Treasury policy

1.0 Introduction

The purpose of the Treasury Policy (Policy) is to outline approved policies and procedures in respect of all treasury activity to be undertaken by Rotorua Lakes Council (Council). The formalisation of these policies and procedures will enable treasury risks within Council to be prudently managed. The Policy establishes borrowing limits to ensure prudent management of anticipated debt borrowings over time, interest rate risk management limits to ensure prudent management of interest rate risks, and that investment returns are maximised within an acceptable risk management framework, to ensure capital preservation, for the benefit of current and future ratepayers.

2.0 Scope and Objectives

2.1 Scope

This document identifies the policy and procedures of Council in respect of treasury management activities.

2.2 Objectives

The objective of this Policy is to control and manage costs and investment returns that can influence operational budgets and public equity. Specifically:

2.3 Statutory Objectives and requirements

- All projected external borrowing, investments and incidental arrangements (such as the use of interest rate hedging instruments) will meet the requirements of the Local Government Act 2002, and incorporate the Liability Management and Investment Policy.
- Council is governed by the following relevant legislation:
    - Local Government Act 2002, in particular Part 6 including sections 101, 102, 104 and 105 requiring Council to adopt a number of funding and financial policies including a liability and investment policy. Council must manage its revenue, expenses, assets, liabilities and investments prudently, in a manner that promotes the current and future interests of the community.
    - Trusts Act 2019 (effective 30 January 2021). When acting as a trustee or investing money on behalf of others, the Trusts Act highlights that trustees have a duty to invest prudently and that they shall exercise care, diligence and skill that a prudent person of business would exercise in managing the affairs of others. Details of relevant sections can be found in the Trusts Act 2019 Part 4 Investments.
    - Public Bodies Lease Act 1969.
    - Property Law Act 2007.
    - Local Government (Financial Reporting and Prudence) Regulations 2014, in particular Schedule 4.
- All projected borrowings are to be approved by Council as part of the Annual Plan process, or resolution of Council before the borrowing is undertaken.
- Lenders and debenture trust deed covenants, including the specific requirements to the New Zealand Local Government Funding Agency which Council joined in February 2013 as a borrower and guarantor.
- Liabilities outside of policy - Council from time-to-time will enter into transactions and agreements that can expose Council to financial liability. These may include creditors, leases and guarantees.
- Council will not enter into borrowings denominated in a foreign currency.

- Council will not transact with any Council Controlled Organisation ("CCO") or Council Controlled Trading Organisation ("CCTO") on terms more favourable than those achievable by Council itself, (subject to the exemption as per Section 9 of the Local Government Borrowing Act 2011, lending and financial accommodation provided to the Local Government Funding Agency).
- A resolution of Council is not required for hire purchase, credit or deferred purchase of goods if:
  - The period of indebtedness is less than 91 days (including rollovers); or
  - The goods or services are obtained in the ordinary course of operations on normal terms for amounts not exceeding in aggregate amount determined by resolution of the Council as not being so significant as to require specific authorisation.

2.4 General Objectives

- Comply with financial ratios and limits stated within this Policy.
- Ensure that all statutory requirements are adhered to.
- Borrow funds, invest funds and transact risk management instruments within an environment of control and compliance under the Council approved Policy, so as to protect Council's financial assets.
- Minimise Council's costs and risk in the management of any external borrowings.
- Minimise Council's exposure to adverse interest rate movements.
- Maintain appropriate liquidity levels and manage cash flows to meet known and reasonable unforeseen funding requirements.
- Monitor, evaluate and report on treasury performance, including Policy compliance, financing/borrowing covenants and ratios, and lending/security obligations.
- Minimise Council's exposure to credit risk by dealing with and investing in credit worthy counterparties.
- Ensure adequate internal controls exist to protect Council's financial assets and to prevent unauthorised transactions.
- Manage any investments to optimise returns in the long term, whilst balancing risk and return considerations giving proper regard to the distribution between present and future generations of ratepayers.
- Monitor Council's return on all investments.
- Develop and maintain relationships with financial institutions, the LGFA, credit rating agencies, trustees and investors.
- Ensure Council, management, and all relevant staff are kept abreast of the latest treasury products, methodologies, and accounting treatments through training and in-house presentations.

