUMENTS (continued)

(E) MARKET RISK (continued)

(i) Equity price risk (continued)

	2010 NOTIONAL VALUE NZ$000	2010 FAIR VALUE NZ$000	2009 NOTIONAL VALUE NZ$000	2009 FAIR VALUE NZ$000
Equity derivatives at fair value at balance date:				
Equity swaps				
Assets	109,153	39	390,886	25,551
Liabilities	3,527,536	(194,286)	1,963,102	(37,114)
Equity futures				
Assets	864,480	-	636,223	-
Liabilities	(68,201)	-	(43,628)	-

The margin on futures contracts is settled daily. Contractual maturity of all swaps is within 90 days.

(ii) Foreign currency exchange rate risk

Currency risk is the risk that the value of a financial instrument will fluctuate due to changes in foreign exchange rates. The Group is exposed to currency risk through its investments in offshore assets and actively manages its risk by taking out forward foreign exchange contracts.

Currency risk is managed by:

(a) establishing a foreign currency hedging policy at a total fund level;

(b) specifying the bounds within which each manager may take on currency exposures relative to their benchmark; and

(c) engaging one or more currency execution agents to transact the Group's foreign exchange transactions, including both spot and forward transactions, at the most favourable rate.

The instruments managers may use, and the credit worthiness of the counterparties, are detailed in the investment management agreements with respective managers. Any forward contracts entered into must be with entities that have an appropriate minimum credit rating as determined by an international credit rating agency for counterparty risk and appropriate contractual arrangements must be in place between the currency manager and the counterparty.

Exposures are mainly economically hedged with derivative financial instruments such as forward foreign exchange contracts.

Notes to the Financial Statements (continued)

For the year ended 30 June 2010

20. FINANCIAL INSTRUMENTS (continued)

(E) MARKET RISK (continued)

(ii) Foreign currency exchange rate risk (continued)

	2010 ASSETS NZ$000	2009 ASSETS NZ$000
Foreign currency exposure:		
Australian Dollars	74,924	62,792
Brazilian Real	78,263	52,364
Canadian Dollars	115,133	41,433
Swiss Francs	80,076	28,126
Chilean Pesos	6,673	5,235
Chinese Yuan	62	351
Colombian Peso	2,380	1,586
Czech Republic Koruny	2,038	2,405
Danish Kroner	10,885	17,580
Egyptian Pounds	3,297	1,703
European Union Euros	313,204	216,369
United Kingdom Pounds	199,511	91,728
Hong Kong Dollars	195,348	158,592
Hungarian Forints	4,514	4,445
Indonesian Rupiahs	11,064	8,943
Israeli New Shekels	22,956	11,285
Indian Rupees	46,434	36,101
Japanese Yen	249,947	112,339
South Korean Won	77,407	58,285
Moroccan Dirhams	604	1,011
Mexican Pesos	22,488	18,693
Malaysian Ringgits	13,822	11,108
Norwegian Krone	7,367	15,658
Philippines Pesos	4,673	1,938
Pakistani Rupees	-	992
Polish Zlotych	7,509	5,875
Russian Rubles	149	94
Swedish Kronor	31,404	71,530
Singaporean Dollars	82,512	52,895
Thai Baht	10,523	5,850
Turkish New Lira	11,353	7,849
Taiwanese New Dollars	61,254	54,268
United States of America Dollars	543,136	355,366
South African Rand	42,676	35,207

This table shows effective foreign currency exposure after forward foreign exchange contracts have been taken into account.

Notes to the Financial Statements (continued)

For the year ended 30 June 2010

20. FINANCIAL INSTRUMENTS (continued)

(E) MARKET RISK (continued)

(ii) Foreign currency exchange rate risk (continued)

Foreign currency exposure (continued)

		CONTRACT VALUE NZ$000	FAIR VALUE NZ$000
Forward foreign exchange contracts (buy foreign currency/(sell foreign currency)):			
2010			
Less than 3 months		(3,063,848)	157,889
3 to 12 months		(5,766,811)	12,832
		(8,830,659)	**170,721**
2009			
Less than 3 months		(3,155,879)	233,814
3 to 12 months		(5,036,608)	576,031
		(8,192,487)	**809,845**

All forward foreign exchange contracts mature within 12 months.

Cross currency swaps (buy/sell):

2010			
2 to 5 years	NZD/USD	728,417	32,603
	NZD/JPY	130,288	(7,012)
	NZD/EUR	199,442	21,636
	NZD/GBP	177,462	6,222
5 to 10 years	NZD/USD	150,552	(6,390)
	NZD/EUR	298,593	32,821
		1,684,754	79,880
2009			
2 to 5 years	NZD/USD	357,890	12,223
		357,890	12,223

The target currency exposure of the Group is determined independently of the target asset exposures. The Strategic Asset Allocation target level for the net foreign exchange exposure by the Group, after currency hedging is 10% (2009: 10%).

Notes to the Financial Statements (continued)

For the year ended 30 June 2010

20. FINANCIAL INSTRUMENTS (continued)

(E) MARKET RISK (continued)

(ii) Foreign currency exchange rate risk (continued)

Foreign currency sensitivity

The following table details the Group's sensitivity to a change in the New Zealand dollar against the major foreign currencies, with all other variables remaining constant. The analysis has been performed only on the effective foreign currency exposure after allowing for the impact of forward foreign exchange contracts. The analysis has been performed on the same basis as 2009. The percentages used represent management's assessment of a reasonably possible change in foreign currency rates.

	%	PROFIT AFTER TAX (NZ$000)		OTHER COMPREHENSIVE INCOME NET OF TAX (NZ$000)	
		Increase	Decrease	Increase	Decrease
30 June 2010					
NZD:USD	10%	(86,753)	86,753	(1,445)	1,445
NZD:EUR	10%	(24,434)	24,434	-	-
NZD:GBP	10%	(14,365)	14,365	-	-
NZD:JPY	10%	(17,996)	17,996	-	-
NZD:Others	10%	(23,025)	23,025	-	-
30 June 2009					
NZD:USD	10%	(20,981)	20,981	(3,894)	3,894
NZD:EUR	10%	(15,146)	15,146	-	-
NZD:GBP	10%	(6,421)	6,421	-	-
NZD:JPY	10%	(7,864)	7,864	-	-
NZD:Others	10%	(54,194)	54,194	-	-

(iii) Interest rate risk

Interest rate risk is the risk that the value of the Group's investments in fixed interest securities and cash and cash equivalents will fluctuate due to changes in market interest rates. Interest rate risk management activities are undertaken by investment managers in accordance with their mandates. The intention of the Group is not necessarily to hold these assets to maturity, but to realise and purchase similar assets as part of the ongoing management of the investments of the Group.

The Group is primarily exposed to changes in New Zealand and US dollar short-term interest rates.

Notes to the Financial Statements (continued)

For the year ended 30 June 2010

20. FINANCIAL INSTRUMENTS (continued)

(E) MARKET RISK (continued)

(iii) Interest rate risk (continued)

Interest rate exposure – maturity profile of financial instruments

The following tables are based on the earlier of contractual repricing or maturity period, and exclude accrued interest.

	WEIGHTED AVERAGE EFFECTIVE INTEREST RATE %	VARIABLE INTEREST RATE NZ$000	FIXED MATURITY DATES LESS THAN 1 YEAR NZ$000	1 - 2 YEARS NZ$000	2 - 5 YEARS NZ$000	5 - 10 YEARS NZ$000	10+ YEARS NZ$000
2010							
Financial assets							
Cash and cash equivalents	3.64%	1,942,798					
New Zealand fixed interest – Crown	2.78%		199,045				
New Zealand State-Owned Entities	6.58%			18,000			2,954
Other investments	3.32%	947,038	246,832	155,242	1,198,402	1,100,013	394,918
		2,889,836	**445,877**	**173,242**	**1,198,402**	**1,100,013**	**397,872**
2009							
Financial assets							
Cash and cash equivalents	1.68%	1,060,920					
New Zealand State-Owned Entities	5.18%						2,837
Other investments	3.01%	360,907	18,361	143,167	736,024	788,848	191,868
		1,421,827	**18,361**	**143,167**	**736,024**	**788,848**	**194,705**

Asset swaps

The notional principal amounts, fair values and period of expiry of the asset swap contracts are as follows:

	2010 NOTIONAL VALUE NZ$000	2010 FAIR VALUE NZ$000	2009 NOTIONAL VALUE NZ$000	2009 FAIR VALUE NZ$000
2 to 5 years	570,234	(36,353)	91,755	(169)
5 to 10 years	368,213	(51,539)	266,135	3,904
	938,447	**(87,892)**	**357,890**	**3,735**

Notes to the Financial Statements (continued)

For the year ended 30 June 2010

20. FINANCIAL INSTRUMENTS (continued)

(E) MARKET RISK (continued)

(iii) Interest rate risk (continued)

Interest rate sensitivity

The sensitivity analysis in the table below of the effect on profit after tax and other comprehensive income has been determined based on the exposure to interest rates at the reporting date and the stipulated change taking place at the beginning of the financial year and held constant throughout the reporting period, with all other variables remaining constant. The analysis has been performed on the same basis as 2009. The percentages used represent management's assessment of a reasonably possible change in interest rates.

	BASIS POINTS	PROFIT AFTER TAX (NZ$000)		OTHER COMPREHENSIVE INCOME NET OF TAX (NZ$000)	
		Increase	Decrease	Increase	Decrease
30 June 2010					
Cash and cash equivalents	50	4,644	(4,644)	-	-
New Zealand fixed interest	50	(2,193)	2,193	-	-
Global fixed interest	50	(52,187)	52,187	-	-
30 June 2009					
Cash and cash equivalents	50	3,713	(3,713)	-	-
New Zealand fixed interest	50	(147)	147	-	-
Global fixed interest	50	(25,041)	26,227	-	-

	2010 NOTIONAL VALUE NZ$000	2010 FAIR VALUE NZ$000	2009 NOTIONAL VALUE NZ$000	2009 FAIR VALUE NZ$000
Fixed interest futures				
Assets	29,590	-	115,513	-
Liabilities	(131,180)	-	(373,121)	-

The margin on futures contracts is settled daily.

(iv) Commodity price risk

The Group is exposed to commodity price risk through its investments in commodity swaps. These investments are classified as held for trading. The commodity portfolios are designed to closely track the Dow Jones UBS Commodities Index.

