



Livestock Improvement Corporation Annual Report

For the year ended 31 May 2018

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Introduction

These financial statements set out the performance, position and cash flows of Livestock Improvement Corporation ("LIC" or the "Company") and its subsidiaries (the "Group") for the year ended 31 May 2018.

LIC is domiciled in New Zealand, registered under the Companies Act 1993 and the Co-operative Companies Act 1996, and listed on the Alternative Board of the New Zealand Stock Exchange Limited ("NZAX"). LIC is an FMC Reporting Entity for the purposes of the Financial Reporting Act 2013 and the Financial Markets Conduct Act 2013.

These financial statements comply with NZ GAAP as appropriate for Tier 1, for-profit entities, NZIFRS and IFRS.

The functional currency of the Company and the presentation currency of the financial statements is NZD.

The financial statements have been prepared on a GST exclusive basis, with the exception of trade receivables and trade payables, which are reported inclusive of GST.

The key estimations and judgements made in preparing these financial statements are the valuation of the Bull team and the impairment testing of software and other intangible assets.

The accounting policies have been applied consistently with prior periods. Accounting standards relevant to the Group that have been issued but are not yet effective, and have not been early adopted, include:

- NZ IFRS 9 (2009) Financial Instruments: effective January 2018, impact assessed to be immaterial
- NZ IFRS 15 Revenue: effective January 2018, impact assessed to be immaterial
- NZ IFRS 16 Leases: effective January 2019, impact assessed to be immaterial.

Key results and position

		2018	2017
RESULTS FOR THE YEAR	Note		
Revenue	1	236,420	203,529
Purchased materials		(35,140)	(28,406)
People costs		(98,943)	(89,357)
Depreciation and amortisation	3,4	(28,295)	(28,085)
Research & Development		(13,246)	(13,944)
One-off transformation costs		(20,665)	(1,735)
Other expenses	10	(33,816)	(33,927)
Net finance costs		(1,297)	(2,241)
Bull team revaluation	2	8,634	24,663
Profit/(loss) before tax expense		13,652	30,498
Tax expense	7	(4,387)	(9,698)
Profit/(loss) for the year		9,265	20,800
Hedge revaluations	5	216	(224)
Investment revaluations	5	3,138	830
Land & buildings revaluations	3,5	3,450	1,049
		6,804	1,654
Comprehensive income for the year		16,069	22,454
<i>Profit per Investment Share (excl. treasury stock)</i>		<i>\$ 0.33</i>	<i>\$ 0.70</i>

Supplementary note to the results for the year:			
<i>Profit/(loss) for the year</i>		9,265	20,800
<i>Less Bull team revaluation</i>		(8,634)	(24,663)
<i>Tax effect</i>		2,418	6,906
Underlying earnings under LIC Constitution		3,049	3,042
<i>Underlying earnings per Investment Share (excl. treasury stock)</i>		<i>\$ 0.11</i>	<i>\$ 0.10</i>

POSITION AT YEAR END		2018	2017
Cash		2,521	3,458
Debtors	8	45,090	47,495
Bull team	2	120,808	112,174
Land, buildings and equipment	3	72,030	78,390
Software, goodwill and other intangible assets	4	74,011	73,106
Other assets	8	27,265	26,861
Total assets		341,725	341,484
Creditors		24,253	22,081
Borrowings	5	19,636	32,070
Co-operative Control Shares	5	6,262	6,238
Deferred tax	7	40,945	39,141
Other liabilities	9	8,528	8,541
Total liabilities		99,624	108,071
Investment Shares	5	53,126	58,464
Retained earnings	5	150,141	141,285
Other reserves	5	38,834	33,664
Total equity		242,101	233,413

Director

Date: 18 July 2018

Director

Date: 18 July 2018

Key results and position

		2018	2017
CASH FLOWS FOR THE YEAR	Note		
Customer receipts		227,082	205,195
Supplier payments		(188,855)	(177,108)
Tax payments		(2,231)	(2,308)
Other operating cash flows		1,834	(420)
Net operating cash flows	12	37,830	25,359
Software development		(21,214)	(11,919)
Net sales/(purchases) of land, buildings and equipment		8,958	45
Other investment cash flows		(6,162)	(1,415)
Net investment cash flows		(18,418)	(13,289)
Drawdown/(repayment) of bank debt		(12,500)	(10,500)
Issue of Co-operative Control Shares		914	821
Repurchase of Co-operative Control Shares		(889)	(1,380)
Interest paid on Co-operative Control Shares		(543)	-
Investment Share repurchases		(5,338)	-
Dividends paid		(2,043)	-
Net financing cash flows		(20,399)	(11,059)
Movement in cash for year		(987)	1,012
Cash at beginning of the year		3,458	2,667
Currency movement on cash holdings		50	(220)
Cash at end of the year		2,521	3,458

CHANGE IN POSITION FOR THE YEAR

	Investment Shares	Retained earnings	Other reserves	Total equity
Balance at 1 June 2017	58,464	141,285	33,664	233,413
Profit/(loss) for the year	-	9,111	154	9,265
Dividends paid	-	(1,900)	(143)	(2,043)
Hedge revaluations	-	-	216	216
Investment revaluations	-	-	3,138	3,138
Land & buildings revaluations	-	-	3,450	3,450
Transfer of asset revaluations on sale	-	1,645	(1,645)	-
Investment Share repurchases	(5,338)	-	-	(5,338)
Balance at 31 May 2018	53,126	150,141	38,834	242,101
Balance at 1 June 2016	58,464	120,703	31,790	210,957
Profit/(loss) for the year	-	20,568	232	20,800
Dividends paid	-	-	-	-
Hedge revaluations	-	-	(224)	(224)
Investment revaluations	-	-	830	830
Land & buildings revaluations	-	-	1,049	1,049
Non-controlling interest movement	-	13	(13)	-
Balance at 31 May 2017	58,464	141,285	33,664	233,413

More details

1. Business analysis

The Group operates in four key operating segments, and across four key geographies as set out below. Figures in the following tables reflect information regularly reported to the Chief Executive on those key operating segments:

- NZ market genetics: provides bovine genetic breeding material and related services, predominately to dairy farmers
- Herd testing: herd testing and animal recording for pastoral farmers
- Farm software: data recording and farm management information services
- Farm automation: provides dairy automated equipment and technology

2018	NZ market genetics	Herd testing	Farm software	Farm automation	Other	Eliminations	Total
External revenue	92,943	31,369	43,924	20,177	48,007	-	236,420
Inter-segment revenue	-	-	-	2,217	1,520	(3,737)	-
Total revenue	92,943	31,369	43,924	22,394	49,527	(3,737)	236,420
Depreciation & amortisation	(1,033)	(2,828)	(7,060)	(2,893)	(14,481)	-	(28,295)
Segment profit before tax	62,360	12,005	26,822	8,937	28,922	-	139,046
Bull team revaluation							8,634
One-off transformation costs							(20,665)
Unallocated amounts							(113,363)
Profit/(loss) before tax							13,652

2017	NZ market genetics	Herd testing	Farm software	Farm automation	Other	Eliminations	Total
External revenue	81,429	24,631	41,233	14,273	41,963	-	203,529
Inter-segment revenue	-	-	-	1,340	1,833	(3,173)	-
Total revenue	81,429	24,631	41,233	15,613	43,796	(3,173)	203,529
Depreciation & amortisation	(1,239)	(3,002)	(6,380)	(2,184)	(15,281)	-	(28,085)
Segment profit before tax	49,617	7,968	24,770	6,832	24,546	-	113,732
Bull team revaluation							24,663
One-off transformation costs							(1,735)
Unallocated amounts							(106,163)
Profit/(loss) before tax							30,498

The Other segment includes international operations, diagnostics, animal health, research & development and support services. Unallocated amounts include personnel costs, administrative and other fixed costs and net finance costs.

