Investment and Liability Management Policy

Group Responsible: Chief Financial Officer

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1.0 Overview

The Local Government Act 2002 requires local authorities to adopt an Investment Policy and a Liability Management Policy.

The Investment Policy is designed to ensure that the financial resources of the Council are managed in an efficient and effective way. It sets out how Council can utilise funds from the sale of assets, what should be done with the investment income and so on.

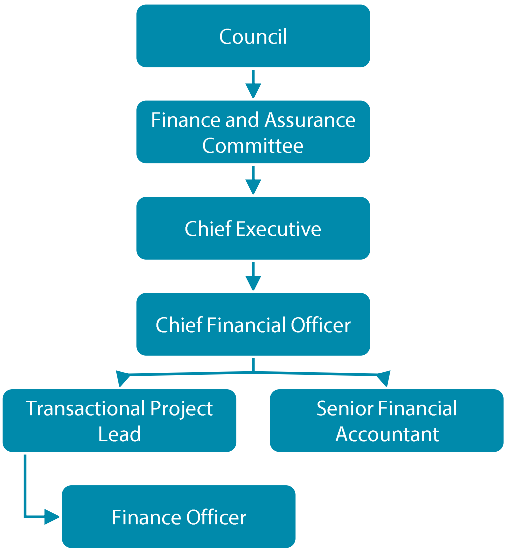
The Liability Management Policy is designed to provide a framework for prudent debt management and sets out how Council may wish to use debt as a funding mechanism.

Council has a structure of responsibilities and reporting lines to ensure the appropriate management and accountability of the liability and investing activities.

2.0 Structure

Organisational Structure

The organisational chart for the finance activity is as follows:



Responsibilities

The key responsibilities of the above positions are as follows:

Council

- approve, adopt and review the Policies including any revisions and amendments
- approve by resolution all external Council borrowing outside of that noted in the long term plan
- approve the external managed fund and the appointment of any fund managers
- approve amount of funds to be placed with external managed fund
- approve membership to Local Government Funding Agency (LGFA) including CCO/CCTOs.

Finance and Assurance Committee

- oversee the treasury function of Council ensuring compliance with the relevant Council policies and plans
- ensuring compliance with the requirements of Council's trust deeds
- recommend to Council treasury policies at least every three years
- approving debt, interest rate and external investment management strategy.

Chief Executive (CE)

- ultimately responsible for ensuring the Policies adopted by Council are implemented by officers of Council and administered in accordance with their terms.

Chief Financial Officer (CFO)

- responsible for recommending investment, borrowing and risk management strategy in conjunction with relevant staff
- ensure compliance with any relevant strategies
- responsible for determining the level of cash available for investment and that held for working capital purposes
- execute the external investment management and interest rate strategy
- approve amounts to be placed with an external fund manager for investment purposes within that set within the Annual Plan or Long Term plan or by way of separate Council resolution
- recommend to Finance and Assurance Committee and Council amendments to the Policies as required
- recommend to Finance and Assurance Committee the debt, interest rate and external investment management strategy for approval
- review internal audit reports and ensure any recommendations agreed by the Finance and Assurance Committee are made
- approve new treasury investments ensuring the proposed investment complies with these policy documents
- receive managed fund reports and annually monitor performance and present the necessary reports to the Finance and Assurance Committee.

Transactional Project Lead

- responsible for confirming adherence to the policies, through internal reviews, to be performed on a regular basis and present a summarised report of compliance to the CFO
- responsible for recommending to the CFO the level of cash available for investment and that held for working capital purposes

- negotiate and undertake treasury investment and borrowing/funding transactions
- assist in identifying amendments to the investment, borrowing and risk management strategy, which may require amendment of the Policies
- responsible for all activities relating to the daily implementation and maintenance of the Policies
- assist in determining the most appropriate sources and terms for borrowing and investing
- responsible for keeping the CFO informed of significant activity and market trends
- responsible for reviewing/approving the weekly cashflow and cash management transaction requirements completed by the Senior Accounts Payable Officer (or equivalent).

Senior Financial Accountant

- check all treasury deal confirmations against the treasury spreadsheet and report any irregularities immediately to the CFO
- responsible for settling treasury transactions.

Finance Officer

- prepare and manage Council's cashflow and cash requirements
- report to the Finance Manager on the weekly cashflow position and resulting cash management transactions required.

3.0 Investment

Introduction

This Investment Policy has been prepared pursuant to Section 102(1) of the Local Government Act 2002 (the "Act"), which requires the Council to adopt an Investment Policy and a Liability Management Policy. Section 105 of the Act sets out what must be included in an Investment Policy.

Council generally holds investments for strategic reasons where there is some community, social, physical or economic benefit accruing from the investment activity.

Council's rationale for retaining investments is:

- strategic assets are to be held by the Council, for public good
- to earn from strategic investments a cash flow for investment in community wellbeing
- to prudently manage cash flows within annual budget parameters.

Council is a risk conscious entity and does not wish to incur additional risk from its treasury activities. Accordingly, Council's primary objective when investing is the protection of its initial investment and generating a commercial return on strategic investments is considered a secondary objective.