Commodity price risk exposure

	2010 NOTIONAL VALUE NZ$000	2010 FAIR VALUE NZ$000	2009 NOTIONAL VALUE NZ$000	2009 FAIR VALUE NZ$000
Commodity swaps				
Assets	1,324,307	2,084	-	-
Liabilities	-	-	644,462	(16,646)

Notes to the Financial Statements (continued)

For the year ended 30 June 2010

20. FINANCIAL INSTRUMENTS (continued)

(E) MARKET RISK (continued)

(iv) Commodity price risk (continued)

Commodity price sensitivity

The following details the Group's sensitivity to a change in the commodity price index, with all other variables remaining constant. The analysis has been performed on the same basis as 2009. The percentages used represent management's assessment of a reasonably possible change in commodity prices.

	%	PROFIT AFTER TAX (NZ$000)		OTHER COMPREHENSIVE INCOME NET OF TAX (NZ$000)	
		Increase	Decrease	Increase	Decrease
30 June 2010					
Dow Jones UBS Commodities Index	22%	113,102	(113,102)	-	-
30 June 2009					
Dow Jones UBS Commodities Index	22%	96,683	(96,683)	-	-

(F) CREDIT RISK MANAGEMENT

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

The Group invests in a wide range of assets in New Zealand and overseas in accordance with its Statement of Investment Policies, Standards and Procedures. This contains credit and exposure policies to limit credit risk from the Group's investments.

Significant concentrations of credit risk

Concentration of credit risk exists if a single counterparty, or group of counterparties, are engaged in similar activities, operate within similar industries, geographies, or have similar economic characteristics that would cause their ability to meet contractual obligations to be similarly affected by changes in economic conditions. The maximum amount of credit risk for each class is the carrying amount in the statement of financial position.

The Group seeks to mitigate credit risk by applying policies as follows:

(1) Any investment that represents exposure to a single sector within one geography or is a listed security that is over 2% of the net asset value of the Fund requires Board approval; and

(2) Total direct exposure to a counterparty is capped at 2% of the Fund's net asset value.

Notes to the Financial Statements (continued)

For the year ended 30 June 2010

20. FINANCIAL INSTRUMENTS (continued)

(F) CREDIT RISK MANAGEMENT (continued)

At balance date, the Group has industry concentration risk in respect of its investments. The table below sets out the exposures by industry for all of the Group's investments.

	GROUP ACTUAL 2010 NZ$000	GROUP ACTUAL 2009 NZ$000
By industry		
Basic materials	1,061,416	1,367,924
Communications	89,975	48,914
Consumer – Cyclical	17,049	17,591
Consumer – Non-cyclical	902,573	800,410
Diversified	10,560	4,558
Energy	648,718	352,038
Financial	3,166,839	2,373,964
Funds	2,285,958	2,695,442
Government	1,843,400	806,722
Industrial	1,407,657	1,513,044
Mortgage securities	83,852	101,018
Technology	367,354	395,297
Utilities	756,695	669,945
Other	901,188	967,634
Net investments	**13,543,234**	**12,114,501**

At balance date, the Group has geographic concentration risk in respect of its investments. The table below sets out the exposures by geography for all of the Group's investments.

	GROUP ACTUAL 2010 NZ$000	GROUP ACTUAL 2009 NZ$000
New Zealand	3,318,391	3,567,313
Australia	767,107	562,012
Japan	526,354	488,497
United States	5,428,150	4,922,593
Canada	208,987	191,349
Europe	2,576,920	1,833,190
Other Asia	428,085	358,165
Central & South America	224,905	140,552
Africa	46,417	37,740
Middle East	17,918	13,090
Net investments	**13,543,234**	**12,114,501**

Notes to the Financial Statements (continued)

For the year ended 30 June 2010

20. FINANCIAL INSTRUMENTS (continued)

(F) CREDIT RISK MANAGEMENT (continued)

At balance date, the Group has counterparty exposure in respect of its forward foreign exchange contracts, cross currency swaps, commodity swaps, asset swaps, longevity contingent swaps, equity swaps, credit default swaps and insurance-linked swaps. The table below sets out the exposures by individual counterparty where an instrument has a positive fair value:

	GROUP ACTUAL	
	NOTIONAL VALUE NZ$000	FAIR VALUE NZ$000
2010		
Allied World Bermuda	13,997	1,727
Aspen Re	11,634	814
Barclays Bank plc	481,401	22,235
Barclays Capital plc	20,000	301
Commonwealth Bank of Australia	295	-
Credit Suisse First Boston	436,268	108,913
Deutsche Bank	1,179,871	14,639
Goldman Sachs & Co	339,633	1,180
JP Morgan Chase	102,109	295
Morgan Stanley & Co	8,556	227
New Zealand Debt Management Office	8,679,420	445,830
Northern Trust Singapore	6,380	82
Odyssey Re	25,304	2,025
Partner Re	29,521	1,998
State Street Bank & Trust Co	493	-
Taiping Re	5,817	491
UBS AG London	81,531	2,880
UBS New York	1	-
Westpac Banking Corp	35,787	705
	11,458,018	**604,342**

Notes to the Financial Statements (continued)

For the year ended 30 June 2010

20. FINANCIAL INSTRUMENTS (continued)

(F) CREDIT RISK MANAGEMENT (continued)

	GROUP ACTUAL	
	NOTIONAL VALUE NZ$000	FAIR VALUE NZ$000
2009		
ANZ Banking Corp	173,732	1,625
Barclays Bank plc	180,131	3,077
Barclays Wholesale GTS	17,223	540
BNP Paribas	1,137	20
Chase Manhattan Bank	995	28
Citibank NA	4,554	51
Citigroup Global Markets Australia	86,004	828
Commonwealth Bank of Australia	618,496	13,978
CSFB Global Foreign Exchange	69,586	478
Credit Suisse First Boston	463,106	85,366
Deutsche Bank	670,460	20,360
Goldman Sachs & Co	169,419	6,166
HSBC Bank USA	260	4
JP Morgan Securities Australia	171,348	38,031
Morgan Stanley Capital Services	(41,820)	12,091
National Australia Bank	820,931	13,207
New Zealand Debt Management Office	8,022,532	824,287
Northern Trust Singapore	14,623	856
RBS Financial Markets Treasury	151,427	2,928
Royal Bank of Canada	351,146	3,483
Société Générale	268,500	401
State Street Bank & Trust Co	896,812	14,783
State Street Boston DTC	316,480	2,204
UBS New York	145,057	4,327
UBS Singapore	85,029	665
Westpac Banking Corp	1,118,709	24,036
	14,775,877	**1,073,820**

The Group has assessed that there is no evidence of impairment.

(G) LIQUIDITY RISK MANAGEMENT

The Group's liquidity management framework is designed to ensure that the Group has the ability to generate sufficient cash in a timely manner to meet its financial commitments.

The Fund is long-term by nature (no capital withdrawals are permitted prior to 30 June 2020 and, on current assumptions, none are expected before 30 June 2030), and has had strong positive cashflow into the Fund to date.

Liquidity risk is managed by:

(a) forecasting liquidity requirements;

(b) requiring managers, within the terms of their individual contracts, to hold diversified portfolios;

(c) requiring managers to invest primarily in securities traded on recognised exchanges with specified maximums for unlisted securities;

(d) maintaining a buffer of cash and highly liquid securities to meet short term liquidity requirements.

Information about the contractual maturity periods of financial assets and liabilities is included at 20(e)(i),(ii),(iii), and (iv) above.

Notes to the Financial Statements (continued)

For the year ended 30 June 2010

20. FINANCIAL INSTRUMENTS (continued)

(H) FAIR VALUES

The majority of the Group's assets and liabilities are carried at fair value. For all financial assets and liabilities, carrying value is not materially different from fair value.

21. COMPARISON TO BUDGET

During the year ended 30 June 2010, market returns have generated a positive variance over the assumptions utilised in the budget.

The Group produces its budget based on long-term return expectations which is for a profit. The Group cannot forecast short-term returns, whether they be gains or losses.

Overall, with the exception of New Zealand property, all asset classes contributed positively to Group performance.

ERNST & YOUNG Chartered Accountants

AUDIT REPORT

TO THE READERS OF THE NEW ZEALAND SUPERANNUATION FUND AND GROUP'S FINANCIAL STATEMENTS FOR THE YEAR ENDED 30 JUNE 2010

The Auditor-General is the auditor of the New Zealand Superannuation Fund (the Fund) and group. The Auditor-General has appointed me, Brent Penrose, using the staff and resources of Ernst & Young, to carry out the audit of the financial statements of the Fund and group, on her behalf, for the year ended 30 June 2010.

Unqualified opinion

In our opinion the financial statements of the Fund and group on pages 59 to 105:

- comply with generally accepted accounting practice in New Zealand; and
- fairly reflect:
    - the Fund and group's financial position as at 30 June 2010; and
    - the results of operations and cash flows for the year ended on that date.

The audit was completed on 13 September 2010, and is the date at which our opinion is expressed.

The basis of our opinion is explained below. In addition, we outline the responsibilities of the Guardians of New Zealand Superannuation (the Guardians) and the Auditor, and explain our independence.

Basis of opinion

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

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

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

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

Audit procedures generally include:

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

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

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

Responsibilities of the Guardians and the Auditor

The Guardians are responsible for preparing the financial statements in accordance with generally accepted accounting practice in New Zealand. The financial statements must fairly reflect the financial position of the Fund and group as at 30 June 2010 and the operations and cash flows for the year ended on that date. The Guardians' responsibilities arise from the New Zealand Superannuation and Retirement Income Act 2001.

We are responsible for expressing an independent opinion on the financial statements and reporting that opinion to you. This responsibility arises from section 15 of the Public Audit Act 2001 and New Zealand Superannuation and Retirement Income Act 2001.

Independence

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

Other than the audit, we have no relationship with or interests in the Fund, or any of its subsidiaries.

B Penrose

BRENT PENROSE
Ernst & Young
On behalf of the Auditor-General
Auckland, New Zealand

Statement of Responsibility

The Board and management of the Guardians of New Zealand Superannuation accept responsibility for the preparation of the annual financial statements and the statement of service performance of the Guardians of New Zealand Superannuation and Group and the judgements used in them.

