INVESTMENT AND LIABILITY POLICY

CATEGORY:	Finance	**STATUS:**	Adopted
DATE POLICY ADOPTED:	5 August 2015 (as part of LTP 2015-2025 document)	**APPROVAL BY:**	Council
REVIEW PERIOD:	3 years	**NEXT REVIEW DUE BY:**	2018
DATE PREVIOUSLY ADOPTED:	Not applicable	**REVISION NUMBER:**	0

1. POLICY OBJECTIVES

The Council has Treasury risks arising from debt raising, investments and associated interest rate management activity and the Council wishes to minimise that risk.

Treasury activities are:

- Compliance with the Local Government Act 2002[1];
- Provide linkage to the Council's financial strategy;
- Develop and maintain professional relationships with the financial markets;
- Invest surplus cash in liquid and creditworthy investments;
- Raise appropriate finance, in terms of both maturity and interest rate; and,
- Manage the overall cash position of the Council's operations.

2. GENERAL APPROACH

The Council seeks to minimise risk from its Treasury activities;

- Activity which may be construed as speculative in nature is expressly forbidden; and,
- The Council manages both liabilities and cash investments through an internal Treasury activity. Funds are advanced by the Treasury activity for a specific period. Loans are repaid to the Treasury activity based on standard loan lives, depending on the useful lives of the assets.

<u>Calculation of interest</u>

- Interest for loans is based on the Council's weighted cost of funds; and,
- Interest is credited to activities based on investment rates.

3. LIABILITY MANAGEMENT POLICY (S.102(2)(B))

The Council approves borrowing by resolution during the Annual Planning process.

The Council raises borrowing for the following primary purposes:

- General debt to fund the Council's Balance Sheet;

[1] Sections 104 & 105 set out the required contents of the Liability Management Policy and the Investment Policy required by s.102(2)(b) & (c).

- Specific debt associated with "special one-off" projects and capital expenditure; and,
- To fund assets with inter-generational qualities consistent with Council's Revenue and Financing Policy.

3.1 SPECIFIC BORROWING LIMITS

In managing borrowing, the Council will adhere to the following limits:

- The net interest expense of all external borrowings will not exceed 10% of total revenues;
- The net interest expense of all external borrowings will not exceed 7.5% of annual rates revenue;
- Liquid ratio of ≥ 1:1;
- Current ratio ≥ 1.25; and,
- The percentage of net external debt to total revenue to be less than 100%.

'Revenue' - is defined as earnings from rates, government grants and subsidies, user charges, interest and other revenue.

'Liquidity ratio' - is defined as (term debt plus committed loan facilities less liquid investments divided by current external debt) to be greater than 110%.

'Rates' - is defined as all income under the Local Government (Rating) Act 2002.

'Total revenue' - for the purposes of this policy includes: earnings from rates revenue; grants and subsidies; user charges; interest and other operating revenue (excluding vested assets).

3.2 LIQUIDITY AND CREDIT RISK MANAGEMENT

The Council's ability to readily attract cost-effective borrowing is largely driven by its ability to maintain a strong balance sheet, as well as its ability to rate, manage its image in the market and its relationships with bankers. Where possible, the Council seeks a diversified pool of stock and bank borrowing and ensures that bank borrowings are only sought from the approved list of registered banks.

To minimise the risk of large concentrations of debt maturing or being reissued in periods where credit margins are high for reasons within or beyond the Council's control, the Council ensures debt maturity is spread widely over a band of maturities. The Council manages this specifically by ensuring that: no more than 35% of total borrowing is subject to refinancing in any financial year unless total borrowing is less than $7.5 million. Total borrowing includes any forecast external borrowing.

3.3 NEW ZEALAND LOCAL GOVERNMENT FUNDING AGENCY LIMITED INVESTMENT

The Council may borrow from the New Zealand Local Government Funding Agency Limited (LGFA), and in connection with that borrowing, may enter into the transaction to the extent it considers necessary or desirable to secure its borrowing from the LGFA, and the performance of other obligations to the LGFA or its creditors with a charge over the Council's rates and rates revenue.