Objectives

The key investment policy objectives are to:

- provide a framework for the prudent and effective management of investments
- ensure that investments are managed in accordance with current governing legislation and Council's strategic and commercial objectives
- manage investments in a sustainable and equitable way, having regard to current and future generations

- recognise the community ownership of these assets and the need for a balanced investment/risk profile.
- ensure Council assets are managed prudently and adequately safeguarded
- safeguard Council's financial market investments by establishing and regularly reviewing investment parameters and ensuring all investment activities are carried out within these parameters
- maximise interest income on treasury investments, within a prudent level of investment risk. Council recognises that as a responsible public authority any treasury investments that it does hold should be of relatively low risk. It also recognises that lower risk generally means lower returns
- maintain and increase the real capital value of the eternal managed funds
- ensure funds are available to meet Council's needs
- maintain professional relationships with the Council's bankers, financial market participants, fund managers, trustees and other stakeholders
- regularly review the performance and creditworthiness of all investments
- maintain procedures and controls and provide timely and accurate financial and management information.

These objectives will be achieved by having regard to:

- the mix of investments that Council will utilise
- the process for the acquisition and divestment of new investments
- the management and assessment of risk
- the need for appropriate management and reporting procedures.

Investment Mix

Council has a portfolio of investments; at any time, these could comprise:

- treasury investments
- direct equity investments
- property
- other property investments – Community Housing
- forestry
- loans, advances for community development purposes
- internal loans
- external managed funds that could include equities.

The decision on which mix of investments Council will hold at any time will be based on the purpose for which the funds were acquired and the market conditions at the time.

Acquisition of New Investments

With the exception of treasury investments, internal loans and equity investments, new investments are acquired if an opportunity arises and approved by Council resolution, based on advice and recommendations from management. Before approving any new investments, Council gives due consideration to the contribution the investment will make in fulfilling Council's strategic objectives and the financial risks of owning the investment.

The authority to acquire treasury investments is delegated to the Chief Financial Officer.

Application of Returns from Investments

Some returns are earmarked for specific purposes, but generally returns on Council investments are applied to give equal benefit to the District ratepayers by application in a pro-rata basis to offset the costs of District services.

Direct Equity Investments

Nature of Investment

Direct equity investments are held for strategic purposes only and include interests in:

- **Civic Assurance Corporation** (13,715 shares)
  Civic Assurance is a specialist Local Government insurance company
- **Milford Sound Tourism Limited** (2,000 shares)
  The role of Council is to facilitate and co-ordinate development and operations at Milford Sound/*Piopiotahi* and Council's intention is to retain its shareholding in the company.

Rationale for Holding Investment

The Council may hold equity for non-investment purposes, provided that the holding is in furtherance of its purpose under the Local Government Act 2002.

To have the ability to utilise equity investments where necessary to:

- achieve the desired level of returns; and/or
- to provide a diversified investment portfolio.

Disposition of Revenue

These investments are held for strategic reasons only and not for investment purposes.

As such these investments do not derive revenue to Council in the form of dividends. If they do, revenue or dividends will be used to offset general rates.

Risk Management

Investments in the Civic Assurance Corporation and the Milford Sound Tourism Limited are held for strategic purposes. For any other equity investments, Council reviews the performance of the trading enterprises at least annually to ensure that strategic and financial objectives are being achieved.

Dispositions and acquisitions require Council approval.

Property

Nature of Investment

The Council's first objective is to only own property that is strategically necessary for the economic, physical and social development of the Southland District and secondly, to achieve an acceptable rate of return. Property investments do not include properties for operational purposes.

Rationale for Holding Investment

Council holds investment properties in order to generate income to offset general rates.

The Council reviews the performance of its property investments on an annual basis and ensures that the benefits of continued ownership are consistent with its stated objectives. Any disposition of these investments requires the Council's approval.

Disposition of Revenue

Income generated is used to offset operational expenditure. Surplus funds will be used to fund future property projects.

Risk Management

The risk in respect of holding investment property is evaluated as low given the location of the properties and their current and long-term use.

Rental income is considered low risk, due to the fixed and long-term nature of the lease agreements. Lease rental is negotiated at the time the lease expires.

Other Property Investments - Community Housing

Nature of Investment

Council has 69 community housing units available for rental. These houses are located in various townships across Southland District.

Rationale for Holding Investment

Council retains community housing to allow people to continue to live in its local community. The elderly or people with disabilities are given preference.

Council's philosophies include ensuring that rental charges cover costs (excluding depreciation) and to continue to maintain the housing at its current high standard. There is no required rate of return on this investment.

Disposition of Revenue

Revenue earned from the investment in community housing is retained in the community housing investment.

Risk Management

The risk in respect of holding other property investments is evaluated as low given the location of the properties and their current and long term use.

Council's community housing activities are managed by staff in the Property department. They regularly review Council's involvement in community housing, including assessment of the need for this asset within the community.

Dispositions and acquisitions require Council approval.

Forestry

Nature of Investment

The Council and its predecessor organisations have been involved in forestry for many years. Council's current forestry policy is that it will operate and maintain up to 3,000 planted hectares. The Council currently maintains 1,800 hectares of land.

Rationale for Holding Investment

Forestry assets are held as a long-term investment. The overall investment policy of the Council with regard to forestry is to maximise profit, with harvesting on a sustainable yield basis and without any demand on rates.

Disposition of Revenue

Any surplus revenue is used to offset rates. Any surplus not used in the year it was earned is accumulated into a forestry reserve and used to offset future rates. The use of the reserve in future years, will often be based on an even spread over a number of years to minimise rates fluctuations. Approximately $100,000 is retained for operating working capital at any time.

Risk Management

Forests are currently managed by a specialist external party. Forestry activities are reviewed by the Services and Assets Committee.

Significant risk management strategies include diversity of forest age classes, insurance against fire and access to a rural fire fighting force, a mix of species, geographic spread of forests and controlled access. Retention of the forest is reviewed periodically.