The Board and management of the Guardians of New Zealand Superannuation accept responsibility for establishing and maintaining a system of internal control designed to provide reasonable assurance as to the integrity and reliability of financial and non-financial reporting of the Guardians of New Zealand Superannuation and Group.

In the opinion of the Board and management of the Guardians of New Zealand Superannuation, the annual financial statements and the statement of service performance for the year ended 30 June 2010, fairly reflect the financial position, operations, and cash flows of the Guardians of New Zealand Superannuation and Group.

DAVID MAY
Chairman
13 September 2010

MARK TUME
Board Member
13 September 2010

Statement of Comprehensive Income

For the year ended 30 June 2010

		PARENT AND GROUP ACTUAL		BUDGET
		2010	2009	2010
	Note	NZ$000	NZ$000	NZ$000
Revenue	2(a)	16,500	12,148	21,839
Expenses	2(b)	16,500	12,148	21,839
Profit/(loss) for the year		-	-	-
Other comprehensive income		-	-	-
Total comprehensive income for the year		-	-	-

The attached notes form part of and should be read in conjunction with these financial statements.

Statement of Financial Position

As at 30 June 2010

	Note	PARENT AND GROUP ACTUAL 2010 NZ$000	2009 NZ$000	BUDGET 2010 NZ$000
CURRENT ASSETS				
Cash and cash equivalents	15	1,130	853	1,164
Trade and other receivables	4	141	211	1,778
Inter-entity receivables	4, 12	2,023	1,067	-
Total current assets		**3,294**	**2,131**	**2,942**
NON-CURRENT ASSETS				
Inter-entity receivables	4, 12	10	-	-
Investments in subsidiaries	11	-	-	-
Intangible assets	5	-	-	-
Property, plant, and equipment	6	2	2	-
Total non-current assets		**12**	**2**	**-**
TOTAL ASSETS		**3,306**	**2,133**	**2,942**
CURRENT LIABILITIES				
Trade and other payables	7	2,392	1,248	2,172
Total current liabilities		**2,392**	**1,248**	**2,172**
NON-CURRENT LIABILITIES				
Trade and other payables	7	10	-	-
Provisions	8	404	385	270
Total non-current liabilities		**414**	**385**	**270**
TOTAL LIABILITIES		**2,806**	**1,633**	**2,442**
NET ASSETS		**500**	**500**	**500**
PUBLIC EQUITY				
Retained surplus		-	-	-
General equity reserve	9	500	500	500
TOTAL PUBLIC EQUITY		**500**	**500**	**500**

The attached notes form part of and should be read in conjunction with these financial statements.

Statement of Changes in Public Equity

For the year ended 30 June 2010

	PARENT AND GROUP ACTUAL		
	GENERAL EQUITY RESERVE NZ$000	RETAINED SURPLUS NZ$000	TOTAL NZ$000
BALANCE AT 1 JULY 2008	500	-	500
Profit/(Loss) for the year	-	-	-
Total recognised income and expense for the year	-	-	-
BALANCE AT 30 JUNE 2009	**500**	**-**	**500**
Profit/(Loss) for the year	-	-	-
Total recognised income and expense for the year	-	-	-
BALANCE AT 30 JUNE 2010	**500**	**-**	**500**

The attached notes form part of and should be read in conjunction with these financial statements.

Statement of Cash Flows

For the year ended 30 June 2010

	Note	PARENT AND GROUP ACTUAL 2010 NZ$000	2009 NZ$000	BUDGET 2010 NZ$000
CASH FLOWS FROM OPERATING ACTIVITIES				
Cash was provided from:				
Receipts from the Crown		261	637	504
Receipts from New Zealand Superannuation Fund		15,066	12,433	21,174
Interest received		53	89	41
Other receipts		128	10	-
Goods and Services Tax		22	(67)	718
Total cash inflow from operating activities		**15,530**	**13,102**	**22,437**
Cash was applied to:				
Payments to suppliers		(4,139)	(4,687)	(8,236)
Payments to employees		(11,114)	(8,871)	(14,053)
Total cash outflow from operating activities		**(15,253)**	**(13,558)**	**(22,289)**
NET CASH PROVIDED BY/(USED IN) OPERATING ACTIVITIES	15	**277**	**(456)**	**148**
NET CASH PROVIDED BY INVESTING ACTIVITIES		**-**	**-**	**-**
NET CASH PROVIDED BY FINANCING ACTIVITIES		**-**	**-**	**-**
NET INCREASE/(DECREASE) IN CASH AND CASH EQUIVALENTS		**277**	**(456)**	**148**
Cash and cash equivalents at the beginning of the financial year		853	1,309	1,016
CASH AND CASH EQUIVALENTS AT THE END OF THE FINANCIAL YEAR	15	**1,130**	**853**	**1,164**

The attached notes form part of and should be read in conjunction with these financial statements.

Statement of Commitments

As at 30 June 2010

	PARENT AND GROUP ACTUAL 2010 NZ$000	2009 NZ$000
NON-CANCELLABLE OPERATING LEASE COMMITMENTS PAYABLE		
Payable no later than 1 year	387	380
1-2 years	387	357
2-5 years	291	624
	1,065	**1,361**

Statement of Contingent Liabilities

As at 30 June 2010

There were no contingent liabilities as at 30 June 2010 (2009:nil).

Notes to the Financial Statements

For the year ended 30 June 2010

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

GENERAL INFORMATION

These are the financial statements of Guardians of New Zealand Superannuation (Guardians), a Crown entity in terms of the Crown Entities Act 2004.

The Guardians are domiciled in New Zealand and the address of their principal place of business is set out in the Corporate Directory on page 142.

STATEMENT OF COMPLIANCE

The Guardians are a public benefit entity, as the primary purpose is to manage and administer the New Zealand Superannuation Fund (Fund). The financial statements have been prepared in accordance with Generally Accepted Accounting Practice in New Zealand (NZ GAAP). They comply with the New Zealand Equivalents to International Financial Reporting Standards (NZ IFRS) and other applicable financial reporting standards as appropriate for public benefit entities.

The financial statements of the Guardians of New Zealand Superannuation and Subsidiaries (Group) for the year ended 30 June 2010 were authorised for issue in accordance with a resolution of the Board of Guardians of New Zealand Superannuation on 13 September 2010.

BASIS OF PREPARATION

The financial statements have been prepared in accordance with the Crown Entities Act 2004 and the Public Finance Act 1989.

The financial statements have been prepared on a historical cost basis and are presented in New Zealand dollars and all values are rounded to the nearest thousand dollars (NZ$000).

Accounting policies are selected and applied in a manner which ensures that the resulting financial information satisfies the concepts of relevance and reliability, thereby ensuring that the substance of the underlying transactions or other events is reported.

Standards and interpretations that have recently been issued or amended but are not yet effective have not been adopted for the annual reporting period ending 30 June 2010. These are outlined in the table below:

REFERENCE	TITLE	SUMMARY	APPLICATION DATE OF STANDARD*	IMPACT ON FINANCIAL STATEMENTS	APPLICATION DATE FOR GROUP*
NZ IAS 24	Related Party Disclosures (Revised 2009)	This Standard makes amendments to New Zealand Accounting Standard NZ IAS 24 Related Party Disclosures. The amendments simplify the definition of a related party and provide a partial exemption from the disclosure requirements for government-related entities.	1 January 2011	Reduced disclosure requirements for related party transactions.	1 July 2011

* Designates the beginning of the applicable annual reporting period.

All accounting policies have been consistently applied by the Group with those of the previous financial year except as follows:

The Group has adopted the following amendment as of 1 July 2009:

NZ IAS 1 (Revised 2007) Presentation of Financial Statements

The International Accounting Standards Board (IASB) issued a revised version of IAS 1 Presentation of Financial Statements (IAS 1R), which is effective for periods beginning on or after 1 January 2009. The revised standard is intended to improve the users' ability to analyse and compare the information given in the consolidated financial statements. The Board have determined that this does not have any material financial impact on the consolidated financial statements of the Group. However, adoption of IAS 1R impacts the presentation of the consolidated financial statements of the Group. As permitted under IAS 1R, the Board have chosen to present one single statement of comprehensive income.

Notes to the Financial Statements (continued)

For the year ended 30 June 2010

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

The following particular accounting policies which materially affect the measurement of comprehensive income and financial position have been applied:

(a) Budget figures

The budget was approved by the Board of Guardians of New Zealand Superannuation for the year. The budget figures are unaudited.

(b) Consolidation of subsidiaries

The Group financial statements comprise the Guardians of New Zealand Superannuation and their subsidiaries.

Subsidiaries are those entities that are controlled by the Guardians. The financial statements of subsidiaries are prepared for the same reporting period as the parent entity, using consistent accounting policies.

Adjustments are made to bring into line any dissimilar accounting policies that may exist.

The Group financial statements incorporate the financial statements of the Guardians and their subsidiaries, which have been consolidated using the purchase method. The results of any subsidiaries that become or cease to be part of the Group during the year are consolidated from the date that control commenced or until the date that control ceased.

All inter-entity transactions, balances and unrealised profits are eliminated on consolidation.

(c) Revenue and income

The Group primarily derives revenue through the provision of outputs to the Crown and to the Fund, and also derives income from its investments. Revenue and income is recognised to the extent that it is probable that the economic benefits will flow to the Group and the revenue can be reliably measured. The following specific recognition criteria must also be met before revenue is recognised:

Rendering of services

Revenue from the rendering of services is recognised by reference to the stage of completion.

New Zealand Superannuation Fund reimbursement of costs:
Stage of completion is measured by the proportion of costs incurred to date, compared to the total costs of the outputs.

Crown appropriations:
Revenue is recognised on a straight line basis over the period the appropriations relate to, because the services are performed by an indeterminate number of acts over a specified period of time.

Other service revenue:
Where outputs cannot be measured reliably, revenue is recognised only to the extent that the expenses recognised are recoverable.

Interest

Interest revenue is recognised as the interest accrues (using the effective interest method which is the rate that exactly discounts estimated future cash receipts through the expected life of the financial instrument to the net carrying amount of the financial asset).

(d) Goods and Services Tax (GST)

Revenues, expenses, assets, and liabilities are recognised exclusive of GST, with the exception of receivables and payables which are stated with GST included. Where GST is irrecoverable as an input tax, then it is recognised as part of the related asset or expense.

Cash flows are included in the cash flow statement on a gross basis. The GST component of cash flows arising from investing and financing activities which is recoverable from, or payable to, the taxation authority is classified as operating cash flows.