3.4 RISK RECOGNITION

- Local government risk is priced to a higher fee and margin level;
- The Council's own financial strength as a borrower, deteriorates due to financial, regulatory or other reasons;
- A large individual lender to the Council experiences its own financial/ exposure difficulties, resulting in the Council not being able to manage their debt portfolio as optimally as desired; and,
- New Zealand investment community experiences a substantial "over supply" of Council investment assets.

A key factor of funding risk management is to spread and control the risk to reduce the concentration of risk at one point in time. This is so that if any of the above events occur, the overall borrowing cost is not unnecessarily increased and the desired maturity profile is not compromised due to market conditions.

3.5 LIQUIDITY/FUNDING RISK CONTROL LIMITS (BORROWINGS)

- Term debt and committed debt facilities must be maintained at an amount that averages 115% of projected peak net debt levels over the next year (per long term cash and debt forecasts);
- Disaster recovery requirements are met through the liquidity ratio; and,
- The maturity profile of the total committed funding in respect to all loans and committed facilities is to be controlled by the following system:

PERIOD	MINIMUM	MAXIMUM
0 to 3 years	15%	60%
3 to 5 years	15%	60%
5 years plus	10%	40%

- A maturity schedule outside these limits requires specific Council approval. A 12-month phase-in, non-compliance period is permitted.

3.6 INTEREST RATE RISK MANAGEMENT

The Council's borrowing gives rise to direct exposure to interest rate movements. Generally, given the long-term nature of Council's assets, projects and inter-generational factors and Council's preference to avoid an adverse impact on rates, there is a general tendency to have a high percentage of long-term fixed rate or hedged borrowing.

3.7 APPROVED FINANCIAL INSTRUMENTS

Dealing in interest rate products must be limited to financial instruments approved by the Council. Any other financial instrument must be specifically approved by Council on a case-by-case basis and only be applied to the one singular transaction being approved.

CATEGORY	INSTRUMENT
Cash management and borrowing	Bank overdraft. Committed cash advance and bank accepted bill facilities (term facilities).
Interest rate risk Management	Uncommitted money market facilities Stock/Bonds issuance. Forward rate agreements ('FRAs') on: • Bank bills; and, • Government bonds.
	Interest rate swaps including: • Forward start swaps (start date <24 months); and, • Amortising swaps (whereby notional principal amount reduces).
	Interest rate options on: • Bank bills (purchased caps and one for one dollars); and, • Government bonds.
	• Interest rate swaps (purchased only).

3.8 INTEREST RATE RISK CONTROL LIMITS

Debt/borrowings

The Council debt/borrowings/financial risk management instruments must be within the following fixed/floating interest rate risk control limit:

MASTER FIXED/FLOATING RISK CONTROL LIMIT	
MINIMUM FIXED RATE	MAXIMUM FIXED RATE
50%	95%

- 'Fixed Rate' is defined as an interest rate re-pricing date beyond 12 months forward on a continuous rolling basis;

- ‘Floating Rate’ is defined as an interest rate re-pricing within 12 months; and,
- The fixed rate amount at any point in time must be within the following maturity bands.

4. INVESTMENT POLICY (S.102(2)(C))

4.1 THE COUNCIL MAINTAINS INVESTMENTS IN THE FOLLOWING FINANCIAL ASSETS:

- Equity investments including shareholdings and loan advances to trading and service enterprises, charitable trusts and incorporated societies; for example sporting and community organisations;
- Property investments, including land and buildings; and,
- Treasury instruments incorporating longer term and liquidity investments.