Dispositions and acquisitions require Council approval.

Loans and Advances for community development purposes

Nature of Investment

The Council is not a lender and therefore is not generally involved in providing loans or advances.

Rationale for Holding Investment

Council provides loans for community development purposes. From time to time, Council has provided a loan or advance to a community organisation to facilitate the ongoing provision of community services or recreational opportunities. The loans/investments are not made for financial investment purposes.

Council sets the terms and conditions for any loans or advances as they are granted. Council will require security as deemed appropriate for each loan or advance. The security will be the assets or revenue of the organisation.

Disposition of Revenue

Generally, these loans are to the benefit of the local community and not for financial investment purposes. Interest will be charged at a rate that is consistent with Council's interest rate on internal loans. Any revenue would be applied to reserves, reduce external debt or offsetting general rates.

Risk Management

Council will review the performance of its loan advances on a regular basis to ensure the planned strategic and economic objectives are being achieved.

Council monitors the compliance of the borrower with the terms and conditions agreed upon.

All loans and advances documentation are subject to independent legal review prior to finalisation.

Internal Loans

Nature of Investment

Council may utilise its general reserves and surplus funds for internal borrowing/lending purposes to reduce external debt, thus effectively reducing borrowing costs.

Rationale for Holding Investment

To facilitate the development of Council activities within Council and the community to minimise the costs associated with borrowing externally.

Disposition of Revenue

Income derived from internal loans is generally used to generate a return to reserves. Any surplus income is used to reduce external debt and/or offset against general rates.

Risk Management

Internal loans shall be managed as a treasury investment. Interest rates will be set having regard for Council's opportunity cost forgone.

Council may not achieve the opportunity cost due to actual external interest rates being different to the interest rate set for any given year as part of the LTP/Annual Plan process. In this case the return to Council may be more or less and will impact on the return to reserves.

Treasury Investments

Nature of Investment

To provide the ability to utilise a range of financial investments not already specified in this policy.

Approved treasury investments include;

Category	Instrument
Treasury Investments	Call and term bank deposits Bank certificates of deposit (RCDs) Treasury Bills and Government Bonds LGFA bonds/Floating Rate Notes (FRN)/Commercial Paper (CP) LGFA borrower notes

With the exception of LGFA borrower notes, the term of the treasury instruments is no greater than one year.

Rationale for Holding Investment

Council’s philosophy in the management of treasury investments is to optimise its capital protection and liquidity objectives while balancing risk and return considerations. Council recognises that as a responsible public authority any treasury investments that it does hold should be low risk. It also recognises that lower risk generally means lower returns.

The Council maintains treasury investments to:

- invest surplus cash and working capital funds
- achieve the desired level of returns within acceptable risk parameters
- invest amounts allocated to general reserves, trust funds and special funds.

Council's primary objective when investing is the protection and liquidity of its investment. Accordingly, only credit-worthy counterparties are acceptable. Credit-worthy counterparties are selected on the basis of their current Standard and Poor’s (S&P) or equivalent rating, which must be strong or better.

To avoid undue concentration of exposures, treasury investments should be used with as wide a range of counterparties as practicable. Transaction principal amounts and maturities should be well spread where possible.

Within the above constraints, Council also seeks to:

- ensure investments are liquid
- maximise investment return
- manage potential capital losses due to interest rate movements.

Liquidity risk is minimised by ensuring that all negotiable treasury investments must be capable of being liquidated in a readily available secondary market.

Disposition of Revenue

Income derived from Council’s treasury activities will be used to fund Council activities including the allocation of interest on reserves, offsetting rates and repaying external debt.

Externally Managed Funds

Nature of Investment

Council may invest its general reserves in externally managed funds. Council has a medium to long-term investment horizon as it seeks to manage investments in a sustainable and equitable way, having regard to both current and future generations of ratepayers.

Council would purchase units in a NZD managed fund or funds.

Rationale for Holding Investment

Council maintains externally managed funds to:

- maintain, protect and increase the real capital value of the principal amount invested. Real capital value is the value that has been adjusted for the effect of inflation
- diversify the investment of Council’s general reserves
- maintain liquidity and access to cash if needed
- obtain annual cash income to subsidise rates revenue.

Where practical, investments will be made considering the ethical practices of the investment entity. Council's intention for the Funds is to avoid direct involvement with industries that have a negative impact on society and the environment. This includes:

- alcohol
- tobacco
- military/weapons
- labour practices.

Disposition of Revenue

The managed funds are expected to return (before fees and taxes) at least 5% per annum. Council will consider as part of its planning process what is appropriate to subsidise rates revenue and what should be accrued back to its reserves, having regard to its rationale noted above. The actual disposition may differ from that planned as a result of the actual returns being more or less than budgeted again having regard to the rationale above.

Income derived from managed funds in the form of interest and dividends, is generally used to offset general rates with any surplus income used to provide a return on reserves. Surplus income can be re-invested in the managed fund(s).

Annually, Council evaluates whether to realise any capital gains that have been accumulated by the managed funds over the period. Overall the objective is to hold the managed funds for the medium to long term.

Risk Management

Council has a preference to invest indirectly in externally managed funds that are managed by a suitably qualified fund manager(s) and be managed within the below criteria.

Council's risk profile is considered moderate for financial investment purposes and therefore seeks to invest in a 'balanced' managed fund where there is a mix of capital growth and income asset types. Council will buy units in an established externally managed fund but could appoint its own investment manager.