2018	New Zealand	Australia	Ireland	United Kingdom	Other	Total
Revenues	219,268	6,942	2,888	3,382	3,940	236,420
Non-current assets	265,574	6,595	260	8,047	154	280,630
2017						
Revenues	186,988	6,402	2,809	2,883	4,448	203,529
Non-current assets	261,470	6,590	219	381	192	268,851

More details

1. Business analysis (cont.)

The Group's significant subsidiaries are:

- **New Zealand:** LIC Agritechnology Company Limited (100%), LIC Automation Limited (100%)
- **Australia:** Livestock Improvement Pty Ltd (100%), Beacon Automation Pty Ltd (75%)
- **Ireland:** LIC Ireland Limited (100%)
- **United Kingdom:** Livestock Improvement Corporation (UK) Ltd (100%)

The Group is not dependent on any one major customer in any of its reportable segments.

External revenues attributable to other segments include government grant income of \$3.257 million (2017: \$3.275 million).

2. Bull team

The bull team is the cornerstone asset of LIC's genetics business. The 993 total bulls (2017: 1,036 bulls) from which the bull team are selected are carried at their fair value, which is based on LIC's modelling of future cash flows from the bulls (a "Level 3 valuation"). Changes in their fair value are reported in profit.

The fair value from the bulls is partly dependent on the future sales mix of LIC's genetics products, which is historically strongly correlated to the Farmgate Milk Price paid by Fonterra Co-operative Group. The valuation is therefore most sensitive to this input and the WACC rate used to discount those future cash flows. The expected useful life of the existing bull team is also considered to be a key driver of the model.

	2018	2017
Opening balance	112,174	87,511
Bull team revaluation	8,634	24,663
Closing balance	<u>120,808</u>	<u>112,174</u>

Key drivers of the model:

Mean 3 year forward Fonterra Farmgate Milk Price*	\$6.00	\$5.80
WACC annualised post tax rate	6.42% - 8.16%	6.34% - 7.78%
Existing Sire Proving Scheme bull team size	180	180
Expected average bull useful life	4.7	4.7

* This is the average of market analyst consensus

3. Land, buildings and equipment

Land and buildings are carried at fair value, determined by an independent valuer at least every three years (most recently as at 30 April 2018). Revaluations are reflected in the revaluation reserve. Equipment includes plant, vehicles, furniture and fittings and IT hardware, and is carried at depreciated cost. Buildings and equipment are depreciated on a straight-line basis over their estimated useful lives, and reviewed annually for any indications of impairment.

	2018				2017			
	Land	Buildings	Equipment	Total	Land	Buildings	Equipment	Total
Opening balance	31,405	30,981	16,004	78,390	36,551	32,464	23,292	92,307
Additions	-	504	7,167	7,671	-	254	3,544	3,798
Disposals	(1,010)	(6,106)	(2,542)	(9,658)	(36)	(37)	(2,899)	(2,972)
Transfer to held for sale	-	-	-	-	(5,110)	(1,298)	(116)	(6,524)
Depreciation	-	(1,746)	(6,240)	(7,986)	-	(1,865)	(7,753)	(9,618)
Revaluation	1,874	1,743	-	3,617	-	1,456	-	1,456
Foreign exchange impact	-	(18)	14	(4)	-	7	(64)	(57)
Closing balance	32,269	25,358	14,403	72,030	31,405	30,981	16,004	78,390
<i>Value if carried at cost</i>	<i>9,684</i>	<i>18,807</i>	<i>N/A</i>		<i>10,694</i>	<i>26,154</i>	<i>N/A</i>	
<i>Estimated useful lives</i>	<i>N/A</i>	<i>10-40 years</i>	<i>3-10 years</i>		<i>N/A</i>	<i>10-40 years</i>	<i>3-10 years</i>	

More details

4. Software and other intangibles

(i) Software and other intangible asset balances

Software development expenditure is capitalised only where costs are directly attributable, and once the product or process is commercially feasible, the benefits are probable, and the Group intends to sell or use the completed software.

Software assets are amortised over their useful lives of up to seven years on a straight line basis, and reviewed annually for indicators of impairment.

Intellectual property (IP) assets are amortised over their estimated useful lives, being up to 13 years.

The genetic data in the LIC database increases in value with each successive generation. Both goodwill and the LIC database have indefinite useful lives. They are recognised at cost and are not amortised, are allocated to a cash generating unit ("CGU") and tested for impairment annually.

	2018				2017			
	Software & IP	Goodwill	Database	Total	Software & IP	Goodwill	Database	Total
Opening balance	56,286	6,320	10,500	73,106	58,576	10,579	10,500	79,655
Additions	21,146	-	-	21,146	16,660	(4,143)	-	12,517
Disposals	(129)	-	-	(129)	(484)	-	-	(484)
Amortisation	(20,309)	-	-	(20,309)	(18,468)	-	-	(18,468)
Impairment	-	-	-	-	-	-	-	-
Foreign exchange impact	4	193	-	197	2	(116)	-	(114)
Closing balance	56,998	6,513	10,500	74,011	56,286	6,320	10,500	73,106

At reporting date, software includes \$12.883 million of work in progress, which is not being amortised until it is ready for use.

(ii) Impairment testing of intangible assets

Allocation of Goodwill and the LIC Database to CGUs:

	2018				2017			
	Farm software and herd testing CGU	Farm automation CGU	Other CGU	Total	Farm software and herd testing CGU	Farm automation CGU	Other CGU	Total
LIC database	10,500	-	-	10,500	10,500	-	-	10,500
Goodwill	-	4,144	2,369	6,513	-	4,144	2,176	6,320
	10,500	4,144	2,369	17,013	10,500	4,144	2,176	16,820

The LIC database and all goodwill recoverable amounts have been determined using value in use.

A discounted cash flow model is used for impairment testing based on expected results and capital expenditure from the current year forecast, 3 year Board approved plan and a projection for further periods using terminal growth rate. A five year cash flow projection period is used. The terminal growth rate used is 2% (2017: 2%) for the Database and Goodwill. The discount rate applied is reviewed and updated annually based on published Treasury risk-free rates and is 8.5% for the Database and 8.5-10.0% for Goodwill (2017: 7.1% for the Database and Goodwill).

More details

5. Funding

The Group's funding comes from Investment Shares, Co-operative Control Shares, retained earnings, other reserves and borrowings. **Following the balance date, all shares in the Company have been reclassified into Ordinary Shares as further described on page 17.**

(i) Investment Shares

Investment Shares are listed on the NZAX and tradeable between Co-operative Control Shareholders. They are also able to be purchased by employees under the LIC Employee Share Scheme. They are fully paid, redeemable at LIC's option, pay discretionary dividends, carry no voting rights, and entitle the holder to a share of LIC's residual net assets on wind-up. They are recognised as equity, and dividends are shown as a reduction in equity. At reporting date, there were 28,194,194 Investment Shares on issue, excluding 1,334,396 shares purchased from minority shareholders during the year and held as treasury stock (2017: 29,528,590 shares with no treasury stock).

(ii) Co-operative Control Shares

Co-operative Control Shares are held by LIC's New Zealand dairy customers. The shares have a nominal value of \$1.00, and must be redeemed when a shareholder stops being a customer. They carry voting rights, and pay a dividend in preference to Investment Shares based on Westpac New Zealand's Farm First mortgage rate. They are recognised as a liability, and dividends are shown as a finance expense. At reporting date, there were 6,262,489 Co-operative Control Shares on issue (2017: 6,238,006 shares).

(iii) Other reserves and equity

	Hedge revaluation reserve	Investment revaluation reserve	Land & building revaluation reserve	Non- controlling interests	Other reserves
Balance at 1 June 2017	(265)	1,628	32,074	227	33,664
Profit/(loss) for the year	-	-	-	154	154
Dividends paid	-	-	-	(143)	(143)
Revaluations	216	3,138	3,450	-	6,804
Transfer of asset revaluations on sale	-	-	(1,645)	-	(1,645)
Non-controlling interest movement	-	-	-	-	-
Balance at 31 May 2018	(49)	4,766	33,879	238	38,834
Balance at 1 June 2016	(41)	798	31,025	8	31,790
Profit/(loss) for the year	-	-	-	232	232
Revaluations	(224)	830	1,049	-	1,655
Non-controlling interest movement	-	-	-	(13)	(13)
Balance at 31 May 2017	(265)	1,628	32,074	227	33,664

(iv) Bank debt

Bank loans and borrowings are secured by a Negative Pledge granted to Westpac and Rabobank over certain New Zealand-based subsidiaries. All debt outstanding at 31 May 2018 is considered current.