4.2 EQUITY INVESTMENTS AND LOAN ADVANCES

Investments include shareholdings in trading and service enterprises and loan advances to charitable trusts, incorporated societies, residential and rural housing which are consistent with the Council’s Long Term Plan. The Council operates an internal borrowing system for funding infrastructural improvements as well as funding current accounts. This information is reported to the Finance, Audit and Risk Committee on a quarterly basis.

Advances and loans are only provided to organisations where the Council has significant interest. In default, the assets of the organisation may not revert to the Council, however personal guarantees are obtained from the principals of the organisation.

4.3 QUALITY ROADING SERVICES (WAIROA) LTD.

The Council owns 100% of the shares of QRS which was set up as a Local Authority Trading Enterprise, and is now classified as a CCO. The company is a contractor providing construction, forestry, quarrying, reserves and utility services mainly in the Wairoa district.

The strategic objectives in owning QRS are to reduce costs and provide greater competition in tendering for construction, roading and maintenance work, to provide revenue by way of dividends to offset overheads, and to maintain employment levels and expertise in contracting within Wairoa District.

Dividends of 40% of the after-tax paid profit are paid to the Wairoa District Council, with payments made after reporting of the six-month and annual result.

In order to achieve the strategic objectives, the Council requires regular reporting of financial and non-financial results against target, including a statement of corporate intent, half-yearly financial statements, and annual financial statements. The Council appoints appropriately qualified directors to manage the business, and ensures that proper governance procedures are in place.

The Council appoints the board of QRS and annually approves the Statement of Corporate Intent. The Council also monitors the performance by reviewing the six-monthly accounts, and annual accounts.

4.4 TREASURY INVESTMENTS

The Council maintains treasury investments for the following primary reasons:

- Provide ready cash in the event of a natural disaster. This cash is intended to bridge the gap between the disaster and the reinstatement of normal income streams and assets;
- Invest amounts allocated to accumulated surplus, the Council created and restricted reserves, and general reserves;
- Invest funds allocated for approved future expenditure, to implement strategic initiatives or to support inter-generational allocations;
- Invest proceeds from the sale of assets; and,
- Invest surplus cash and working capital funds.

<u>Treasury investment objectives</u>
The Council’s primary objective when investing is the protection of its investment. Accordingly, only creditworthy counterparties are acceptable.

The Council also seeks to:

- Maximise investment return;
- Ensure investments are liquid; and,
- Manage potential capital losses due to interest rate movements if investments need to be liquidated before maturity.

Credit risk is minimised by limiting investments to registered banks, strongly rated State Owned Enterprises (SOE) and corporates within prescribed limits.

Liquidity risk is minimised by ensuring that all investments must be capable of being liquidated in a readily available secondary market. Where practical, the Council maintains $1 million of its investments with a maturity less than one year.

4.5 INTEREST RATE RISK MANAGEMENT

The Council's investments give rise to a direct exposure to a change in interest rates, impacting the return and capital value of its fixed rate investments.

Interest rate risk will be managed by reviewing rolling cash flow forecasts and using risk management instruments to protect investment returns and/ or to change interest rate and maturity profile.

4.6 ACQUISITION AND DISPOSAL OF ASSETS

Any disposal of assets requires the approval of the Council except those assets within delegated authority.

5. DEVELOPMENT AND FINANCIAL CONTRIBUTIONS POLICY (S.102(2)(D))

The Local Government Act 2002 provides for local authorities to recover, through development contributions, capital expenditure related to growth. Councils may require development contributions from developments where the effect, including the cumulative effect, of development is to require new or additional assets or assets of increased capacity, and as a consequence, the Council incurs capital expenditure. This includes capital expenditure Council has already incurred in anticipation of growth.

Significant growth in services resulting from a population increase is not foreseen in Wairoa District over the ten year period, therefore the Council has chosen not to take development contributions as a form of revenue at this time.

Financial Contributions can be provided for in a council's district plan. Contributions may be imposed as a condition of development or resource consent. Currently the Council has no Financial Contributions, but the Council will consider Financial Contributions as part of the review for the next District Plan.