The strategic asset allocation and tactical ranges are provided in the following table:

Allocation	Benchmark %	Ranges %
Total growth assets	50%	40-60%
Total income assets	50%	40-60%

Growth assets include approved asset types; listed domestic and international equities and listed property shares. Income assets include asset types such as; cash, term deposits, domestic and international floating and fixed rate debt securities. Any other asset types must be approved by Council before any investment is made.

Investments may be hedged back to NZD.

The counterparty risk policy set out in section 4 does not apply to externally managed funds. The investment guidelines are set out in Appendix 1.

At least quarterly reporting is provided on the performance of the managed fund(s). Annually the fund performance is benchmarked to other similar funds.

Local Government Funding Agency Limited (LGFA)

Despite anything earlier in this Investment Policy, Council may invest in shares and other financial instruments of the New Zealand LGFA and may borrow to fund that investment. The Council's objective in making any such investment will be to:

- obtain a return on the investment; and
- ensure that the LGFA has sufficient capital to remain viable, meaning that it continues as a source of debt funding for the Council.

Because of this dual objective, Council may invest in LGFA shares in circumstances in which the return on that investment is potentially lower than the return it could achieve with alternative investments.

If required in connection with the investment, Council may also subscribe for uncalled capital in the LGFA.

4.0 Liability Management

Introduction

This Liability Management Policy has been prepared pursuant to the Local Government Act 2002; section 102(1) which requires the Council to adopt a Liability Management Policy and section 104 which outlines the contents of the policy.

Generally, Council borrows to provide funding for the following activities:

- fund Council capital expenditure requirements
- manage timing differences between cash inflows and outflows
- cover special 'one-off' projects
- fund assets with intergenerational qualities
- manage timing differences in the rebalancing of its internal loan portfolio into externally managed funds.

Total debt levels are determined through Council's Long-Term Plan (LTP) and Annual Plans. Council approves this borrowing requirement for each financial year in the Annual Plan or LTP or by resolution during the year.

Objectives

- ensure Council has appropriate working capital funds available to carry out its plans as outlined in its LTP and Annual Plan
- ensure that Council has an on-going ability to meet its debts in an orderly manner as and when they fall due in both the short and long term, through appropriate liquidity and funding risk management
- arrange appropriate funding facilities for Council, ensuring they are at market related margins utilising bank debt facilities and/or capital markets as appropriate
- maintain lender and LGFA relationships and Council general borrowing profile in the local debt and, if applicable, capital markets, so that Council is able to fund its activities appropriately at all times
- control Council's cost of borrowing through the effective management of its interest rate risks, within the interest rate risk management limits established by this policy
- ensure compliance with any financing/borrowing covenants and ratios
- maintain adequate internal controls to mitigate operational risks

- produce accurate and timely reports that can be relied on by senior management and Council for control and exposure monitoring purposes in relation to the debt raising activities of Council.

Council will manage its borrowing activities prudently to ensure the best interests of the District are maintained. To undertake this, the following will be considered in conjunction with every transaction undertaken:

- cost minimisation
- cost stabilisation/risk management.

Specific Borrowing Limits

Total debt levels are maintained at a prudent level and will be managed within the following limits:

Item	Borrowing Limit
Net debt as a percentage of total revenue	<175%
Net interest as a percentage of total revenue	<10%
Net interest as a percentage of rates revenue	<7%
Liquidity (external, borrowing +available committed loan facilities + available liquid investments as a percentage of existing external debt)	>110%

- total revenue is defined as cash earnings from rates, government grants and subsidies, user charges, interest, dividends, financial and other revenue and excludes non-government capital contributions (e.g. developer contributions and vested assets)
- net debt is defined as total debt less treasury investments. External debt that is specifically borrowed for on-lending to a CCO/CCTO is netted with the corresponding loan asset for the LGFA covenant calculation
- liquid investments are unencumbered assets defined as being:
    - overnight bank cash deposits
    - wholesale/retail bank term deposits no greater than 31 days.
    - bank issued registered certificates of deposit less than 181 days
- external debt funding and associated investment activity relating to pre-funding is excluded from the liquidity ratio calculation
- net interest is defined as the amount equal to all interest and financing costs less interest income for the relevant period
- annual rates revenue is defined as the amount equal to the total revenue from any funding mechanism authorised by the Local Government (Rating) Act 2002 together with any revenue received from other local authorities for services provided (and for which the other local authorities rate)
- financial covenants are measured on Council only
- disaster recovery requirements are to be met through the liquidity ratio.

Debt Repayment

Total debt levels are indicated through Council's LTP or Annual Plans. Council's Annual Report will contain information to allow actual debt levels to be compared with those forecasted.

Loans raised for specific projects will generally be repaid through user charges or rates. Loans raised for local purposes will generally be repaid by the ratepayers in the relevant local area. Surplus Council funds and proceeds from the sale of investments and assets will be reviewed periodically by Council with a view to repaying debt, or for funding capital projects.

The Council may repay debt before maturity in special cases where the circumstances suggest that this would be in the best interests of the District.

Debt will be repaid as it falls due in accordance with the applicable borrowing arrangement. Subject to the appropriate approval and debt limits, a loan may be rolled over or re-negotiated as and when appropriate.

Guarantees/contingent liabilities and other financial arrangements

Council may act as guarantor to CCOs, financial institutions on loans when the purposes of the loan are in line with Council's strategic objectives.

For any outstanding guarantees, Council will ensure that sufficient financial capacity exists relative to LGFA lending covenants. Unless approved by Council, guarantees or financial arrangements given will not exceed NZ$1 million in aggregate.