(e) Taxation

The Guardians are exempt from income tax under the Income Tax Act 2007.

Notes to the Financial Statements (continued)

For the year ended 30 June 2010

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

(f) Receivables

Short-term receivables are stated at their estimated realisable value after providing for doubtful and uncollectible debts.

Collectability of receivables is reviewed on an ongoing basis. Individual debts that are known to be uncollectible are written off when identified. An impairment provision is recognised when there is objective evidence that the Group will not be able to collect the receivable. Financial difficulties of the debtor, default payments or debts more than 60 days overdue are considered objective evidence of impairment. The amount of the impairment loss is the receivable carrying amount compared to the present value of estimated future cash flows, discounted at the original effective interest rate.

(g) Subsidiaries

Subsequent to initial recognition, investments in subsidiaries are measured at cost.

(h) Property, plant, and equipment

Initial recording

All items of property, plant, and equipment are initially recognised at cost. Cost includes the value of consideration exchanged, or fair value in the case of donated or subsidised assets, and those costs directly attributable to bringing the item to working condition for its intended use.

Subsequent expenditure

Subsequent expenditure relating to an item of property, plant, and equipment is capitalised to the initial cost of the item when the expenditure increases the economic benefits over the life of the item or where that expenditure was necessarily incurred to enable the future economic benefits to be obtained and the expenditure would have been included in the initial cost of the item had the expenditure been incurred at the time of acquisition.

All other subsequent expenditure is expensed in the period in which it is incurred.

Subsequent measurement

Subsequent to initial recognition, property, plant, and equipment is stated at cost less accumulated depreciation and any impairment in value.

Disposal

An item of property, plant, and equipment is derecognised upon disposal or when no future economic benefits are expected to arise from the continued use of the asset.

Any gain or loss arising on disposal of the asset (calculated as the difference between the net disposal proceeds and the carrying amount of an item) is included in the statement of comprehensive income in the year the item is disposed of.

Impairment

All items of property, plant, and equipment are assessed for indications of impairment at each balance date.

Where the carrying amount is assessed to be greater than its recoverable amount, the item is written down to its recoverable amount. The write down is recognised in the statement of comprehensive income.

Where an impairment loss subsequently reverses, the carrying amount of the item is increased to the revised estimate of its recoverable amount, but only to the extent that the increased carrying amount does not exceed the carrying amount that would have been determined had no impairment loss been recognised for the item in prior years. A reversal of an impairment loss is recognised in the statement of comprehensive income immediately.

Recoverable amount is the greater of fair value less costs to sell and value in use. The recoverable amount is determined for an individual asset, unless the asset's value in use cannot be estimated to be close to its fair value less costs to sell and it does not generate cash inflows that are largely independent of those from other assets or groups of assets, in which case, the recoverable amount is determined for the cash generating unit to which the asset belongs.

In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset.

Held for sale

Items of property, plant, and equipment classified as held for sale are measured at the lower of carrying amount and fair value less costs to sell.

Items of property, plant, and equipment are classified as 'held for sale' if their carrying amount will be recovered through a sale transaction rather than through continuing use. This condition is regarded as met only when the sale is highly probable and the asset is available for immediate sale in its present condition. The sale of the asset is expected to be completed within one year from the date of classification.

Notes to the Financial Statements (continued)

For the year ended 30 June 2010

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

(i) Depreciation

Depreciation is provided on a straight line basis on all property, plant, and equipment at a rate which will write off the cost of the assets to their estimated residual value over their useful lives.

The useful lives and associated depreciation rates of major classes of assets have been estimated as follows:

Office equipment	3 years
Computer equipment	1 – 3 years

(j) Intangible assets

Software and licences are finite life intangibles and are recorded at cost less accumulated amortisation and impairment. Amortisation is charged on a straight line basis over their estimated useful lives of 3 years. The estimated useful life and amortisation method is reviewed at the end of each annual reporting period.

(k) Employee benefits

Provision is made for benefits accruing to employees in respect of wages and salaries, annual leave, long service leave, long-term incentives, and sick leave when it is probable that settlement will be required and they are capable of being measured reliably.

Provisions made in respect of employee benefits expected to be settled within 12 months, are measured at their nominal values using the remuneration rate expected to apply at the time of settlement.

Provisions made in respect of employee benefits which are not expected to be settled within 12 months are measured as the present value of the estimated future cash outflows to be made by the Group in respect of services provided by employees up to reporting date.

(l) Operating leases

The determination of whether an arrangement is, or contains, a lease is based on the substance of the arrangement and requires an assessment of whether the fulfilment of the arrangement is dependent on the use of a specific asset or assets and the arrangement conveys a right to use the asset.

Leases where the lessor effectively retains substantially all the risks and benefits of ownership of the leased items are classified as operating leases. Operating lease expenses are recognised on a straight-line basis over the period of the lease.

In the event that lease incentives are received to enter into operating leases, such incentives are recognised as deferred income in the statement of financial position. The aggregate benefits of incentives are recognised as a reduction of rental expense on a straight-line basis over the period of the lease.

(m) Foreign currency transactions

Transactions denominated in a foreign currency are converted to New Zealand dollars at the exchange rate in effect at the date of the transaction.

Monetary assets and liabilities denominated in foreign currency at balance date are translated at the rate of exchange ruling as at that date. The resulting exchange differences are recognised in the statement of comprehensive income. Foreign exchange gains and losses for fair value through profit or loss investments are included within the change in their fair value.

(n) Financial instruments

The Group is party to financial instruments as part of its normal operations. These financial instruments include cash and cash equivalents, receivables, and payables. All financial instruments are recognised in the statement of financial position and all revenues and expenses in relation to financial instruments are recognised in the statement of comprehensive income.

Financial assets and financial liabilities are recognised in the statement of financial position when the Group becomes a party to the contractual provisions of the instrument. The Group offsets financial assets and financial liabilities when the Group has a legally enforceable right to set off the recognised amounts and interests and intends to settle on a net basis.

Except for items covered by a separate accounting policy, all financial instruments are shown at their amortised cost.

Notes to the Financial Statements (continued)

For the year ended 30 June 2010

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

(o) Provisions

Provisions are recognised when the Group has a present obligation as a result of a past event, the future sacrifice of economic benefits is probable, and the amount of the provision can be measured reliably.

The amount recognised as a provision is the best estimate of the consideration required to settle the present obligation at the reporting date, taking into account the risks and uncertainties surrounding the obligation. Where a provision is measured using the cash flows estimated to settle the present obligation, its carrying amount is the present value of those cash flows.

When some or all of the economic benefits required to settle a provision are expected to be recovered from a third party, the receivable is recognised as an asset if it is virtually certain that recovery will be received and the amount of the receivable can be measured reliably.

(p) Payables

Short-term payables are not interest bearing and are stated at their nominal value.

(q) Equity

Equity is the Crown's interest in the Guardians and is measured as the difference between total assets and total liabilities.

(r) Statement of cash flows

The following are the definitions of the terms used in the statement of cash flows:

Operating activities include all activities other than investing and financing activities. The cash inflows include all receipts from the sale of goods and services, interest, and other sources of revenue that support the Group's operating activities. Cash outflows include payments made to employees, suppliers and for taxes.

Investing activities are those activities relating to the acquisition, holding, and disposal of current and non-current securities and any other non-current assets.

Financing activities are those activities relating to changes in equity and debt capital structure of the Group and those activities relating to the cost of servicing the Group's equity capital.

Cash and cash equivalents includes cash balances on hand, held in bank accounts, demand deposits, and other highly liquid investments with an original maturity of three months or less.

(s) Changes in accounting policies

There have been no changes in accounting policies. All policies are consistent with prior year.

(t) Critical accounting estimates and assumptions

In preparing these financial statements the Group has made estimates and assumptions concerning the future. These estimates and assumptions may differ from the subsequent actual results. Estimates and assumptions are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances. The estimates and assumptions that have a significant risk of causing a material adjustment to the carrying amount of assets and liabilities within the next financial year are discussed below:

Employee entitlements – long-term incentive

A component of the long-term incentive scheme is a measure of the performance of the Fund, calculated based on a rolling four-year performance average. The calculation of this liability utilises assumptions regarding the future performance of the Fund, the employee's average salary over the vesting period, and the percentage of service rendered. The key variable is the performance of the Fund. Should the performance of the Fund differ from the assumption utilised in the calculation of the long-term incentive liability, this will impact the employee benefits expense in the statement of comprehensive income, and the carrying amount of the liability in the statement of financial position. The Group minimises the risk of this estimation uncertainty by using a model based on historical evidence to forecast future returns of the Fund.

Notes to the Financial Statements (continued)

For the year ended 30 June 2010

	PARENT AND GROUP ACTUAL 2010 NZ$000	2009 NZ$000
2. PROFIT/(LOSS) FROM OPERATIONS		
(A) REVENUE		
Revenue from operations consisted of the following items:		
Revenue from the Crown	354	384
Cost reimbursement from New Zealand Superannuation Fund	15,973	11,635
Other revenue	120	40
Interest revenue	53	89
	16,500	**12,148**
(B) EXPENSES		
Profit/(Loss) has been arrived at after charging for (crediting):		
Depreciation and amortisation of non-current assets (note 5 and note 6)	-	59
Auditors' remuneration (note 3)	37	39
Finance charge – provision discount adjustment	19	18
Board members' fees (note 12)	206	216
Employee benefit expense*:		
Long-term employee benefits	1,330	(1,188)
Employer contributions to Kiwisaver	158	60
Other employee remuneration and related expenses	11,493	9,916
Operating lease rental expenses:		
Minimum lease payments	411	402
Professional fees	48	222
Other expenses	2,798	2,404
	16,500	**12,148**

* Compensation of key management personnel of the entity is specifically disclosed in the related party note 12.

	2010 NZ$000	2009 NZ$000
3. REMUNERATION OF AUDITORS		
Auditor of the parent entity		
Audit of the financial statements – Attest current year	37	37
Audit of the financial statements – Attest prior year	-	2
	37	39
Auditor of entities in the Group (not including the parent entity)		
Audit of the financial statements	-	-
	-	**-**

The audit fees of other entities in the Group are paid by the Fund.

The auditor of all entities in the Group is Brent Penrose of Ernst & Young, on behalf of the Auditor-General.