More details

6. Liquidity and interest rate risk

(i) Liquidity risk

Liquidity risk is the risk of having insufficient liquid assets to pay the Group's debts as they fall due. The Group manages the risk by monitoring forecast cashflows and holding sufficient bank facilities to meet the Group's needs. The contractual maturity of the Group's funding is shown below.

	2018				2017			
	Demand to 6 months	6 months to 1 year	1 year plus	Total	Demand to 6 months	6 months to 1 year	1 year plus	Total
Bank debt	19,636	-	-	19,636	17,070	-	15,000	32,070
Co-operative Control Shares	6,262	-	-	6,262	6,238	-	-	6,238
Creditors	24,253	-	-	24,253	22,081	-	-	22,081
	50,151	-	-	50,151	45,389	-	15,000	60,389

Co-operative Control Shares must be redeemed when a Shareholder has ceased to be, or no longer has the capacity to be, a user of the Company's products or services. Redemptions can occur either on application for voluntary surrender by the Shareholder or by the Company pursuant to the Constitution. Following the balance date, all Co-operative Control Shares in the Company have been reclassified into Ordinary Shares as further described on page 17.

The Group has bank funding facilities in place until June 2020 and expects to be able to meet any obligations which fall due.

(ii) Interest rate risk

Interest rate risk is the risk that changes in interest rates will impact the Group's results or position. The weighted average interest rate paid on borrowings in 2018 was 3.60% (2017: 3.32%). A 1% increase in interest rates would reduce profit after tax by approximately \$0.245 million (2017: \$0.320 million).

More details

7. Tax

Tax expense is recognised for items arising this year that are either taxable this year (current tax) or in other years (deferred tax). The main items giving rise to deferred tax are revaluations of Bull team and Land & Buildings.

<i>(i) Tax expense</i>	2018	2017
Profit/(loss) for the year	9,265	20,800
Tax expense	4,387	9,698
Profit/(loss) for the year before tax	13,652	30,498
Tax at 28% NZ company tax rate	3,823	8,539
Effect of overseas income	19	77
Non-deductible expenses	789	613
Adjustments from prior periods	(244)	469
Tax expense	4,387	9,698
<i>Current tax expense</i>	2,750	2,152
<i>Deferred tax expense</i>	1,637	7,546
<i>Imputation credits available</i>	17,385	17,005

<i>(ii) Deferred tax liability</i>	As at 31 May 2018	Through Profit/(loss)	Through Other reserves	As at 31 May 2017	Through Profit/(loss)	Through Other reserves	As at 31 May 2016
Livestock revaluation	33,165	2,390	-	30,775	6,532	-	24,243
Land & buildings revaluation	5,970	(838)	167	6,641	464	408	5,769
Other	1,810	85	-	1,725	550	-	1,175
Total	40,945	1,637	167	39,141	7,546	408	31,187

8. Debtors and other assets

(i) Debtors

Bad debts of \$0.038 million have been expensed during the year (2017: \$0.015 million), and 98% of trade receivables are not past due (2017: 97%). In 2017, Debtors included a prepayment of \$12.125 million relating to revenue generation and cost efficiency projects for future years.

<i>(ii) Other assets</i>	2018	2017
Inventories	12,739	12,003
Investments	13,780	5,181
Other livestock	746	3,153
Land & buildings held for sale	-	6,524
	27,265	26,861

Inventories utilised and expensed during the period amounted to \$21.022 million (2017: \$15.716 million). Inventories written off in 2018 totalled \$0.003 million (2017: \$0.938 million).

9. Other liabilities

	2018	2017
Provisions for employee entitlements	4,483	4,290
Provision for sire proving rebate	2,772	3,424
Derivatives used for hedging	57	206
Provision for tax	840	320
Other	376	301
	8,528	8,541

Following the approval by shareholders of the share simplification (see page 17), a small number of shareholders elected to exercise their minority buy-out rights arising from the proposal under the Companies Act 1993 ("Act"). LIC confirms that on 19 April 2018 it bought back 1,334,396 Investment Shares as a result of the shareholders exercising their rights. LIC will hold these shares as treasury stock. Those shareholders that exercised their minority buy-out rights have objected to the price proposed by LIC, being \$4.00 per share, and the final purchase price to be paid by LIC for the affected shares will therefore be determined in an arbitration. No provision has been made for any additional payments in these financial statements as LIC believes the price paid was fair and reasonable and is supported by independent valuations.

More details

10. Other expenses

Other expenses includes the following amounts paid to the Group's auditors, KPMG:

	2018	2017
Audit of the financial statements	136	156
Other assurance work	6	6
Audit-related services	42	-
	184	162

11. Transactions with related parties, directors and management

The Group has had the following short term transactions with key management and directors during the year, noting sale of goods and services were under normal trade terms:

	2018	2017
Remuneration of key management and directors	4,249	3,273
Sale of goods and services to key management and directors	669	574

Directors of the Company and their related entities hold 17,970 Co-operative Control Shares and 93,166 Investment Shares, representing 0.3% and 0.3% of shares on issue (2017: 17,259 and 91,674; representing 0.3% and 0.3%).

There are no loans or deposits with related entities outside of the consolidated group.

12. Reconciliation of the Profit/(Loss) for the year to Net operating cashflows

	2018	2017
Profit for the year	9,265	20,800
Adjusted for non-cash items:		
Depreciation and amortisation	28,295	28,085
Bull team revaluation	(8,634)	(24,663)
Working capital movements and other non-cash items	8,904	1,137
Net operating cash flows	37,830	25,359

13. Operating leases

Non-cancellable operating lease rentals are payable as follows:

	2018	2017
Less than one year	3,468	1,759
Between one and five years	8,074	2,790
More than five years	2,989	262
	14,531	4,811

The Group leases a number of facilities and vehicles under operating leases. The leases vary in length depending on location, fit out and business need. During the year ended 31 May 2018 \$1.683 million was recognised as operating lease expense (2017: \$1.205 million).

14. Subsequent events

On 14 March 2018, LIC Shareholders approved the share simplification, which will bring LIC's two classes of shares into one. As a result, LIC's share capital is being reorganised and its constitution amended in July 2018 to reflect the share simplification approvals.

After 31 May 2018 a dividend of 1.71 cents per Ordinary Share was proposed by the Directors in relation to the 2018 year, or \$2.439 million (2017: 6.44 cents per Investment Share, or \$1.900 million)



Independent Auditor's Report

To the Shareholders of Livestock Improvement Corporation Limited

Report on the consolidated financial statements

Opinion

In our opinion, the accompanying consolidated financial statements of Livestock Improvement Corporation Limited (the Company) and its subsidiaries (the Group) on pages 1 to 10:

- i. Present fairly in all material respects the Group's financial position as at 31 May 2018 and its financial performance and cash flows for the year ended on that date; and
- ii. Comply with New Zealand Equivalents to International Financial Reporting Standards and International Financial Reporting Standards.

We have audited the accompanying consolidated financial statements which comprise:

- The consolidated statement of position at year end as at 31 May 2018;
- The consolidated statements of results for the year, changes in position for the year and cash flows for the year then ended; and
- Notes, including a summary of significant accounting policies and other explanatory information.



Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (New Zealand) ('ISAs (NZ)'). We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

We are independent of the Group in accordance with Professional and Ethical Standard 1 (Revised) Code of Ethics for Assurance Practitioners issued by the New Zealand Auditing and Assurance Standards Board and the International Ethics Standards Board for Accountants' Code of Ethics for Professional Accountants (IESBA Code), and we have fulfilled our other ethical responsibilities in accordance with these requirements and the IESBA Code.

Our responsibilities under ISAs (NZ) are further described in the auditor's responsibilities for the audit of the consolidated financial statements section of our report.

Our firm has also provided other assurance services in connection with certification of the Group's grant funding, reviewing a new template for the financial statements, and auditing of the Group's share structure transaction. Subject to certain restrictions, partners and employees of our firm may also deal with the Group on normal terms within the ordinary course of trading activities of the business of the Group. These matters have not impaired our independence as auditor of the Group. The firm has no other relationship with, or interest in, the Group.