Council is not permitted to provide any guarantee of indebtedness in favour of any loans to CCTOs under Section 62 of the Local Government Act.

For any guarantee for indebtedness provided by Council to a CCO that borrows directly from the LGFA or bank lender, Council will approve the specific borrowing and guarantee arrangement.

Borrowing mechanisms for council-controlled organisations and council-controlled trading organisations

To better achieve its strategic and commercial objectives, Council may provide financial support in the form of debt funding directly or indirectly to CCO/CCTOs.

Guarantees of financial indebtedness to CCTOs are prohibited, but financial support may be provided by subscribing for shares as called or uncalled capital.

Any lending arrangement to a CCO/CCTO must be approved by Council. In recommending an arrangement for approval the Chief Financial Officer considers the following:

- credit risk profile of the borrowing entity, and the ability to repay interest and principal amount outstanding on due date
- impact on Council's credit standing, debt cap amount (where applied), borrowing limits with the LGFA and other lenders and Council's future borrowing capacity
- the form and quality of security arrangements provided
- the lending rate given factors such as; CCO/CCTO credit profile, external Council borrowing rates, borrower note and liquidity buffer requirements, term etc
- lending arrangements must be documented on a commercial arm's length basis. A term sheet, including matters such as borrowing costs, interest payment dates, principal payment dates, security and expiry date is agreed between the parties
- accounting and taxation impact on-lending arrangement.

All lending arrangements must be executed under legal documentation (e.g. loan, guarantee) reviewed and approved by Council's independent legal counsel.

LGFA

Despite anything earlier in this Liability Management Policy, Council may borrow from LGFA and, in connection with that borrowing, may enter into the following related transactions to the extent it considers necessary or desirable:

- contribute a portion of its borrowing back to the LGFA as an equity contribution to the LGFA
- provide guarantees of the indebtedness of other local authorities to the LGFA and of the indebtedness of the LGFA itself
- commit to contributing additional equity (or subordinated debt) to the LGFA if required
- subscribe for shares and uncalled capital in the LGFA
- 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.

Internal Loans

All Council investments may be used as a source for internal loans in relation to expenditure of a capital (or one off) nature related to any activity that would otherwise be funded by external loan.

The term of any internal loan shall not be more than 30 years and will be set after taking into account the ability of ratepayers affected to pay, alternative uses of the funds and the life of the assets to be funded. The term set will be subject to review during the course of the loan.

The interest rate to be applied to internal loans for any given year will be developed as part of Council's Long-Term Plan or Annual Plan. To remove any doubt, the interest rate calculated will be the interest rate used for that year for budgeting and end of year actual results.

The method of calculation and the resulting interest rate will be resolved by Council as part of this annual process. In developing the method of calculation, Council will consider its investment policy objective, which is to obtain the net opportunity cost of not having the funds invested externally. Council will also consider its present and future financial position as well as market conditions.

After taking into account fairness and equity, Council can resolve to apply a lesser interest rate than the interest rate calculated where it agrees the circumstances are such that it is warranted.

Security

It is Council's general policy to offer security for its borrowing and risk management activities by way of negative pledge or a charge over its rates offered through a Debenture Trust Deed. Under a Debenture Trust Deed, Council's borrowing is secured by a floating charge over all Council rates levied under the Local Government Rating Act. The security offered by Council ranks equally or pari passu with other lenders.

In the normal course, the Council's policy is not to offer a guarantee or security over any of the other assets of the Council. However, the Council may decide to offer security over the asset:

- where borrowing is by way of finance lease, or some other form of trade credit under which it is normal practice to provide security over the asset concerned, or
- where the Council considers doing so would help further its community goals and objectives.

Any lending to a CCO or CCTO will be on a secured basis and be approved by Council.

Interest Rate Exposure

Interest rate risk management refers to managing the impact that movements in interest rates can have on Council's cash flows. This can have both a positive and/or negative impact. A 1% change in interest rate will have a 0.4% impact on rates (on rates of $50 million).

The primary objective of interest rate risk management is to reduce uncertainty relating to interest rate movements through fixing/hedging of wholesale interest costs. Certainty around interest costs is to be achieved through the proactive management of underlying interest rate exposures.

When actual debt amounts are at $20 million or above it is mandatory that the interest rate exposures of Council are managed according to the limits detailed in the following table. Council's gross external core debt forecasts (less any pre-funded debt amounts) must be within the following fixed/floating interest rate risk control limits:

FIXED RATE HEDGING PERCENTAGES		
Term	**Minimum Fixed Rate Amount**	**Maximum Fixed Rate Amount**
Current	40%	90%
Year 1	40%	90%
Year 2	35%	85%
Year 3	30%	80%
Year 4	25%	75%
Year 5	20%	70%
Year 6	0%	65%
Year 7	0%	60%
Year 8	0%	50%
Year 9	0%	50%
Year 10	0%	50%
Year 11	0%	25%
Year 12	0%	25%
Year 13	0%	25%
Year 14	0%	25%
Year 15	0%	25%

"Fixed rate" is defined as all known interest rate obligations on forecast external core debt, including where hedging instruments have converted floating rate obligations into firm commitments.

"Floating rate" is defined as any interest rate obligation subject to movements in the applicable reset rate.

Gross forecast external core debt is the amount of total external debt for a given period. This allows for pre-hedging in advance of projected physical drawdowns of new debt. When approved forecasts are changed, the amount of fixed rate cover in place may have to be adjusted to ensure compliance with the Policy minimums and maximums. Pre-funded debt amounts are excluded from the gross debt forecast.