In the prior year the auditor of the parent entity was Francis Caetano of Audit New Zealand, on behalf of the Auditor-General.

Notes to the Financial Statements (continued)

For the year ended 30 June 2010

	PARENT AND GROUP ACTUAL 2010 NZ$000	2009 NZ$000
4. TRADE AND OTHER RECEIVABLES		
Current receivables		
Trade receivables	2	2
Goods and Services Tax (GST) receivable	56	78
Prepayments	83	131
Allowance for doubtful debts	-	-
	141	**211**
Inter-entity receivables:		
Accident Compensation Corporation	11	15
Government Superannuation Fund Authority	11	15
The Treasury	67	-
New Zealand Superannuation Fund	1,934	1,037
	2,023	**1,067**
Non-current receivables		
Inter-entity receivables:		
New Zealand Superannuation Fund	10	-
	10	**-**

Trade receivables have standard 30-day credit terms.

Inter-entity receivables classified as current consist of amounts payable by the Fund or other Crown Entities to the Guardians on standard 30-day credit terms.

The Group does not have a history of default on receivables. Accordingly, no allowance has been made for doubtful debts.

	PARENT AND GROUP ACTUAL 2010 NZ$000	2009 NZ$000
5. INTANGIBLE ASSETS		
Gross carrying amount		
Opening balance	63	63
Disposals	(42)	-
Closing balance	**21**	**63**
Accumulated amortisation		
Opening balance	63	52
Amortisation expense	-	11
Accumulated amortisation reversed on disposals	(42)	-
Closing balance	**21**	**63**
Net book value	**-**	**-**

Intangible assets are software licences and applications used by the Group in day-to-day operations.

Notes to the Financial Statements (continued)

For the year ended 30 June 2010

	PARENT AND GROUP ACTUAL		
	OFFICE EQUIPMENT NZ$000	COMPUTER EQUIPMENT NZ$000	TOTAL NZ$000
6. PROPERTY, PLANT, AND EQUIPMENT			
Gross carrying amount			
Balance at 1 July 2008	247	244	491
Additions	-	-	-
Disposals	-	-	-
Balance at 30 June 2009	**247**	**244**	**491**
Additions	-	-	-
Disposals	(1)	(186)	(187)
Balance at 30 June 2010	**246**	**58**	**304**
Accumulated depreciation			
Balance at 1 July 2008	226	215	441
Depreciation expense	19	29	48
Balance at 30 June 2009	**245**	**244**	**489**
Depreciation expense	-	-	-
Accumulated depreciation reversed on disposals	(1)	(186)	(187)
Balance at 30 June 2010	**244**	**58**	**302**
Net book value			
As at 30 June 2009	2	-	2
As at 30 June 2010	**2**	**-**	**2**

Notes to the Financial Statements (continued)

For the year ended 30 June 2010

	PARENT AND GROUP ACTUAL 2010 NZ$000	2009 NZ$000
7. TRADE AND OTHER PAYABLES		
Current payables and accruals		
Trade payables [i]	209	295
Employee entitlements – annual leave (key management personnel)	130	108
Employee entitlements – annual leave (other)	391	279
Employee entitlements – accrued salary (key management personnel)	26	20
Employee entitlements – accrued salary (other)	101	55
Employee entitlements – long-term incentives (key management personnel) [ii]	328	-
Employee entitlements – long-term incentives (other) [ii]	1,022	383
Accrued expenses	185	108
	2,392	**1,248**
Non-current payables and accruals		
Employee entitlements – long-term incentives (key management personnel) [ii]	2	-
Employee entitlements – long-term incentives (other) [ii]	8	-
	10	**-**

[i] The average credit period on purchases is 30 days. No interest is charged on overdue balances. The Group has financial risk management policies in place to ensure that all payables are paid within the credit time frame.

[ii] The Guardians have a long-term incentive scheme for all employees. A component of the scheme is a measure of the performance of the Fund, calculated based on a rolling four-year performance average. The incentive vests progressively over the four-year performance period. Since payments in relation to the Fund performance component of the scheme are based on four-year averages, any negative returns generated during the four year period are offset against positive returns. As such, during the first three years of the four-year calculation period, the value of the accrual is dependent on the outcome of future periods. The liability reflected in the statement of financial position reflects the present value of the Guardians obligations in respect of that liability. The liability has been calculated based on management's best estimate of the returns that will be achieved by the Fund in future years.

	2010 NZ$000	2009 NZ$000
8. PROVISIONS		
Non-current provisions		
Provision for refurbishment	404	385
	404	**385**

	PARENT AND GROUP REFURBISHMENT
Balance at 1 July 2009	385
Unwinding and discount rate adjustment	19
Balance at 30 June 2010	**404**

The provision for refurbishment represents the present value of management's best estimate of the future sacrifice of economic benefits that will be required under the Group's programme for restoring premises to the condition required under the lease agreement. The estimate has been made on the basis of advice received from a Quantity Surveyor and may vary as a result of changes in the price of building materials.

Notes to the Financial Statements (continued)

For the year ended 30 June 2010

9. MANAGEMENT OF CAPITAL

As a public benefit entity which is fully funded by Crown appropriations (for budgeted Board and audit costs) and by Fund reimbursements (for all other operating costs), the Group has no specific liquidity policies, procedures, or targets. Operating budgets are set on an annual basis, with an emphasis upon cost control. The Group is not permitted to borrow, and ensures a positive cash position at all times through collection of appropriations and reimbursements.

10. LEASES

Operating leases

Non-cancellable operating lease commitments payable have been disclosed under the statement of commitments.

Operating leases relate to office premises in one location. The lease has a remaining term of 3 years with an option to extend for a further 6 years. The operating lease contract contains a market review clause in the event that the Group exercises its option to renew. The Group does not have an option to purchase the leased assets at the expiry of the lease period.

11. SUBSIDIARIES

NAME OF ENTITY	BALANCE DATE	COUNTRY OF INCORPORATION	OWNERSHIP INTEREST AND VOTING RIGHTS 2010 %	2009 %
Subsidiaries				
New Zealand Superannuation Fund Nominees Limited	30 June	New Zealand	100	100
NZSF Timber Investments (No 1) Limited	30 June	New Zealand	100	100
NZSF Timber Investments (No 2) Limited	30 June	New Zealand	100	100
NZSF Timber Investments (No 3) Limited	30 June	New Zealand	100	100
NZSF Timber Investments (No 4) Limited	30 June	New Zealand	100	100
NZSF Private Equity Investments (No 1) Limited	30 June	New Zealand	100	100
CNI Timber Operating Company Limited	30 June	New Zealand	100	100

The principal activity of each subsidiary (with the exception of CNI Timber Operating Company Limited) is to act as a nominee company holding assets and liabilities on behalf of the New Zealand Superannuation Fund. These assets and liabilities are recognised in the financial statements of the New Zealand Superannuation Fund, and accordingly are not presented in these financial statements.

The share in CNI Timber Operating Company Limited, together with the rights and benefits arising from that share, is held for and on behalf of the New Zealand Superannuation Fund. As such, this company is consolidated into the financial statements of the Fund rather than these financial statements.

12. RELATED PARTY DISCLOSURES

(A) PARENT ENTITIES

The parent entity in the Group is the Guardians, which is 100% owned by the ultimate parent entity, the Crown.

(B) EQUITY INTERESTS IN RELATED PARTIES

Equity interests in subsidiaries

Details of the percentage of ordinary shares held in subsidiaries are disclosed in note 11 to the financial statements.

(C) TRANSACTIONS WITH RELATED PARTIES

Revenue

The Guardians are a wholly owned entity of the Crown, and have paid expenses relating to the Fund during the year, as they are required to do under the Act. Crown appropriations (for budgeted Board and audit costs) and reimbursement of costs from the Fund are the main sources of revenue. Other revenue is gained from sharing outputs with other Crown Entities.

Notes to the Financial Statements (continued)

For the year ended 30 June 2010

12. RELATED PARTY DISCLOSURES (continued)

(C) TRANSACTIONS WITH RELATED PARTIES (continued)

	PARENT AND GROUP ACTUAL	
	2010 NZ$000	2009 NZ$000
Appropriations from the Crown	354	384
Cost reimbursement from New Zealand Superannuation Fund	15,973	11,635
Other income from Crown Entities:		
Accident Compensation Corporation	40	14
Government Superannuation Fund Authority	40	13
Earthquake Commission	40	13
	16,447	**12,059**

Amounts receivable from or payable to related parties at balance date are disclosed in notes 4 and 7 of these financial statements.

The Group has entered into a number of transactions with other government entities on an arms length basis. Where those parties are acting in the course of their normal dealings with the Guardians, related party disclosures have not been made for transactions of this nature.

Employee benefits

The compensation of the Board, executives, and other key management personnel, is set out below:

Short-term employee benefits (including board member fees)	2,821	2,889
Long-term employee benefits	328	-
	3,149	**2,889**

Board members' fees

Board members earned the following fees during the year:

D May (Chairman)	54	54
Sir D Graham*	-	30
B Liddell**	25	27
D Newman (Deputy Chaiman)***	31	27
G Saunders****	6	24
M Tume	27	27
J Evans	27	27
C Savage*****	18	-
S Moir*****	18	-
	206	**216**

* Sir Douglas Graham retired from the Board in June 2009
** Bridget Liddell retired from the Board in May 2010
*** David Newman was appointed Deputy Chairman in November 2009
**** Glen Saunders retired from the Board in September 2009
***** Catherine Savage and Stephen Moir were appointed to the Board in November 2009

Board fees are paid inclusive of GST. Where a Board member is registered for GST their fees detailed above are recorded exclusive of GST. Board members' travel expenses to attend meetings are also paid by the Guardians.

Board members' indemnity and insurance

The Guardians have indemnified Board members in respect of a liability incurred where that Board member has breached one of the individual duties set out in Sections 53 to 57 of the Crown Entities Act 2004 (subject to certain limitations). Liability in respect of a breach of these duties is excluded from the scope of the statutory immunity provided in Section 121 of the Crown Entities Act 2004. Each Board member is also indemnified in respect of costs incurred by that Board member in defending or settling any claim or proceeding.

The Guardians have effected Directors and Officers Liability insurance cover in respect of the liability or costs of Board members and employees.