Materiality

The scope of our audit was influenced by our application of materiality. Materiality helped us to determine the nature, timing and extent of our audit procedures and to evaluate the effect of misstatements, both individually and on the consolidated financial statements as a whole. The materiality for the consolidated financial statements as a whole was set at \$1.2 million.



Key audit matters

Key audit matters are those matters that, in our professional judgement, were of most significance in our audit of the consolidated financial statements in the current period. We summarise below those matters and our key audit procedures to address those matters in order that the Shareholders as a body may better understand the process by which we arrived at our audit opinion. Our procedures were undertaken in the context of and solely for the purpose of our statutory audit opinion on the consolidated financial statements as a whole and we do not express discrete opinions on separate elements of the consolidated financial statements.

The key audit matter

How the matter was addressed in our audit

Valuation of the bull team

Refer to Note 2 to the Financial Statements

Determining the valuation of the bull team, which is the core asset to both the domestic and international genetics operations of the Group, is a highly judgmental and complex area. Management prepare a model that projects the number of straws that the current team can produce and will be sold over the life of the bulls. The valuation model factors the cost of rearing, animal and farm management costs, and forecasts of processing costs to make sales. The calculated surplus is discounted to reflect the time value of money.

Our audit procedures included, among others, valuation specialist review of the model and challenge of management's significant assumptions such as:

- Projected sales volumes and pricing;
- Discount rates applied; and
- Useful life of the bulls.

We compared sales and costs growth, and inflation rates to historical data and published market forecast data where available. We reviewed market and industry data to assess management's discount rate applied to the final model. We assessed projected pricing and life of the bulls based on our knowledge of the industry. We found the inputs to be comparable.

We also considered management's forecasts in previous years and found it to be sufficiently accurate based on actual results achieved.

Carrying value of intangible assets

Refer to Note 4 to the Financial Statements

The Group has two categories of intangible assets with indefinite useful lives:

- Goodwill of \$6.3m, arising primarily from acquisitions made to facilitate growth and diversification of the Group's farm automation products; and
- The LIC Animal Database of \$10.5m which is used by the Group to deliver its Herd Testing and Farm Software services.

The three significant cash generating units (CGUs) holding these assets are required to be tested for impairment on an annual basis, and management have developed models to test the carrying value of these assets.

We focussed our audit effort in determining whether the judgements made by management in allocating goodwill to each CGUs were appropriate.

We also challenged management on the reasonableness of the assumptions included in the cashflow forecast models, with particular attention paid to the following:

- Assessing management's future sales and growth assumptions compared to external market data and historical performance of each of the CGUs;
- Comparing management's previous forecasts to actual results achieved overall; and
- Assessing whether the outcome of the cashflow forecast models were influenced by use of alternative inputs within a reasonable range.

From the procedures performed, we have no matters to report.

Other information

The Directors, on behalf of the Group, are responsible for the other information included in the entity's Annual Report. Other information includes the Directors Report and the Governance Report. Our opinion on the consolidated financial statements does not cover any other information and we do not express any form of assurance conclusion thereon.

In connection with our audit of the consolidated financial statements our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the consolidated financial statements or our knowledge obtained in the audit or otherwise appears materially misstated. If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.



Use of this independent auditor's report

This independent auditor's report is made solely to the Shareholders as a body. Our audit work has been undertaken so that we might state to the Shareholders those matters we are required to state to them in the independent auditor's report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Shareholders as a body for our audit work, this independent auditor's report, or any of the opinions we have formed.



Responsibilities of the Directors for the consolidated financial statements

The Directors, on behalf of the Company, are responsible for:

- The preparation and fair presentation of the consolidated financial statements in accordance with generally accepted accounting practice in New Zealand (being New Zealand Equivalents to International Financial Reporting Standards) and International Financial Reporting Standards;
- Implementing necessary internal control to enable the preparation of a consolidated set of financial statements that is fairly presented and free from material misstatement, whether due to fraud or error; and
- Assessing the ability to continue as a going concern. This includes disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless they either intend to liquidate or to cease operations, or have no realistic alternative but to do so.



Auditor's responsibilities for the audit of the consolidated financial statements

Our objective is:

- To obtain reasonable assurance about whether the consolidated financial statements as a whole are free from material misstatement, whether due to fraud or error; and
- To issue an independent auditor's report that includes our opinion.

Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs NZ will always detect a material misstatement when it exists.



Misstatements can arise from fraud or error. They are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these consolidated financial statements.

A further description of our responsibilities for the audit of these consolidated financial statements is located at the External Reporting Board (XRB) website at:

<http://www.xrb.govt.nz/standards-for-assurance-practitioners/auditors-responsibilities/audit-report-1/>

This description forms part of our independent auditor's report.

The engagement partner on the audit resulting in this independent auditor's report is **Matthew Prichard**.

For and on behalf of

A handwritten signature of the KPMG firm, written in black ink. The letters 'KPMG' are written in a stylized, cursive-like font.

Auckland

18 July 2018

Directors' report

Directors' Report 2017-18 **Another solid year for LIC**

The 2017-18 financial year marked a solid 12 months for LIC despite at times, some challenging operating conditions.

The full-year result was in-line with market expectations and shows a strong underlying increase in profitability from the 2016-17 financial year after allowing of the one-off costs related to the transformation programme. Total revenue for the year was relative to last year and LIC's highest ever annual revenue amount. This reflects sustained confidence from farmers in LIC and the value its products provide for herd improvement.

After a year of transformation and change, including share simplification, our co-operative is in strong shape. As a business we are more match-fit than what we have been for a number of years and better positioned to drive good outcomes for our farmers.

We are pleased to confirm a dividend of \$2.44 million fully imputed will be paid to shareholders on 17 August, representing 80% of underlying earnings. This is the first dividend to be paid on LIC's ordinary shares.

Performance highlights:

- \$236.4 million total revenue, up 16% from \$203.5 million last year.
- \$27 million earnings before interest and tax (EBIT) excluding bull team revaluation and one-off transformation costs of \$20.7million, up 175% on last year.
- Reported EBIT of \$14.9 million, 54% down on same period last year. This is due to the impact of the one-off transformation costs and the annual revaluation of the biological bull team.
- \$9.3 million net profit after tax (NPAT), down from \$20.8 million last year due to one-off transformation costs and a smaller increase in bull valuation than last year.
- \$3.0 million Underlying Net earnings (NPAT excluding the increase on fair value of the biological assets and related tax effect), same as previous year.

This is a positive result for LIC and reflects a strong performance in our core service areas, as well as continued benefits from our transformation programme.

We sold 5.2 million AB straws and 10.9 million milk samples were processed for herd testing. Demand for diagnostics and animal health testing was also strong and international business continued to grow with AB export sales exceeding 1 million straws for the first time.

Ongoing volatility in milk prices, increasing environmental constraints, and new biosecurity challenges such as *Mycoplasma bovis* (M. bovis) show how critical it is that as a co-operative we take nothing for granted and that we continue our focus on agility.

A highlight of the year was the successful shareholder vote on simplification of LIC's share structure. This has allowed us to address concerns around the growing disparity between LIC's two share classes and will ensure a more agile co-operative for the future. We thank you for your support of the proposal.

During the financial year, LIC continued the transformation programme it begun in 2016-17 and the cost efficiencies gained were key contributors towards the improved full-year result. The business processes adopted as part of the transformation programme is now a normal part of how we operate. As such we expect it will continue to deliver earnings improvements in future years.

Directors' report

This annual result includes the annual non-cash revaluation of the biological bull team, required under accounting standards to reflect “fair value”. The valuation of the bull team is based on a model designed independently of LIC that looks at future revenue streams and costs associated with the current bulls owned, discounted back to current value. The 2017-18 financial year saw the valuation of the team increase slightly, after a significant increase the year prior. This reflects increased confidence for future year’s milk price and confidence from farmers, in NZ and internationally in LIC genetics, as well as cost efficiencies.

Other business highlights for the year included the launch of a new pasture management service SPACE™ which utilises satellite technology to estimate a farm’s pasture cover.

Investor communications

This year the Board has also reviewed how we communicate with you and how we can make our shareholder communications more engaging and easier to understand.