Core debt is defined as debt that is expected to remain for a period of greater than one year.

A fixed rate maturity profile that is outside the above limits, but self corrects within 90-days is not in breach of this Policy. However, maintaining a maturity profile that is outside the above limits beyond 90-days requires specific approval by Council.

Any fixed rate hedge with a maturity beyond 15 years must be approved by Council. The exception to this will be if Council raises LGFA funding as fixed rate or as a swapped floating rate and this maturity is beyond 15 years.

Hedging outside the above risk parameters must be approved by Council.

Approved interest rate instruments are as follows:

Category	Instrument
Interest rate risk management	Forward rate agreements ("FRAs") on: • bank bills Interest rate swaps/collars including: • swap extensions, deferrals and shortenings Interest rate options on: • bank bills (purchased caps and one for one collars) • interest rate swaptions (purchased swaptions and one for one collars only)

- One for one collar option structures are allowable, whereby the sold option is matched precisely by amount and maturity to the simultaneously purchased option. During the term of the option, only the sold side of the collar can be closed out (i.e. repurchased) otherwise, both sides must be closed simultaneously. The sold option leg of the collar structure must not have a strike rate 'in-the-money';
- Selling interest rate options for the primary purpose of generating premium income is not permitted because of its speculative nature;
- Purchased borrower swaptions must mature within 12 months;
- Interest rate options with a maturity date beyond 12 months that have a strike rate (exercise rate) higher than 2.00% above the appropriate swap rate, cannot be counted as part of the fixed rate cover percentage calculation;
- Forward start period on swaps and collars to be no more than 36 months from deal date except where the forward start swap/collar starts on the expiry date of an existing swap/collar and has a notional amount which is no more than that of the existing swap/collar.

Any other interest rate instrument must be specifically approved by Council on a case-by-case basis and only be applied to the one singular transaction being approved. Credit exposure on these financial instruments is restricted by specified counterparty credit limits.

Prudent selection of interest rate instruments and mix will help the Council achieve its low debt servicing costs and risk minimisation objectives.

Liquidity and Funding Risk Management

Liquidity management refers to the timely availability of funds to Council when needed, without incurring penalty costs. This takes into account the ability to refinance or raise new debt at a future time at the same or more favourable pricing and terms of existing facilities.

Council's ability to readily attract cost effective borrowing is largely driven by its ability to rate, maintain a strong credit rating and manage its relationships with the LGFA and financial institutions. To this end it is the Council's intention to seek and maintain a strong balance sheet position.

Council may use a mixture of short-term facilities (which generally have lower credit margins) as well as longer term facilities to achieve an effective borrowing mix, balancing the requirements of liquidity and cost.

Council's objective for funding risk management is to minimise the risk of large concentrations of debt being reissued or raised at a time of adverse movements in borrowing margins beyond the Council's control.

The Council's policy for liquidity and funding risk management is:

- ensuring that Council's committed debt facilities and term loans mature over a wide time period
- external debt plus available committed debt facilities, plus liquid assets must be maintained at an amount of at least 110% over existing external debt
- through the LGFA and bank lenders, diversify borrowing over a range of wholesale investors and lenders
- ensuring that bank borrowings are only sought from approved strongly rated New Zealand registered banks
- matching expenditure closely to its revenue streams and managing cash flow timing differences
- maintaining its treasury investments in cash/cash equivalent liquid investments
- Council has the ability to pre-fund up to 18 months of the forecast debt requirements including re-financings.

When actual debt amounts are at $20 million or above it is mandatory that the following limits apply for managing funding risk. The maturity profile of the total committed funding in respect to all external debt and committed debt facilities is to be controlled by the following system:

Period	Minimum %	Maximum %
1 to 3 years	15	60
3 to 7 years	25	85
7 years plus	0	60

A funding maturity profile that is outside the above limits, but self corrects within 90-days is not in breach of this Policy. However, maintaining a maturity profile outside of policy limits beyond 90-days requires specific approval by Council.

To minimise concentration risk, the LGFA requires that no more than the greater of NZD 100 million or 33% of a Council's borrowings from the LGFA will mature in any 12-month period.

Approved debt and liquidity instruments include;

Category	Instrument
Cash management, liquidity and borrowing	Bank overdraft Committed cash advance and bank accepted bill facilities (short term and long-term loan facilities) Floating Rate Note (FRN) Fixed Rate Note (MTN) Commercial paper (CP)/Promissory notes

Credit Risk Management

Counterparty credit risk is the risk of losses, realised or unrealised, arising from a counterparty defaulting on a financial instrument where the Council is a party. Treasury investments, interest rate and foreign currency instruments are captured within the policy. The credit risk to the Council in a default event will be weighted differently depending on the type of instrument entered into.

Amounts should be spread amongst a number of counterparties to avoid concentrations of credit exposure.

Credit risk is minimised by placing maximum prescribed limits for each broad class of non-Government issuer and by limiting investments and risk management instruments to registered banks that have a credit rating from a recognised international credit rating agency. The limit system is as follows;

Counterparty/Issuer	Minimum S&P long term/short term credit rating	Total maximum combined limit per counterparty ($million)*
NZ Government	AA+/A-1+	Unlimited
NZ Local Government Funding Agency	AA/A-1	Unlimited
NZ Registered Bank (per bank)	AA /AA-/A-1	10.0
NZ Registered Bank (per bank)	A+/A/A-1	5.0
* This combined total maximum limit includes exposure to the counterparties including treasury investments and risk management instruments and excludes externally managed fund(s).		