Notes to the Financial Statements (continued)

For the year ended 30 June 2010

12. RELATED PARTY DISCLOSURES (continued)

(C) TRANSACTIONS WITH RELATED PARTIES (continued)

Terms/price under which related party transactions were entered into

All balances advanced to and payable to related parties are unsecured and subordinate to other liabilities. Interest is not charged on outstanding balances.

There have been no write-downs of receivables in respect of transactions with related parties. No amounts were provided for doubtful debts relating to debts due from related parties at reporting date (2009: $nil).

The terms and conditions around settlement of related party balances are set out in note 4 and note 7.

13. EMPLOYEES' REMUNERATION OVER $100,000 PER ANNUM

TOTAL REMUNERATION AND BENEFITS

REMUNERATION RANGE NZ$000			PARENT AND GROUP ACTUAL NUMBER OF EMPLOYEES 2010	2009
100	-	110	3	2
110	-	120	3	4
120	-	130	1	2
130	-	140	3	2
140	-	150	3	3
150	-	160	2	2
160	-	170	3	1
170	-	180	3	2
180	-	190	2	1
190	-	200	1	2
200	-	210	1	3
210	-	220	6	1
220	-	230	1	3
230	-	240	2	3
250	-	260	3	3
260	-	270	3	2
270	-	280	1	-
280	-	290	1	1
290	-	300	4	1
300	-	310	2	-
320	-	330	-	1
330	-	340	2	-
340	-	350	1	-
350	-	360	-	1
380	-	390	-	2
390	-	400	1	-
430	-	440	-	1
450	-	460	2	-
480	-	490	1	-

The total remuneration figures in this table consist of both an employee's gross base salary and the proportion of the long-term incentive entitlement that will be paid out after this financial year end.

The total remuneration bands and benefits listed above are annual amounts. As some employees commenced part way through the year, the actual remuneration they received during the year is less than the amount shown. For employees who left during the year, the actual remuneration paid has been reported, rather than annual remuneration.

The bonus entitlement is a long-term incentive scheme that has both organisation and financial performance targets of the Fund. The financial performance component is based on rolling four-year periods of returns against thresholds and benchmarks. If both the organisation and financial performance targets are achieved over a rolling four-year period, a maximum of 30% of an employee's salary can be paid in bonus.

Notes to the Financial Statements (continued)

For the year ended 30 June 2010

14. SUBSEQUENT EVENTS

There were no reportable events subsequent to year end (2009:nil).

15. NOTES TO THE STATEMENT OF CASH FLOWS

(A) RECONCILIATION OF CASH AND CASH EQUIVALENTS

For the purposes of the statement of cash flows, cash and cash equivalents includes cash on hand and in banks and investments in money market instruments. Cash and cash equivalents at the end of the financial year as shown in the statement of cash flows is reconciled to the related items in the statement of financial position as follows:

	PARENT AND GROUP ACTUAL	
	2010	2009
	NZ$000	NZ$000
Cash and cash equivalents	**1,130**	**853**
(B) RECONCILIATION OF PROFIT/(LOSS) FOR THE YEAR TO NET CASH FLOWS FROM OPERATING ACTIVITIES		
Profit/(loss) for the year	-	-
Add/(deduct) non-cash items:		
Depreciation and amortisation of non-current assets	-	59
Changes in working capital:		
(Increase)/decrease in assets:		
Receivables	(896)	821
Increase/(decrease) in liabilities:		
Payables and accruals	1,154	(1,625)
Provisions	19	289
Net cash provided by/(used in) operating activities	**277**	**(456)**

Notes to the Financial Statements (continued)

For the year ended 30 June 2010

16. FINANCIAL INSTRUMENTS

(A) FINANCIAL ASSETS AND FINANCIAL LIABILITIES BY MEASUREMENT BASIS

Key:

L&R: Loans and receivables

AC: Amortised cost or cost

	L&R NZ$000	AC NZ$000	TOTAL NZ$000
2010			
Financial assets			
Cash and cash equivalents	-	1,130	1,130
Receivables	2	-	2
Inter-entity receivables	2,033	-	2,033
Total financial assets	**2,035**	**1,130**	**3,165**
Financial liabilities			
Payables and accruals	-	2,402	2,402
Total financial liabilities	**-**	**2,402**	**2,402**
2009			
Financial assets			
Cash and cash equivalents	-	853	853
Receivables	2	-	2
Inter-entity receivables	1,067	-	1,067
Total financial assets	**1,069**	**853**	**1,922**
Financial liabilities			
Payables and accruals	-	1,248	1,248
Total financial liabilities	**-**	**1,248**	**1,248**

(B) FINANCIAL RISK MANAGEMENT OBJECTIVES

Through their activities, the Guardians are exposed to the financial risks of market risk, credit risk, and liquidity risk.

The Guardians are risk averse. They do not hold significant financial assets or liabilities. Cash and cash equivalents are held with creditworthy institutions. Market risk, credit risk and liquidity risk are not considered significant for these reasons. Policies do not allow any transactions which are speculative in nature to be entered into.

(C) SIGNIFICANT ACCOUNTING POLICIES

Details of the significant accounting policies and methods adopted, including the criteria for recognition, and the basis of measurement applied in respect of each class of financial asset, financial liability, and equity instrument are disclosed in note 1 to the financial statements.

Notes to the Financial Statements (continued)

For the year ended 30 June 2010

16. FINANCIAL INSTRUMENTS (continued)

(D) MARKET RISK

The market risk that the Guardians are primarily exposed to is interest rate risk (primarily to changes in New Zealand interest rates).

The Guardians do not hold significant interest-bearing assets, and have no interest-bearing liabilities. The Guardians invest cash and cash equivalents with the The National Bank of New Zealand, ensuring a fair market return on any cash position, but do not seek to speculate on interest returns, and do not specifically monitor exposure to interest rates or interest rate returns.

Interest rate risk

Interest rate risk is the risk that the value of the Guardians' investments in cash and cash equivalents will fluctuate due to changes in market interest rates. There are no interest rate options or interest rate swap options in place as at 30 June 2010 (30 June 2009: $nil). The Board does not consider that there is any significant interest exposure on the Group's investments.

Interest rate exposure – maturity profile of financial instruments

The following tables are based on the earlier of contractual repricing or maturity period.

	PARENT AND GROUP ACTUAL	
	WEIGHTED AVERAGE EFFECTIVE INTEREST RATE	CASH AT VARIABLE INTEREST RATE
	%	NZ$000
2010		
Financial assets		
Cash and cash equivalents	2.38	1,130
	2.38	1,130
2009		
Financial assets		
Cash and cash equivalents	5.88	853
	5.88	853

Interest rate sensitivity

The sensitivity analysis in the table below of the effect on net surplus has been determined based on the exposure to interest rates at the reporting date and the stipulated change taking place at the beginning of the financial year and held constant throughout the reporting period. A 100 basis point change is used when reporting interest rate risk internally to key management personnel and represents the Guardians' assessment of a reasonably possible change in interest rates.

		PROFIT/(LOSS)	
		2010	2009
	BASIS POINTS	NZ$000	NZ$000
Cash and cash equivalents	+ 100 bps	11	9
Cash and cash equivalents	- 100 bps	(11)	(9)

The Guardians' sensitivity to interest rate changes has not changed significantly from the prior year.

Notes to the Financial Statements (continued)

For the year ended 30 June 2010

16. FINANCIAL INSTRUMENTS (continued)

(E) CREDIT RISK MANAGEMENT

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

The Group places its investments with institutions that have a high credit rating. The Group believes that this policy reduces the risk of any loss which could arise from its investment activities. The Group does not require any collateral or security to support financial instruments.

Significant concentrations of credit risk

The Group primarily invests cash balances with The National Bank of New Zealand, which is considered to be a low credit risk institution. The maximum amount of credit risk for each class is the carrying amount in the statement of financial position.

(F) LIQUIDITY RISK MANAGEMENT

Liquidity management is designed to ensure that the Group has the ability to generate sufficient cash in a timely manner to meet its financial commitments.

Because the Guardians recover all expenditure from the Crown or the New Zealand Superannuation Fund, and as the Guardians have a positive cash position, no specific liquidity policies have been developed.

Information about the contractual maturity periods of financial assets and financial liabilities is included above.

(G) FAIR VALUES

The fair value of financial instruments is equivalent to the carrying amount disclosed in the statement of financial position.

17. COMPARISON TO BUDGET

	ACTUAL 2010 NZ$000	BUDGET 2010 NZ$000	FAVOURABLE/ (UNFAVOURABLE) VARIANCE 2010 NZ$000
Statement of Comprehensive Income – expenses [(i)]	16,500	21,839	5,339
Statement of Changes in Public Equity	500	500	-
Statement of Financial Position	500	500	-
Statement of Cash Flows – cash and cash equivalents	1,130	1,164	(34)

[(i)] Expenses were lower than budget predominantly due to recruitment of additional staff taking longer than was assumed in the budget.

ERNST & YOUNG

Chartered Accountants

AUDIT REPORT

TO THE READERS OF THE GUARDIANS OF NEW ZEALAND SUPERANNUATION AND GROUP'S FINANCIAL STATEMENTS AND STATEMENT OF SERVICE PERFORMANCE FOR THE YEAR ENDED 30 JUNE 2010

The Auditor-General is the auditor of the Guardians of New Zealand Superannuation (the Guardians) and group. The Auditor-General has appointed me, Brent Penrose, using the staff and resources of Ernst & Young, to carry out the audit on her behalf. The audit covers the financial statements and statement of service performance included in the annual report of the Guardians and group for the year ended 30 June 2010.

Unqualified opinion

In our opinion:

- The financial statements of the Guardians and group on pages 109 to 129:
  - comply with generally accepted accounting practice in New Zealand; and
  - fairly reflect:
    - the Guardians and group's financial position as at 30 June 2010; and
    - the results of operations and cash flows for the year ended on that date.
- The statement of service performance of the Guardians and group on pages 38 to 39:
  - complies with generally accepted accounting practice in New Zealand; and
  - fairly reflects for each class of outputs:
    - standards of delivery performance achieved, as compared with the forecast standards outlined in the statement of forecast service performance adopted at the start of the financial year; and
    - actual revenue earned and output expenses incurred, as compared with the forecast revenues and output expenses outlined in the statement of forecast service performance adopted at the start of the financial year.

The audit was completed on 13 September 2010, and is the date at which our opinion is expressed.