As a result of this work the Annual Report has been significantly reduced in length and a greater focus put on key details and making it easier to read. We have also introduced an online microsite for the first time to showcase the year’s financial results and highlights at ayearinreview.lic.co.nz

Strategy refresh

During the year there has also been a full refresh undertaken of LIC’s strategy to ensure it remains fit for purpose and aligned with the co-operative’s direction. The refreshed strategy reiterates that our growth will be innovation-led but with an ongoing focus on the core New Zealand dairy industry.

A summary of the strategy is on the LIC website (www.lic.co.nz > About > Our Strategy).

Mycoplasma bovis (M. bovis)

A major focus for all of us in recent months has been the presence of M. bovis in New Zealand. It is a significant concern for everyone in the dairy industry.

LIC is taking all measures possible to protect the national herd from this disease and we are working closely with MPI in this process. We have extensively tested our bulls and found no sign or indication of M. bovis. We are taking nothing for granted but we are confident that the measures we have in place will protect our bulls and customers from the disease.

Outlook

The increased revenue position in the 2017-18 financial year was driven by the success of the transformation programme. However NPAT is lower as it includes the one-off implementation costs of the programme. These costs will not be incurred in years ahead, so a stronger reported EBITDA and reported EBIT is expected next financial year.

LIC expects underlying earnings for the 2018-19 financial year to be in the range of \$18-22 million, assuming no significant climate event or milk price drop takes place between now and then nor any major impacts from M. bovis.

Thank you for all your support over the last year.

We look forward to another positive and busy twelve months.

Governance report

Role of Board of Directors

The Board is responsible for the direction and control of LIC's activities. It is committed to the Company's vision to improve the prosperity and productivity of our farmers and the guiding values of the Company of integrity, innovation and being in tune with customers. Legislation, the NZAX Listing Rules and the Constitution establish the Board's responsibility and include provisions for how the Co-operative will operate.

Responsibility

The Board is responsible for setting the strategic direction, approval of significant expenditures, policy determination and stewardship of the Co-operative's assets. The Board and the security holders shall not, except with the written consent of the Minister of Primary Industries, or other relevant Minister, exercise any of their rights, directions and powers under or alter the Constitution so as to cause or permit the Company to cease to be a Co-operative supplying goods and services to Shareholders.

Share simplification (Reclassification)

LIC's share capital is being reorganised and its constitution amended in July 2018 to reflect the share simplification approvals obtained at LIC's Special Meeting of Shareholders held on 14 March 2018. For further details, please refer to the document entitled Notice of Special Meeting and Explanatory Memorandum which can be found at www.lic.co.nz/shareholders. In July 2018, the share simplification will bring LIC's two classes of shares together into a single class of Ordinary Shares. Ordinary Shares will have both voting rights and the right to receive dividends based on the profits of the Company.

Co-operative principles

The Company is committed to the following co-operative principles:

- 1 The Company will remain a Co-operative Company;
- 2 The Company is controlled by Users of the Company's qualifying products and services;
- 3 Core products and services are made available to all Shareholders at fair commercial prices;
- 4 Products and services which benefit Shareholders and which otherwise might not be made available, are developed and made available to Shareholders, provided that the Company receives a commercial return; and
- 5 Shareholders co-operate with the Company and each other, including the sharing of information to promote their common interests.

Pricing of products and services

In setting prices to be paid for products and services, the Company should seek to create wealth for the Company and its Shareholders, supply products and services at commercial prices reflecting market conditions, taking into account the Company's co-operative principles and key strategic objectives set by the Board and approved by the Shareholder Council.

Principal activities

The Board has a responsibility to ensure the principal activities of the Company are the co-operative activities of supplying goods and services to its Shareholders with particular reference to:

- 1 Measurement and evaluation of growth, yield of milk or milk constituent and feed conversion efficiency of livestock, and any other relevant decisions on breeding and management of livestock;
- 2 The development and commercial application of artificial breeding for livestock; and
- 3 Improvement of livestock and farm management practices through products based on genetics, biotechnology, automation, information and advice.

Board composition

The Board of LIC is comprised of seven Elected Directors elected by the Co-operative Control Shareholders (or, following Reclassification, Ordinary Shareholders) within the region each Director represents (four regions in total) and up to three Appointed Directors. Elected Directors hold office for a period of four years and Appointed Directors for up to three years. A retiring Director is eligible for re-election as a Director of the Company.

Governance report

Current Board

Elected Directors are Murray King (Chair), Gray Baldwin, Murray Jagger, David Jensen, Steve Poole (retired 31 May 2018), Matt Ross and Dr Alison Watters.

Appointed Directors are Tim Gibson, Abby Foote and Candace Kinser Reed.

Election of Directors

The Directors elected by the Central Region (Steve Poole and Dr Alison Watters) retired by rotation in 2018. Dr Watters being eligible, offered herself for re-election and Steve Poole retired. Three nominations were received for the two positions on the Board, resulting in Dr Watters being re-elected for a further four year term effective 1 June 2018 and Ben Dickie being elected by the Shareholders for a four year term, also effective 1 June 2018.

Appointed Director Abby Foote was due to retire, by rotation, in October 2017 and did seek re-election. Abby Foote was elected for a further three year term but has now resigned with effect from 17 October 2018.

Appointed Director Phil Lough was due to retire, by rotation, in October 2017 and did not seek re-election. Tim Gibson was elected on 25 October 2017 for a two year term.

Committees

The Board uses committees to facilitate effective decision-making.

Audit, Finance & Risk Committee

A Sub-Committee of the Parent Board, the Audit, Finance and Risk Committee ensures the Company complies with its audit, financial and risk management responsibilities. Up to six Directors are on the Committee, which is chaired by Appointed Director, Abby Foote.

The Audit Committee meets at least four times a year and met seven times in 2017/18.

Disclosure Committee

This Parent Board Sub-Committee assists the Board and Company in ensuring that all material information is identified, reported and reviewed by the Committee, and if required, disclosed in a timely manner to the NZX. The Committee comprises two Directors and Senior Executives and is chaired by the Chair of the Board, Murray King.

The Committee meets as and when required and met four times in 2017/18.

Remuneration and Appointment Committee

This Sub-Committee of the Parent Board comprises up to four Directors and is chaired by Appointed Director, Tim Gibson. The Committee approves appointments and terms of remuneration of the Chief Executive, oversees the people policies for LIC and it also considers, and if appropriate recommends to the Board, any wage and salary percentage adjustments for the Co-operative's employees.

The Committee meets at least four times a year and met four times in 2017/18.

Capital Structure Committee

This Sub-Committee of the Board was established to assist the Board through a review of LIC's capital structure. The Committee did not meet in 2017/18 as the review of LIC's capital structure, and the resulting share simplification proposal, was undertaken by the full board.

Meetings

The Board met nine times in 2017/18 with two additional strategy session days.

Policies

LIC has in place policies including safety and wellbeing, delegated authorities, a code of ethics, continuous disclosure, legislative compliance, risk management and charters/terms of reference for the Parent's Board and Board Sub-Committees.

Governance report

Share trading and disclosure

The Company has adopted a 'Share Trading and Disclosure Policy' for Directors, Councillors, Restricted Persons and other Employees wanting to deal in the securities of the Company.

The Policy outlines:

- (a) when Directors, Councillors, Restricted Persons and other Employees of the Company may deal in the securities of the Company;
- (b) procedures to reduce the risk of insider trading; and
- (c) disclosure requirements.

The Policy records the Company's procedures for compliance with the Financial Markets Conduct Act 2013 and other relevant legislation/regulation for the trading and disclosure of trading in the securities of the Company.

The Policy aims to protect Directors, Councillors, Restricted Persons and Employees, as well as the Company and the Company's shareholders, against acts of insider trading that could disadvantage holders of the Company's securities.

SHAREHOLDING

Co-operative Control Shares

An Elected Director shall hold the minimum Co-operative Control shareholding requirement (or, following Reclassification, the Shareholding Requirement in respect of Ordinary Shares).

Investment Shares

An Elected Director can hold Investment Shares in accordance with the Company's Constitution.

Interests Register

A Directors' Interest Register is maintained and Directors' interest in transactions during the financial year are outlined on page 20 of the report.