In determining the usage of the above gross limits, the following weightings will be used:

- treasury investments (e.g. bank term deposits) – transaction principal amount
- interest rate risk management (e.g. swaps, FRAs) – transaction notional x maturity (years) x 3%
- foreign exchange risk (e.g. forward exchange contract) – transaction face value amount x ((square root of the maturity (years)) x 15%).

Each transaction should be entered into a treasury spreadsheet and a quarterly report prepared to show assessed counterparty actual exposure versus limits. Credit ratings are reviewed on an ongoing basis and in the event of material credit downgrades should be immediately reported to the Chief Financial Officer and assessed against exposure limits. If any counterparty's credit rating falls below the minimum specified in the above table, then all practical steps are taken to eliminate the credit exposure to that counterparty as soon as practicable.

Counterparties exceeding limits should be reported to Council.

Foreign currency

Council has foreign exchange exposure through the occasional foreign exchange transactions that Council may undertake such as plant and equipment.

Significant commitments for foreign exchange can be hedged using foreign exchange contracts, once expenditure is approved. Forward exchange contracts can be used by the Council. The majority of these transactions would be small and would carry no significant foreign exchange risk.

Council does not borrow or enter into incidental arrangements within or outside New Zealand in currency other than New Zealand currency.

5.0 Procedures for Management and Reporting

Cash Management

The finance function is responsible for managing the Council's cash surpluses and/or deficits.

The Council maintains rolling daily, monthly and annual cash flow projections which form the basis of its cash management activity. The Council maintains one main bank account for its operating cash flows as well as other bank accounts for specialist activities such as investment and borrowing requirements. Individual business units within the Council do not maintain separate bank accounts.

The Council manages its working capital balances by matching expenditure closely to its revenue streams and managing cash flow timing differences to its favour. Daily bank balances are extracted by the Finance Officer.

Generally, cash flow surpluses from timing differences are available for periods less than 90 days.

Cash management activities must be undertaken within the following parameters:

- an optimal daily range of $10,000 is targeted for in the Council's main bank account, with investments adjusted to balance the current account if required
- cash flow surpluses are placed in call deposits, term deposits, registered certificates of deposits and promissory notes
- amounts invested must be in approved instruments and within approved credit limits
- the Council has a committed bank facility with a limit of $5,000,000 for working capital purposes which is used on an operational basis
- the use of interest rate risk management on cash management balances is not permitted.

Internal Controls

The Council's systems of internal controls over cash management and treasury activity includes adequate segregation of duties among the core treasury functions of deal execution, confirmation, settling and accounting/reporting.

Key internal cash management controls are as follows:

- cheque/electronic banking signatories - dual signatures are required for all cheques and electronic transfers
- authorised personnel - all counterparties are provided with a list of personnel approved to undertake transactions, standard settlement instructions and details of personnel able to receive confirmations

- reconciliations - general bank reconciliation is performed daily and monthly by the Debtors Officer (or equivalent) and reviewed by a senior finance staff member.

There are a small number of people involved in treasury activity. Accordingly, strict segregation of duties is not always achievable. The risk from this is minimised by the following processes:

- a documented discretionary approval process for treasury activity
- regular management reporting
- operational risk control reviews will be undertaken periodically
- appropriate organisational, systems, procedural and reconciliation controls exist to ensure:
  (a) all treasury activity is bona fide and properly authorised;
  (b) checks are in place to ensure the Council's accounts and records are updated promptly, accurately and completely.

The details of any exceptions, including remedial action taken or intended to be taken.

Legal risk

Legal risks relate to the unenforceability of a transaction due to an organisation not having the legal capacity or power to enter into the transaction usually because of prohibitions contained in legislation. While legal risks are more relevant for banks, Council may be exposed to such risks.

Council will seek to minimise this risk by adopting policy regarding:

- the use of standing dealing and settlement instructions (including bank accounts, authorised persons, standard deal confirmations, contacts for disputed transactions) to be sent to counterparties
- the matching of third-party confirmations and the immediate follow-up of anomalies
- the use of expert advice.

Financial instruments can only be entered into with banks that have in place an executed International Swaps and Derivatives Association (ISDA) Master Agreement with Council.

Council's internal/appointed legal counsel must sign off on all documentation.

Council must not enter into any transactions where it would cause a breach of financial covenants under existing contractual arrangements.

Council must comply with all obligations and reporting requirements under existing funding facilities and legislative requirements.

Reports

The following reports are produced to monitor treasury activity:

Report Name	Frequency	Prepared by	Recipient
Daily Cash Position	Daily	Finance Officer or equivalent	Senior Finance staff member
Treasury Spreadsheet	As required	Finance Officer or equivalent	Senior Finance staff member
Treasury Exceptions Report	As required	Finance Officer or equivalent	Senior Finance staff member/CFO

Report Name	Frequency	Prepared by	Recipient
Treasury Report Policy limit compliance Borrowing limits Funding and Interest Risk Position Total debt funding facility utilisation New treasury transactions Cost of funds vs budget Cash flow forecast report Liquidity risk position Counterparty credit Debt maturity profile Renewal investment Operating investment Exceptions	Monthly	Finance Officer or equivalent	CFO
Treasury Report Include monthly report along with; External managed Funds Report A statement of policy compliance. Treasury and markets commentary Treasury performance CCO/CCTO loans and guarantees, financial arrangements Revaluation of financial instruments	Quarterly	Finance Officer or equivalent	CFO and Finance and Audit Committee
Trustee Report	As required by the Trustee	Finance Officer or equivalent	CFO/Trustee company
LGFA Report	Annual	Finance Officer or equivalent	CFO/LGFA

Benchmarking

In order to determine the success of Council's treasury management function, the following benchmarks and performance measures have been prescribed.