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

Basis of opinion

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

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

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

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

Audit procedures generally include:

- determining whether significant financial and management controls are working and can be relied on to produce complete and accurate data;
- verifying samples of transactions and account balances;
- performing analyses to identify anomalies in the reported data;
- reviewing significant estimates and judgements made by the Board;

- confirming year-end balances;
- determining whether accounting policies are appropriate and consistently applied; and
- determining whether all financial statement and statement of service performance disclosures are adequate.

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

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

Responsibilities of the Board and the Auditor

The board is responsible for preparing the financial statements and statement of service performance in accordance with generally accepted accounting practice in New Zealand. The financial statements must fairly reflect the financial position of the Guardians and group as at 30 June 2010 and the results of operations and cash flows for the year ended on that date. The statement of service performance must fairly reflect, for each class of outputs, the Guardians and group's standards of delivery performance achieved and revenue earned and expenses incurred, as compared with the forecast standards, revenue and expenses adopted at the start of the financial year. The board's responsibilities arise from the Crown Entities Act 2004, and the New Zealand Superannuation and Retirement Income Act 2001.

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

Independence

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

Other than the audit, we have no relationship with or interests in the Guardians or any of its subsidiaries.

BR Penrose

BRENT PENROSE
Ernst & Young
On behalf of the Auditor-General
Auckland, New Zealand

Responsible Investment Report

Report on how we have integrated ESG in 2009/10

1. Beliefs, policies, standards and procedures

Incorporating Responsible Investment issues into our assessment of external managers of securities

During the financial year we integrated Responsible Investment into our standard due diligence questionnaire for the selection of external investment managers. The managers are expected to complete the document as part of an assessment of their suitability to manage the Fund's money. This information is augmented by our assessment of incumbent managers' Responsible Investment policies, with market and peer reviews. The due diligence questionnaire is divided into four rough sections, as follows:

Policy	Seeking information on whether there are current or planned policies relating to environmental, social and governance issues and at what level in the organisation are these policies supported.
Active ownership	Seeking information on whether the manager has voting or engagement programmes in place to address poor corporate governance standards, or breaches of international standards of corporate behavior. This can be through voting or engagement with company management. In some cases, active ownership may be the only RI mechanism available e.g. for passive managers. Increasingly, we will look to our managers to take on a monitoring and engagement role.
Integration	Seeking information on the extent to which the manager integrates consideration of material environmental, social and governance information into their investment analysis and decision-making.
Exclusions	Seeking information on whether the manager is able to incorporate exclusions into mandates and if the manager offers pooled or passive vehicles with exclusions. Exclusions are a firm RI requirement for mandates where we are the sole client and are written into Investment Management Agreements (IMAs).

We have also incorporated the following into our practices and our documentation:

- Where possible, formal requirements for ESG due diligence, management and reporting are included in Private Equity, Infrastructure, and Timber investment documentation.
- Our property advisor is required to include ESG factors in their manager selection criteria and we are finalising RI property guidelines for our property investments.
- Integration of ESG factors into public (listed) markets (equity and fixed income) is primarily by internal and external analysis of portfolio holdings against ESG standards. We may raise issues with managers as they are identified, including discussions about the material impact of significant ESG issues on the investment.
- All new investment mandates or managers require RI consideration and RI requirements are included

in IMAs. At present for our equity and fixed-income managers this primarily means that we are able to exercise our RI voting, engagement or exclusion activities.

Positive Investment

Positive Investments are those that deliver strong environmental or social returns in addition to sufficient investment returns. We are developing a plan to integrate Positive Investment opportunities into investing.

The Fund already has several significant investments which would meet Positive Investment objectives. These include NZ Timber, given compliance with the standards of the Forestry Stewardship Council; and the Morrison & Co PIP Fund as it focuses on social infrastructure. We will report on our progress on this strategy in future Annual Reports.

Responsible Investment Committee

At its October 2009 meeting the Board made the decision to disestablish this committee, given the embedding of RI policies in the business of the Guardians. The Board now has direct oversight of the observance of RI policies. In our view, such integration is consistent with investment best practice – supported by the UNPRI's assessment of our activities (see the benchmarking section below for more detail).

2. Engagement

Engagement Process

Engagement is when we communicate with companies, either by ourselves or collaboratively with other investors, to encourage them to address poor ESG performance.

A formal framework has been established to manage the engagement process and is available on the website under the Responsible Investment menu.

Briefly, the engagement process begins with screening the portfolio to identify companies that have breached – or are reported to have breached – internationally recognised ESG standards. Our key source of information on potential or actual breaches is Riskmetrics Group, our external research provider. Riskmetrics analyses company performance in these areas, as well as investigating broader sources of information about the company's activities. Where there is evidence that companies have breached international standards, or where there is a high risk of them doing so, Riskmetrics adds the company to a 'red list'.

We prioritise our engagement with companies on the red list by seeking to understand if the breach is:

- Long-term or short-term;
- Historic or ongoing;
- Isolated or endemic.

Responsible Investment Report (continued)

Additionally, higher priority is accorded an engagement if the issue is consistent with an engagement theme (for the year to 30 June 2010 these included human rights and significant environmental damage). Finally, we assess the potential effectiveness of an engagement aimed at changing the behaviours and/or conduct underlying the breach and the resources required to do so. Engagement is our preferred, primary response to dealing with actual and perceived ESG issues within investee companies. However, there are some circumstances where exclusion or divestment of a company's securities from our portfolio may be appropriate. We discuss divestment further below.

Summary of company engagements in 2009/10

Here we summarise by ESG issue the numbers of companies engaged and companies monitored in the past financial year. The table also summarises the number of new additions to the 'red' list – where we have a concern but where more research is required – by ESG issue. Note that we have not identified the specific companies as we do not believe it is beneficial to a transparent, constructive engagement process.

ISSUE	COMPANIES ENGAGED	COMPANIES MONITORED	COMPANIES ADDED TO 'RED' LIST
Human rights	16	4	5
Environmental impact	4	1	6
Bribery/corruption	24	2	8
Supply chain	1		
Climate change disclosure	250		
General governance		1	
TOTAL	345*	8	19*

*Note there are instances of the same company appearing under more than one issue. We nevertheless regard each issue as a separate engagement.

Engagement Examples

ENGAGEMENT	ISSUE	OUR PARTICIPATION
UNPRI Engagement on Anti-Corruption - this focuses on 21 global companies with operations in sectors or countries exposed to a high level of corruption risk	This engagement seeks disclosure from major companies, notably in the defense and construction sectors, of their management policies on bribery and corruption. The investors involved believe it is very important for companies in which they are invested to provide sufficient information and reassurance on the material risks including corruption risks, that they face in the course of their business activities.	We are a signatory to a letter to 21 companies. The letter says: • where companies have not developed relevant policies, they should do so as a matter of urgency. • where policies are in place, companies should report on how the policies are implemented. Communication is continuing between the UNPRI and the companies and progress is being monitored.
Conflict-affected and high-risk countries	This UNPRI and UN Global Compact joint initiative formed an Expert Group on Responsible Investment in Conflict-Affected areas. The Expert Group examined the role of the private sector in fostering peace and development in post-conflict contexts and provided input to the development of a guidance document for companies and investors on responsible business practices in conflict-affected regions. The initiative included a series of multi-stakeholder events and was informed by case studies from around the world. The UN Global Compact published the "Guidance on Responsible Business in Conflict-Affected and High-risk Areas: A resource for companies and investors" at its Global Compact Leaders Summit in June 2010. The Guidance document is a key output from this engagement.	We are a member of the Expert Group on Responsible Investment in Conflict-Affected.Areas. The Expert Group is comprised of company representatives, investors, civil society leaders, UN representatives and others. We are now involved in the next phase of this project which aims to roll-out the Guidance document and encourage its use by companies and investors in companies operating in conflict-affected or high-risk environments.

Responsible Investment Report (continued)

Case Studies (continued)

ENGAGEMENT	ISSUE	OUR PARTICIPATION
UNPRI Sudan Engagement Group	The Sudan Engagement Group (SEG) is made up of 22 institutional investor signatories with approximately US$ 2.1 trillion total assets under management. These signatories recognise that their international investments include companies with operations in, or exposure to, Sudan – a country where human rights, governance and general political stability are a subject of ongoing public and political concern. The SEG believes that company exposure to Sudan poses additional risks to business and local society. The Group wants to better understand these risks and the steps companies need to undertake in order to avoid activities that exacerbate or fuel instability and a negative business environment.	Over the past 18 months, the SEG has issued formal correspondence and held private meetings with target companies operating in Sudan to discuss investors' concerns related to their long-term performance. In addition, the Group has commissioned an independent research study with the goal of acquiring more information on the current practices of selected companies on the ground. The findings of the research have also guided members of the SEG who visited Sudan and met with companies operating in the country, non-governmental organisations (NGOs), communities, diplomats, international experts and government representatives. SEG members attended a meeting with the UNPRI and UN Global Compact local network. The meeting provided input to the UN Guidance document on responsible business in conflict zones.

Case Studies (continued)

ENGAGEMENT	ISSUE	OUR PARTICIPATION
Submission on changes to NZX Listing Rules	In April 2009, the Commerce Minister Simon Power approved changes to the NZSX listing rules in response to the GFC. The Minister required a review of the changes after one year (i.e. in April 2010). The changes aimed to help listed companies to raise capital at the time of the GFC when they may have found themselves cash-constrained. Many of the NZX rule changes were designed to lessen the disclosure burden and reduce process times to ease access to capital and were generally welcomed by companies and investors. However, there were several changes with longer term implications for the protection of minority shareholders given the relaxtion of limitations on security issues to directors, transactions with related paries and reduced protection against dilution.	We made a submission to the Commerce Minister's review of the rule changes. We said we recognised that the changes were broadly emergency measures which, post the crisis, should revert to their original form. We said that reinstating the original shareholder approval requirements for the issue of new securities, participation of directors in placements and participation of directors in share schemes etc was consistent with: • NZ's markets having a good reputation; • alignment with the Australian market; • and, more generally, with being transparent and deterring market abuse.

Responsible Investment Report (continued)

3. Portfolio Monitoring and Exclusions

We have the ability to divest and to exclude companies under certain circumstances and have exercised it. We have excluded those companies that are directly involved:

- In the manufacture of cluster munitions;
- In the manufacture or testing of nuclear explosive devices;
- In the manufacture of anti-personnel mines;
- In the manufacture of tobacco; and
- In the processing of whale meat.