STATUTORY REQUIREMENTS

Nature of LIC Business

The Parent is primarily involved in the development, production and marketing of artificial breeding, genetics, farm software, farm automation and herd testing services in the New Zealand dairy industry, the control and maintenance of the LIC database and the execution of research relating to dairy herd improvement.

ENTRIES IN THE INTERESTS REGISTER

All Elected Directors of the Company are customers and shareholders of Livestock Improvement Corporation Limited and purchase products and services for their farming operations on an arms-length and ongoing basis.

Directorships and Memberships

Gray Baldwin:

Director of Ballance Agri-Nutrients Ltd, Trinity Lands Ltd and Longview Trust Board.

Abby Foote (until 17 October 2018):

Director of Z Energy Ltd and its subsidiaries, Museum of New Zealand Te Papa Tongarewa, Television New Zealand Limited and Sanford Ltd.

Tim Gibson:

Director of Miraka Ltd, Port Otago Ltd and subsidiaries, Skills International Ltd, Tuhana Consulting Ltd, Canarium Nut Company.

Murray Jagger:

Director of Co-operative Business New Zealand, Marsden Maritime Holdings Ltd and Northport Ltd.

David Jensen:

Director of Farmland Co-operative Society Limited, Expressway Orchards General Partnership, El Dorado Orchard General Partnership Ltd and Eastpack Ltd and a shareholder of Figured Limited.

Governance report

Directorships and Memberships (cont.)

Murray King:

Director of Waimea Community Dam Limited, Long Plantation Investments Limited, Callura Dairies Management Limited, Dry Steam Irrigation Company Limited, Waimea Irrigators Limited and New Zealand Dairy Dessert Company Limited.

Candace Kinser Reed:

Director of EROAD and Talent International. Advisor to Palantir Technologies, Beachhead Advisor for NZ Trade & Enterprise, advisory board member of University of Waikato Cyber Security Lab and BECA New Ventures Accelerator. Investment Committee Member to Return on Science Investment Scheme at the University of Auckland.

Steve Poole (retired 31 May 2018):

Director and owner of Poole Brothers Limited, Director of La Salle House Limited. Trustee of Dairy Trust Taranaki.

Matt Ross:

Director of Bortons Agri Ltd and North Otago Irrigation Company Ltd.

Dr Alison Watters:

Director ofASUREQuality Ltd. Shareholder (27.66%) of AgInvest Holdings Limited (AgInvest owns MyFarm Limited).

ENTRIES IN THE INTEREST REGISTER

Calf sales

Participation in the Company's Contract Mating Scheme could lead to the potential sale of bull calves in the 2018/2019 season. Directors participating in the scheme include:

Director	Potential calf sales	Potential value
Matt Ross	8	\$ 88,000
Murray Jagger	3	\$ 33,000

(a) Share Dealings by Directors

As at 31 May 2018, the following Directors, (either in their own names and/or in the name(s) of their dairy farming entities) as qualifying users of LIC's products and services, are holders of the following shares:

Director	2018		2017	
	Co-operative	Investment	Co-operative	Investment
Gray Baldwin	4,356	-	3,028	-
Murray Jagger	1,414	21,967	1,540	21,967
David Jensen	1,442	2,710	1,335	2,710
Murray King	3,465	24,353	3,962	22,861
Steve Poole	2,217	18,939	1,988	18,939
Matt Ross	4,265	17,769	4,652	17,769
Alison Watters	811	7,428	754	7,428

Any increase in holdings of Investment Shares results from participation in LIC's Voluntary Investment Scheme.

(b) Loans to Directors of the Parent and Subsidiaries

There have been no loans during the year.

(c) Directors Indemnity and Insurance

The Parent has issued a Deed of Indemnity and insured all its Directors and Senior Managers against liabilities to third parties for any acts or omissions in their capacity as Directors of the Company and its Related Parties.

(d) Use of Company Information

There were no notices from Directors of the Company requesting to use Company Information received in their capacity as Directors, which would not otherwise have been available to them.

Governance report

DIRECTORS AND REMUNERATION

Directors of the Company received the following remuneration for the twelve months ending 31 May 2018:

In thousands of New Zealand dollars

	Fees
M King	119
G Baldwin	50
A Foote	69
T Gibson	40
M Jagger	50
D Jensen	50
C Kinser Reed	63
P Lough	26
S Poole	50
M Ross	50
A Watters	50
	<hr/>
	617

Directors of subsidiaries of the Company received the following remuneration for the twelve months ending 31 May 2018:

In thousands of New Zealand dollars

	Fees
R Dungey	32
E Ruiz	12
	<hr/>
	44

Except as set out above, no other Directors of subsidiaries received any remuneration or other benefits in their role as a Director of that subsidiary. The remuneration of employees that receive more than \$100,000 as a result of employee remuneration (and other benefits) is included in the Employees' Remuneration table on page 22. The Directors of the Company's subsidiaries are set out below:

LIC Agritechnology Company Limited: Murray King, Gray Baldwin, Abby Foote, Tim Gibson, Murray Jagger, David Jensen, Candace Kinser Reed, Steven Poole, Matt Ross and Alison Watters

Livestock Improvement (NZ) Corporation Limited: Linda Cooper, Murray King and Wayne McNee

LIC Deer Limited: Linda Cooper, Geoffrey Corbett and Wayne McNee

Animal Breeding Services Limited: Linda Cooper and Wayne McNee

LIC Automation Limited: Wayne McNee

LIC Johnes Company Limited: Linda Cooper, Wayne McNee and Richard Spelman

LIC Ventures No.3 Limited: Paul Littlefair and Wayne McNee

Livestock Improvement Pty Limited: Geoffrey Corbett, Andrew Fear, Mike Rose

Farmkeeper Pty Limited: Geoffrey Corbett, Andrew Fear and Mike Rose

Overland Corner Holdings Pty Limited: Geoffrey Corbett, Andrew Fear and Mike Rose

Beacon Automation Pty Limited: Linda Cooper, Jock Roberts and Geoffrey Corbett

Livestock Improvement Corporation (UK) Limited: Linda Cooper, Wayne McNee and Mark Ryder

LIC USA Limited: Linda Cooper and Wayne McNee

LIC Automation USA Limited: Geoffrey Corbett and Wayne McNee

LIC Ireland Limited: Linda Cooper, Mark Ryder and Wayne McNee

NZ Brasil Producao Animal Ltda: Linda Cooper and Simon O'Connor

In addition to the departures of Steven Poole and Abby Foote (noted above), Andrew Fear and Linda Cooper have also resigned effective 15 June 2018 and 17 August 2018 respectively.

Governance report

Employees' Remuneration

During the period 1 June 2017 to 31 May 2018 the following numbers of employees (not being Directors) received total remuneration, including benefits, of at least \$100,000:

Remuneration Range (Gross)	Returning	Cessations	Total
100,000 – 109,999	51		51
110,000 – 119,999	32	2	34
120,000 – 129,999	23	5	28
130,000 – 139,999	15	3	18
140,000 – 149,999	6	1	7
150,000 – 159,999	2	2	4
160,000 – 169,999	11	1	12
170,000 – 179,999	4	-	4
180,000 – 189,999	9	1	10
190,000 – 199,999	8	1	9
200,000 – 209,999	4		4
210,000 – 219,999	4		4
220,000 – 229,999	2	1	3
230,000 – 239,999	2	1	3
250,000 – 259,000	1		1
270,000 – 279,999	-	1	1
280,000 – 289,999	1		1
290,000 – 299,999	1		1
300,000 – 309,999	2		2
310,000 – 319,999	1		1
350,000 – 359,999	1		1
370,000 – 379,999	1		1
470,000 – 479,999	1		1
1,070,000 – 1,079,999 ¹	1		1
Total	183	19	202

¹ Payments to the employee in the top band include two years of performance bonuses due to timing only, compared to only one year's performance bonus in the prior year. Without the May 2018 bonus payment, this band would be similar to last year's band.

RESOLUTION OF DIRECTORS DATED 18 JULY 2018 CONFIRMING THE CO-OPERATIVE STATUS OF LIVESTOCK IMPROVEMENT CORPORATION LIMITED

RESOLVED THAT:

Livestock Improvement Corporation Limited (Company) was registered as a Co-operative Company under the provisions of the Co-operative Companies Act 1996 (Act) on 1 March 2002.