Those performance measures that provide a direct measure of the performance of treasury staff (operational performance and management of debt and interest rate risk) are to be reported to Council or an appropriate sub-committee of Council on a quarterly and YTD basis

- All treasury limits must be complied with including (but not limited to) counterparty credit limits, dealing limits and control limits
- All treasury deadlines are to be met, including reporting deadlines
- The actual borrowing cost for Council (taking into consideration costs of entering into interest rate risk management transactions) should be below the budgeted borrowing costs
- The actual investment return for Council on the external managed funds are above the budget investment return amounts
- Annually the actual total return on the externally managed funds is compared to average annual total return of peer 'balanced' managed funds.

Compliance with the benchmarking standard is not required if Council's nominal debt levels are less than $10M.

Delegations

Pursuant to Clause 32 (2), Schedule 7, of the Local Government Act 2002, the Council may make delegations to officers of the Council to allow for the efficient conduct of Council business. Clause 32 (3), Schedule 7 of this Act allows officers to delegate those powers to other officers.

Notwithstanding Clause 32 (1) (c), Schedule 7 the power to borrow money, or purchase or dispose of assets, other than in accordance with the Long Term Plan remains the sole responsibility of the Council. This responsibility cannot be delegated.

The Liability Management and Investment Policy related delegations are below.

Activity	Delegated to	Limits
Approve and amend policy document	Council	Unlimited
Approve external borrowing as set out in the Annual Plan or Long Term Plan	Chief Executive or Chief Financial Officer	As Per Annual Plan or Long Term Plan
Approve LGFA membership	Council	Unlimited subject to legislative limitations
Approve LGFA membership for CCO/CCTO	Council	Unlimited subject to legislative limitations
Approve giving of Council guarantee or uncalled capital	Council	Unlimited subject to legislative limitations
Approve selection of external managed Funds) and amount placed with Fund(s)	Council	Unlimited
Approve amount placed with approved managed fund	Chief Executive or Chief Financial Officer	As per Annual Plan or Long Term Plan

Activity	Delegated to	Limits
Acquisition and disposition of investments other than treasury investments	Council	Unlimited
Approval for charging assets as security over borrowing and risk management activity	Council	Unlimited
Negotiation and ongoing management of lending arrangements with CCO/CCTO	Chief Executive, Chief Financial Officer	
Approving new and re-financed debt amounts.	Chief Executive, Chief Financial Officer	Unlimited
Open/close bank accounts	Chief Financial Officer with advice given to Chief Executive	Unlimited
Approve signatories to Council's Bank Accounts	Chief Executive and Chief Financial Officer	Unlimited
Approve electronic banking amendment	Chief Financial Officer	
Liquidity, debt and investment management	Chief Executive, Chief Financial Officer	Subject to policy
Interest rate and foreign currency management	Chief Executive and Chief Financial Officer	Subject to policy
Cash management	Chief Executive, Chief Financial Officer, Finance Manager	Subject to policy
Approving transactions outside policy	Council	Unlimited
Approving allowable risk management instruments	Council	Unlimited subject to legislative limitations
Maximum daily transaction amount (approved investment, debt, cash management, interest rate risk and foreign currency management)	Council Chief Executive Chief Financial Officer	Unlimited $10m $5m
Approve debt, investment and interest rate strategies	Finance and Assurance Committee	
Ensuring compliance with policy	Chief Financial Officer	N/A
Triennial review of the Policy	Chief Financial Officer	N/A

Appendix 1 – External Managed Funds - Investment Guidelines

The guidelines and constraints required by Council to be observed by the managed funds or Investment Manager, as applicable are set out below. For the purposes of these constraints, "Funds" shall relate to the portion of the investment assets under the management of the Investment Managers.

Where the Funds are invested into an external managed fund(s) or collective investment vehicle ("units") or product Council recognises that the strict application of these guidelines and constraints may not be possible. The Manager(s) of the externally managed funds will inform Council of its pooled or collective investment guidelines. Council expect the Manager(s) to inform them of any investment or management practice that materially falls outside the guidelines and constraints so that Council can continually reassess the overall suitability of such an investment approach.

Cash and Term deposits

Council may invest cash in bank, call, term deposits or registered certificates of deposit. Where it does so it may invest in the following:

Bank, call, term deposits and registered certificates of deposit with New Zealand Registered Banks with a Standard and Poor's or equivalent credit agency, short term credit rating of 'A-1' or stronger. Bank term deposits have a maturity date of no greater than 3-years.

To be classified as a cash investment, deposits must have a maturity date of 31 days or less. Both bank term deposits and registered bank bills must have a maturity date of no more than 12 months.

New Zealand and International Fixed Interest

Investment in an unsecured, senior or secured debt security and should have a minimum long-term credit rating of no less than BBB or short term credit rating of A-2, as measured by Standard & Poor's, or equivalent credit agency.

Commercial Paper issued by a corporate borrower, with a Standard and Poor's or equivalent credit agency, short term credit rating of 'A-2' or stronger. The maturity date can be no more than 12 months.

No investments in direct mortgages, subordinated debt, structured debt, high yield/junk bonds and leveraged loans should be made.

Equities

Investments must be confined to publicly listed widely held securities trading in recognised markets.

New Zealand and International Property Investments

Investment in property entities that are listed on the New Zealand or internationally recognised Stock Exchange.