You can read more detail about each of these exclusions on our website under *Responsible Investment/Responsible Investment Reporting/Exclusion decisions.*

How do we enforce Exclusions?

We use specialist screening agencies to identify companies involved in cluster munitions, nuclear explosive devices and those companies that manufacture tobacco. These specialist agencies provide us with updated lists which allows us to update our exclusions list every six months. We may also receive relevant information from other organisations with expertise in this field or from the companies themselves. Our screening agencies review their research on a regular basis. We update our exclusion lists as required and inform our managers. The Fund is monitored by our Custodian for compliance with exclusions applied to the Fund.

4. Communication

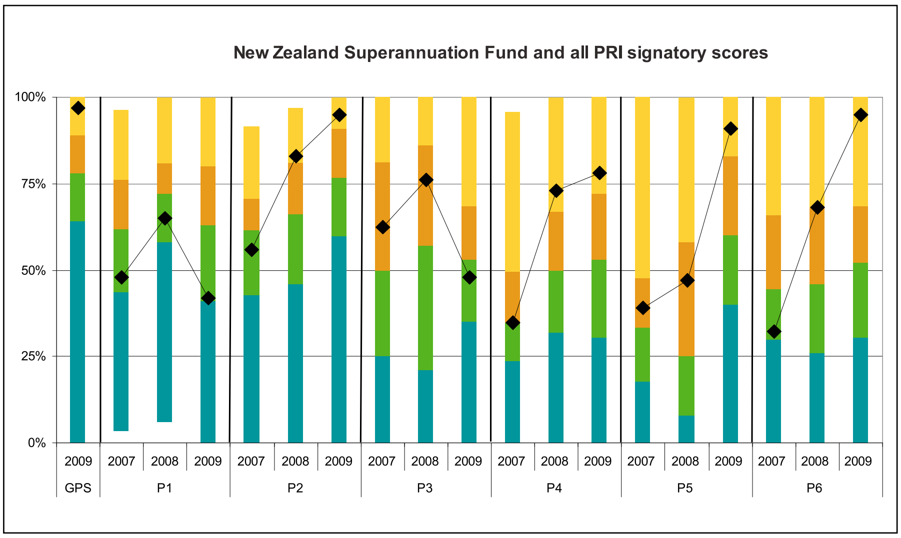
During the past financial year we have published a large amount of detail about our Responsible Investment programme. Highlights include:

- a restructuring of the Responsible Investment section of our website to ensure it is simple to understand and easier to navigate;
- publishing our performance, relative to our peers, in the UNPRI's annual assessment of how its signatories have performed against the six UNPRI principles (see the benchmarking section for further details); and
- publishing two six-monthly reviews of how we have voted our holdings. The reports can be found on the website under *Responsible Investment/Responsible Investment Reports*

Benchmarking

The UNPRI conducts an annual assessment of progress against its six principles for responsible investment by signatories. From 2008 it was compulsory.

Our results for the 2009 survey are set out in the below table (and the full report is available on our website) and show that, following on from our 2008 results, we continue to be one of the top performing funds in the region and in the upper half or quartile globally across the majority of principles. Specifically, we recorded top quartile scores in five of seven categories relative to global peers (as shown on the facing page) and relative to Asia-Pacific peers.



UNPRI Principles

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

We note that for 2009 we were in the one-third of signatories whose responses were verified by the UNPRI and this process resulted in the UNPRI raising the scores we had given ourselves in the self-assessment.

The decline in Principle 3 (P3) was a little unexpected as we have been active in collaborative efforts requiring better disclosure from investee companies however we acknowledge we could do more work in this area - we also note that the UNPRI used a Guardians case study to highlight best practice in this area in its 2009 Report on Progress. We are actively implementing the UNIPRI's suggestions for improvement and will report on these in the 2011 Annual Report.

Principle 1 (P1) was split into a standalone, additional Governance, Policy and Strategy section and a new Principle 1 more focused on integration into investment ESG considerations. Another adjustment was that exclusions and voting were not considered part of integration and scores were weighted by the percentage of assets under management to which ESG integration was applied. As expected, this change reduced our score on the new P1 but also highlighted our leadership in Governance, Policy and Strategy where we are the top of the first quartile.

5. Collaboration

We lead an initiative among Crown Financial Institutions (e.g. the Accident Compensation Corporation and the Government Superannuation Fund Authority) to collaborate on Responsible Investment activities within New Zealand and globally. We share research services, undertake joint collaborative engagement, support for RI initiatives and dialogue with managers and investee companies.

Governance and oversight of each CFI's RI Policy remains the core responsibility of that CFI. This initiative is aimed cost-sharing and at having a collective impact greater than what might be the case individually.

Responsible Investment Report (continued)

Our Environmental Policy

In April 2009 the Guardians prepared an environmental policy statement and developed an environmental action plan. The environmental policy states:

The Guardians of the New Zealand Superannuation are committed to understanding and managing the environmental impact of our activities. Through our individual and collective actions, we will continuously strive to safeguard our natural environment for future generations. As part of this commitment, we aim to measure and reduce;

- *our consumption of energy and resources;*
- *our greenhouse gas emissions; and*
- *the amount of waste we produce.*

We will implement this environmental policy through an environmental action plan which outlines a structured approach to assessing how our operations impact on the environment and identifies clear actions for improving our performance.

Our core business is investment management and one of our core beliefs is that responsible asset owners should have concern for environmental, social and governance issues of companies. Our Responsible Investment Policy integrates environmental considerations into our investment processes.

Implementation

In our 2009 Annual Report we published an assessment of the environmental 'footprint' of our organisation. We expressed this as the emissions of greenhouse gases, per person, arising from our overall consumption of energy and resources arising from our office buildings and our travel. The footprint uses power bills, taxi receipts and travel data to produce baseline data which we have updated for the past financial year.

Having established the baseline, we have strived to reduce our per person emissions. This goal reflects that our organisation is growing and that each individual working for the Guardians has a role to play in implementing the Environmental Policy.

Results

Relative to the 2008/09 financial year there has been an increase in the overall per person emissions of greenhouse gases from 10.83 tonnes per FTE to 12.41 tonnes. This is entirely due to increased airline travel, as there were absolute and per person reductions in both taxi travel and power consumption.

The increase in airline travel is a consequence of our increased international investments. Travel is an inescapable driver of our business activity and we would expect it to continue to be the major contributor to our organisational footprint.

Relevant activities and information

- Our FTE increased from 56.2 at 30 June 2009 to 64 at 30 June 2010;
- Our computer servers were shifted offsite during the year. This removed a significant source of energy consumption from our Auckland office (although the data includes a pro-rata share of the power supplied to where our server sits in the offsite facility);
- We implemented a Guardians 'Green Team' involving representatives from each section of the organisation. The Team introduced the following initiatives:
    - o power-saving procedures for the use of printers. This involves staff being strongly encouraged to use an individual code to collect printed documents. This eliminates wastage arising from printed documents being forgotten and further copies printed;
    - o a 'switch off' education programme for meeting rooms once meetings have concluded – this involves stickers on light switches and regular reminders.
    - o a revised travel form requiring staff members to set out why the objectives underlying travel cannot be met via a phone call or teleconferencing. This was supported with an upgrade of our teleconferencing facilities during the year to ensure they represented a feasible alternative to face-to-face meetings.

Footprint

GUARDIANS 'FOOTPRINT' ASSESSMENT – GREENHOUSE GAS EMISSIONS				
ACTIVITY	BASELINE GREENHOUSE EMISSIONS (tonnes to 30 June 2009)	BASELINE EMISSIONS PER PERSON (tonnes to 30 June 2009)[2]	**EMISSIONS to 30 June 2010**	**EMISSIONS PER PERSON to 30 June 2010**
Power usage	31.8[4]	.57	**31.5**	**.49**
Taxi usage[5]	7.3	.13	**6.0**	**.09**
Flights[6]	569.4	10.13	**757.0**	**11.83**
TOTAL	608.5	10.83	**794.5**	**12.41**

Waste Audit

For the 2009 Annual Report we conducted a waste audit to establish how much waste we could recycle with a full recycling programme. The audit produced 1.2m^3 of waste, of which 95% was recyclable – the majority of it (90%) being paper.

As a consequence we instituted an organisational recycling programme primarily focussed on 100% recycling of waste paper (given its dominance of the weight mix) but which also required separation of food waste from non-food waste. We then conducted a further audit to assess whether the potential for recycling was being met.

The audit occurred in the week of 19 April 2010 and showed that we had achieved a 96% recycling rate, or 1.21m^3 of the 1.26 m^3 of the waste produced in the week. Of the non-recyclable waste, half was food waste.

Our baseline is therefore seeking to recycle at least 96% of the waste we produce. We will audit this quarterly and report the results.

Portfolio footprint

We are conscious that an institutional investor's environmental footprint extends beyond its direct consumption of resources and production of waste. The investor's footprint also includes the companies and enterprises in which it is invested: in particular, those companies and enterprises where the investor controls the company or has a significant influence on its activities via a significant but minority shareholding and/or a position on its board (or equivalent).

The Guardians are working on this issue and we will report on our progress in the 2011 Annual Report. The outcome of this exercise will shape what we ultimately report as our full organisational climate footprint. Logically, it will shape our climate risk reporting expectations of New Zealand and global investee companies. We have an internal team considering the following factors:

- the proposed New Zealand Emissions Trading Scheme (NZETS) and its implications for our local holdings and investments (and clearly there is relevance for our direct interests in New Zealand forestry);
- what useful guidelines and implications for our assessment and reporting of our climate risk exposure are present in global tools such as the Climate Disclosure Project and in international regulatory responses to the issue;
- a broader analysis of our direct and indirect exposures to climate change risk and opportunities; and
- what climate change mitigation actions are being undertaken by our peer funds.

1. All emissions calculations via Climate Friendly at www.climatefriendly.com
2. As at 30 June 2009 the Guardians had 56.2 staff (54 full-time and 2.2 part-time)
3. As at 30 June 2010 the Guardians had 64 staff (59 full-time and five part-time)
4. Note that in the 2009 Annual Report we reported 20.2 tonnes however that total was to 30 April as June 2009 data was not available at the time the report was compiled
5. Taxi data represents 4.4 tonnes for 5-litre taxis and 2.9 tonnes for 4.0-litre taxis
6. All domestic and international travel

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