In the opinion of the Board of Directors, the Company has been a Co-operative Company from that date to the end of the accounting year ended 31 May 2018.

The grounds for this opinion are:

- 1) The principal activity of the Company involves supplying artificial breeding, herd testing, herd recording and other services to transacting Shareholders (as that term is defined in section 4 of the Act). Accordingly, the principal activity of the Company is, and is stated in the Constitution of the Company as being, a Co-operative activity (as the term is defined in section 3 of the Act); and
- 2) Not less than 60 percent of the voting rights attached to shares in the Company are held by transacting Shareholders.

Governance report

Spread of Investment Shareholders as at 31 May 2018

(excluding treasury stock)

Size of shareholding	Number of Shareholders	Investment Shares held	% of Total
1-999	1,460	600,010	2.13
1,000-1,999	1,169	1,759,351	6.24
2,000-2,999	1,111	2,735,321	9.70
3,000-3,999	732	2,542,114	9.02
4,000-4,999	535	2,380,865	8.44
5,000-9,999	1,123	7,806,338	27.69
Over 10,000	509	10,370,195	36.78
Total	6,639	28,194,194	100.00

Twenty Largest Shareholdings of Quoted Securities

(excluding treasury stock)

	Investment Shares held	% of Total
Trinity Lands Ltd	467,376	1.66
Custodial Services Ltd	236,992	0.84
Schmidt Farms Ltd	175,309	0.62
Christopher John Stark & Graham Carr	174,743	0.62
Sim Brothers Ltd	150,000	0.53
Mark Francis Slee & Devon Mathieson Slee	142,569	0.51
Wills Group Ltd	127,039	0.45
Malrose Properties Ltd	101,756	0.36
Farnley Tyas Farms Ltd	93,188	0.33
Laird Farm Ltd	90,164	0.32
Landcorp Farming Ltd	87,844	0.31
Bishop Farms Oxford Ltd	87,427	0.31
The Grass Market Company Ltd	74,630	0.26
Cornelis Smit & Donna Maree Smit & Sharp Tudhope Trustee Services Ltd	71,076	0.25
Kodie Farms Ltd	67,713	0.24
Magatarata Farms Ltd	67,449	0.24
Broad Acres Farms Ltd	63,494	0.23
Gillian Patricia Alice Gow & James Platt Gow & Matthew Platt Gow	60,993	0.22
South Hilton Ltd	54,067	0.19
Stuart Bruce Bay & Doris Beth Bay	53,822	0.19
		8.68

Credit Rating Status

The Co-operative currently does not have a credit rating.

Substantial Security Holders

As at 31 May 2018, no persons have notified the Company that they are substantial product holders of the Company as referred to in Section 274 of the Financial Markets Conduct Act 2013.

Donations

The Company made donations totalling \$11,792 during the year ended 31 May 2018 (2017: \$26,047).

Governance report

Non-Standard Listing

Livestock Improvement Corporation Limited has been classified as a Non-Standard NZAX Issuer by the NZX, pursuant to NZAX Listing Rule 5.1.3, by reason of it being a Co-operative Company having a Constitution which includes provisions having the following effect:

The acquiring of Investment Shares is restricted to New Zealand dairy farmers who hold Co-operative Control Shares and who purchase qualifying products and services from Livestock Improvement Corporation Limited; and

Holders of Investment Shares have no voting rights (except on matters affecting the rights of Investment Shareholders).

Following the Reclassification, all shares in the Company will become Ordinary Shares. The acquiring of Ordinary Shares will be restricted to New Zealand dairy farmers who satisfy the shareholding requirements under the Constitution of LIC.

As part of the Reclassification, NZX has granted a number of waivers to allow LIC to operate as a Co-operative Company. Details of these waivers are included below.

WAIVERS AND APPROVALS GRANTED BY NEW ZEALAND EXCHANGE LIMITED ("NZX") IN THE PROCESS OF THE APPROVAL OF THE CONSTITUTION OF LIVESTOCK IMPROVEMENT CORPORATION LIMITED

Waivers and approvals have been granted in respect of the following NZAX Listing Rules:

- 1 Rule 1.6.1 (previously Rule 1.1.2) in respect of the definition of "Renounceable" to refer to a Right or offer that is transferrable to any person who is entitled to hold the Securities to which the Right or offer relates.
- 2 Rule 3.2.2 to allow for the following aspects of the Company's corporate governance structure:
 - (a) Directors to be nominated by Co-operative Control Shareholders, by region, pursuant to clause 25.4(b) and Schedule 3 of the Constitution;
 - (b) Certain qualifications to be required of directors as set out in paragraphs 1(a) and 2 of Schedule 3 of the Constitution;
 - (c) The nomination procedure for directors as set out in paragraph 1(b) of Schedule 3 of the Constitution.
- 3 Rule 3.2.3 to permit the provisions of paragraph 1(e) of Schedule 3 of the Constitution to allow for the filling of casual vacancies by the Board, where the position becomes vacant less than 8 months before the date on which the director is due to retire by way of rotation.
- 4 Rule 3.2.6 to allow for the rotation of Elected Directors as set out in clause 26 and clauses 1(c) and (d) of Schedule 3 of the Constitution whereby Elected Directors are due to retire on the 1st day of June in each year, on a regional basis, so that a rotation schedule of 4 years for Elected Directors is permitted.
- 5 Rule 7.6.3 to allow clause 3.6.2 of the Constitution to permit financial assistance to be given to an Approved Holding Entity.
- 6 Rule 8.2.1 is not applicable in the case of LIC, given its status as a Non-Standard NZAX Issuer, and as such LIC is not required to comply with the restrictions of that Rule, so that clause 20 of the Constitution (which provides for a more extensive lien on Securities) is allowed.
- 7 Rule 11.1.5 allows an NZAX Issuer to include restrictions on the issue, acquisition or transfer of Equity Securities in its Constitution, subject to the prior approval of NZX. Restrictions in the Constitution requiring approval from NZX are as follows:
 - (a) Clause 3.2.2 of the Constitution restricts the issue of Voting Securities with the aim of ensuring that LIC remains a co-operative company controlled by its Co-operative Control Shareholders (whose control is directly proportionate to the amount of products and services purchased by each such shareholder);
 - (b) Clause 3.2.3 of the Constitution restricts the issue and transfer of Securities so that they are only held by Users or Employee Scheme Holders (or by other persons in certain specified circumstances). Again, this aims to protect the fundamental nature of a co-operative company;
 - (c) Clause 3.2.3A of the Constitution prohibits third party interests by prohibiting a Shareholder from holding Shares on behalf of any person who is not a User (subject to exceptions in the case of Family Trusts and the Employee Share Purchase Scheme);
 - (d) Clauses 10.1(b) and (d) of the Constitution place restrictions on the persons who may hold Investment Shares so that such shares are only held by a Co-operative Control Shareholder, or the Company, or Approved Holding Entity, or an Employee Scheme Holder (or by other persons in certain limited specified circumstances);

WAIVERS AND APPROVALS GRANTED BY NEW ZEALAND EXCHANGE LIMITED (“NZX”) IN THE PROCESS OF THE APPROVAL OF THE CONSTITUTION OF LIVESTOCK IMPROVEMENT CORPORATION LIMITED (cont.)

- (e) Clauses 10.2 to 10.7 (inclusive) of the Constitution place restrictions on how Investment Shares may be held. Clause 10.3 imposes a Maximum Investment Shareholding of not more than 5 percent of the total number of Investment Shares currently on issue. Clause 10.4 provides for disposal of Investment Shares upon a person ceasing to be a Co-operative Control Shareholder. Clause 10.6 permits an Approved Holding Entity to hold Investment Shares to administer any Voluntary Investment Scheme and Dividend Reinvestment Plan. Clause 10.7 provides for shares to be held in Brokers’ Accounts;
 - (f) Clause 10.8 of the Constitution authorises the Board to establish an Employee Share Purchase Scheme which may hold up to 5 percent of the total number of Investment Shares currently on issue;
 - (g) Clause 13.5 of the Constitution permits the Board to refuse to register transfers of Investment Shares where the transfer would breach the restrictions referred to in paragraph 7(e), or would otherwise be in breach of the Constitution, and clause 13.5A empowers the Board to require proof that shares are not being acquired for the benefit of third parties;
 - (h) The consent of the Minister for Primary Industries (or other relevant Minister) is required under the Dairy Industry Restructuring Act 2001 to any changes to who may hold shares, maximum voting rights and postal voting and this requirement must therefore take precedence over all other provisions in the Constitution and the Listing Rules.
- 8 NZX has approved differences in text between certain Listing Rules and the provisions of the Constitution as follows:
- (a) The definition in clause 2.1 of “Average Market Capitalisation” has been amended to take account of the fact that it is only the Investment Shares, which will have a market capitalisation value, and therefore the nominal value of the Co-operative Control Shares will be added to that value. This definition is relevant in relation to section 9 of the Listing Rules in relation to Major Transactions and Material Transactions;
 - (b) Clause 3.5.1(a) of the Constitution reflects Rule 7.3.1(a). However that Rule only requires approval to be given by the classes of Quoted Equity Securities. As the Investment Shares are the only class of shares quoted, the definition in the Constitution excludes the word “Quoted”, so that under clause 3.5.1(a) the approval of each class of Equity Securities is required regardless of whether or not they are Quoted;
 - (c) Clause 3.5.2(a) of the Constitution provides for the reference in Rule 7.3.1(a) to “Quoted Equity Securities” to be deemed a reference to “Equity Securities”, as the Co-operative Control Shares are not Quoted;
 - (d) Clause 3.5.2(b) of the Constitution provides for the reference in Rule 7.3.4(c) to “Equity Securities carrying Votes” to be deemed a reference to “Investment Shares” as Investment Shares do not have voting rights (except in very limited circumstances);
 - (e) Paragraph 6.1 of Schedule 1 of the Constitution reflects Rule 6.2.5; however it applies to notices of meetings of Shareholders rather than of Quoted Security holders.

WAIVERS AND APPROVALS GRANTED BY NEW ZEALAND EXCHANGE LIMITED (“NZX”) IN THE PROCESS OF THE APPROVAL OF THE CONSTITUTION OF LIVESTOCK IMPROVEMENT CORPORATION LIMITED AND THE RECLASSIFICATION OF LIC SHARES

Waivers and approvals have been granted in respect of the following NZAX Listing Rules

- 1 Rule 1.6.1 in respect of the definition of “Renounceable” to refer to a Right or offer that is transferrable to any person who is entitled to hold the Securities to which the Right or offer relates. This reflects the ownership restrictions on Shares, as a result of the co-operative nature of LIC.
- 2 Rule 3.2.2 to allow for the following aspects of the Company’s corporate governance structure:
 - (a) Directors to be nominated by Ordinary Shareholders, by region, pursuant to clause 22.4(b) and Schedule 3 of the Constitution;
 - (b) Certain qualifications to be required of directors as set out in Schedule 3 of the Constitution;
 - (c) The nomination procedure for directors as set out in Schedule 3 of the Constitution.
- 3 Rule 3.2.3 to permit the provisions of Schedule 3 of the Constitution to allow Elected Directors appointed on a casual basis by LIC’s Board to stand for re-election on the first day of June next occurring, as set out in schedule 3 of LIC’s Constitution.
- 4 Rule 3.2.6 to allow Elected Directors to retire by rotation on the first day of June each year, four years following their appointment, as set out in clause 23 and schedule 3 of LIC’s Constitution.
- 5 Rules 3.2.3 and 3.2.6, to allow Appointed Directors to be appointed, to have their appointment ratified and to retire, as set out in schedule 3 of LIC’s Constitution.
- 6 Rule 7.3.11 to allow LIC to issue new shares to a Shareholder in order to ensure they meet the Share Standard. The waiver treats the Share Standard as the “Minimum Holding” requirement for LIC for the purposes of the Listing Rules.
- 7 Rule 7.6.3 to allow clause 3.6.2 of the Constitution to permit financial assistance to be given to an Approved Holding Entity. The Approved Holding Entity acquires Shares in LIC on behalf of Shareholders in administering a voluntary investment scheme and/or dividend reinvestment plan approved by the Board.
- 8 Rule 7.6.9 to allow LIC to buy back shares from an exiting Shareholders as a “routine” buy back.
- 9 Rule 8.1.3 to allow the Nil Paid Ordinary Shares to carry full voting rights. Without this waiver, the Nil Paid Shares could only carry voting rights in proportion to which the Share is paid up.
- 10 Rule 8.2.1 is not applicable in the case of LIC, given its status as a Non-Standard NZAX Issuer, and as such LIC is not required to comply with the restrictions of that Rule, so that clause 18 of the Constitution (which provides for a more extensive lien on Securities) is allowed.
- 11 Rule 11.1.5 allows an NZAX Issuer to include restrictions on the issue, acquisition or transfer of shares in its Constitution, subject to the prior approval of NZX. Restrictions in the Constitution approved by the NZX are as follows:
 - (a) Clause 3.2.2 of the Constitution restricts the issue of Voting Securities with the aim of ensuring that LIC remains a co-operative company controlled by its Shareholders;
 - (b) Clause 3.2.3 of the Constitution restricts the issue and transfer of Securities so that they are only held by Users or Employee Scheme Holders (or by other persons in certain specified circumstances). Again, this aims to protect the fundamental nature of a co-operative company;
 - (c) Clause 3.2.3A of the Constitution prohibits third party interests by prohibiting a Shareholder from holding Shares on behalf of any person who is not a User (subject to exceptions in the case of Family Trusts and the Employee Share Purchase Scheme);
 - (d) Clause 6.3(a) of the Constitution prohibits a person from holding a relevant interest in more than 5% of the total number of Ordinary Shares in LIC on issue;
 - (e) Clause 7.1 of the Constitution may require Users who have spent in excess of the Minimum Purchase Amount to compulsorily acquire sufficient Ordinary Shares to meet the Shareholding Requirement;
 - (f) Clause 7.2 of the Constitution may require Users who no longer spend the Minimum Purchase Amount to compulsorily dispose of their Ordinary Shares; and
 - (g) Clause 20.4 of the Constitution restricts voting rights in LIC so that no person can exercise, or control the exercise of, more than 1% of the maximum number of votes exercisable at any meeting of LIC while the Dairy Industry Restructure Act 2001 is in force.

**DISCLOSURE OF FINANCIAL ASSISTANCE AS
REQUIRED UNDER THE COMPANIES ACT 1993**

- A LIC Employee Share Scheme:** LIC proposes to provide financial assistance to those employees who elect to participate in the LIC Employee Share Scheme ("Employee Scheme") which from the 1 April 2011 has been managed by Craigs Investment Partners Limited ("Craigs"), with Custodial Services Limited acting as custodian. LIC proposes to pay the Manager's and Custodian's fees and expenses (including brokerage). The amount of the Manager's fee will depend on how many employees participate in the Employee Scheme and the level of their contribution. An estimate of the amount of the financial assistance is \$24,000.

The Board of LIC resolved on 18 July 2018 that LIC should provide the financial assistance referred to above ("Employee Scheme Assistance") for the period of 12 months commencing 10 working days after the date of sending this disclosure to Shareholders, and that the giving of the Employee Scheme Assistance is in the best interests of LIC, and is of benefit to Shareholders not receiving that financial assistance; and that the terms and conditions under which the Employee Scheme Assistance is given are fair and reasonable, to LIC, and to the Shareholders not receiving that financial assistance. The grounds for the Board's conclusions are:

- (a) The Employee Scheme will be a valuable addition to the benefits available to the employees of LIC and will assist in retaining them as valuable staff;
- (b) The Employee Scheme is a method of aligning the interests of employees with the interests of Shareholders and is an effective means of motivating future performance of the employees. This is expected to bring about an increase in the value of the Investment Shares;
- (c) Shareholders will not be diluted or otherwise disadvantaged as no new shares are being issued under the Employee Scheme;
- (d) The additional shares will be purchased through Craigs at the NZAX market price;
- (e) The Employee Scheme will enhance the liquidity in the market for the shares, providing a more liquid market for Shareholders wishing to sell those Shares;

The amount of financial assistance is minimal in comparison to the benefits arising out of the Employee Scheme for Shareholders and LIC.