3.0 Delegated Authorities

Council has the following responsibilities, either directly itself or via the following stated delegated authorities:

Activity	**Delegated authority**	**Limit**
Approving and changing policy	Council	Unlimited
Approving external borrowing programme through adopting Annual Plan	Council	Unlimited (subject to legislative and other regulatory limitations)
Acquisition and disposition of investments (other than financial investments)	Council	Unlimited
Approving new and refinanced bank debt facilities	Council	Unlimited
Approval for charging physical assets as security over borrowing	Council	Unlimited
Approval for providing security stock as security over borrowing	Chief Executive or delegate	Unlimited
Appointing Debenture Trustee	Council	Unlimited
Re-financing existing debt	Chief Financial Officer	Per risk control limits
Approving transactions outside policy	Council	Unlimited

Adjusting the interest rate risk profile	Chief Financial Officer	Per risk control limits
Managing funding maturities	Chief Financial Officer	Per risk control limits
Managing cash/liquidity requirements	Chief Financial Officer	Per risk control limits
Maximum daily transaction amount (borrowing, interest rate risk management) excludes roll overs on floating rate debt and interest rate roll overs on swaps	Chief Financial Officer Director of Finance Finance Manager	$50 million $30 million $15 million
Authorising seal register signatories	Mayor/Chief Executive or delegate	Unlimited
Authorising lists of signatories and opening/closing bank accounts	Chief Executive or delegate	Unlimited
Triennial review of Policy	Chief Financial Officer	Approved by Council
Ensuring compliance with Policy	Chief Financial Officer	N/A

All management delegated limits are authorised by the Chief Executive. The following procedures must be complied with:

- All delegated authorities and signatories must be reviewed at least annually to ensure they are still appropriate and current
- A comprehensive letter must be sent to all relevant banks and other counterparties, at least annually, to confirm details of all relevant current delegated authorities empowered to bind Council
- Whenever a person, with delegated authority on any account or facility, leaves Council, all relevant banks and other counterparties must be advised in writing in a timely manner to ensure that no unauthorised instructions are to be accepted from such persons.

4.0 Liability Management Policy

Council's liabilities comprise borrowing and various other liabilities. Council's Liability Management Policy focuses on borrowings as this is the most significant component and exposes Council to the most significant risks. Other liabilities are generally non-interest bearing. Cash flows associated with other liabilities are incorporated in cash flow forecasts for liquidity management purposes and determining future borrowing requirements. 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 its credit rating agency, investors and financial institutions. Lease and guarantee transactions that expose Council to financial liability are considered to be immaterial, and are therefore not required to be actively managed as part of the risk control limits contained within this Policy.

4.1 Purpose

The Liability Management Policy outlines the principles that Council follows to manage the risk associated with Council's borrowing programme. Namely:

- The re-pricing risk involved with financing new and/or existing debt at acceptable rates (fees and borrowing margins), and on the same terms as existing debt.
- The ability to refinance or raise new debt at a future time by maintaining market confidence in the creditworthiness and integrity of Council as a borrower.

Council borrows funds as it determines by resolution arising from the Long term planning and Annual planning processes, with projected future debt levels arising from cash flow and debt forecasting undertaken during these planning processes. Council raises debt for a number of different purposes including:

- To fund capital expenditure for new assets relating to additional demand, new levels of service and/or growth and those that require intergenerational funding.
- Short term working capital.

- Special projects as determined from time to time by Council.

4.2 Objectives

The objectives of the Liability Management Policy are consistent with local authority sector best practice, and will take into account Council's Long Term Plan ("LTP"). The key objectives in relation to borrowings are to:

- Prudently manage Council's external borrowing activities to ensure Council remains adequately funded on an ongoing basis.
- Borrow only under Council approved facilities and as permitted by this Policy.
- Minimise external borrowing costs within risk management control limits.

4.3 Borrowing Limits

Total Council borrowings will be managed within the following limits, in line with LGFA requirements:

(Covenants are measured on Council only, not on the consolidated basis).

Ratio	Council Limit	LGFA Limit
Net Debt/Total Revenue	<250%	<280%*
Net Interest/Total Revenue	<20%	<20%
Net Interest/Annual Rates Income	<25%	<30%
Liquidity [external debt + unutilised committed debt facilities + liquid funds to external debt]	>110%	>110%

*LGFA Net Debt/Total Revenue covenant is currently 290% for the financial year ending 30 June 2024, declining by 5% each financial year until 280% is reached in the financial year ending 30 June 2026.

4.4 Definitions Relating to Borrowing Limits

- Total revenue is defined as earnings from rates, external grants and subsidies, user charges, interest, dividends, development contributions, financial and other revenue income, excludes non-government capital contributions (e.g. vested assets).
- Net debt is defined as total debt less liquid funds, including LGFA borrower notes.
- Net interest is defined as total interest expenses less interest income, excluding interest income from debt on lending to CCOs.
- CCOs are defined as Council Controlled Organisations, in which Council controls 50% or more of the votes or has the right to appoint 50% (or more) of directors or trustees.
- Liquid funds are cash and cash equivalents defined as being:
  - Overnight bank cash deposits.
  - Wholesale/retail bank term deposits no greater than 30 days.
  - Registered Certificate of Deposit with a term of no greater than 180 days
- Bank term deposits linked to prefunding of upcoming maturing term debt exposures cannot be included in liquid funds as they are encumbered.
- Annual rates income 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 from other local governments for services provided and for which the other Local Governments rate.

4.5 Asset Management Plans

In approving new borrowings, Council will consider the impact on its external borrowing limits as well as the economic life of the asset that is being funded, and its overall requirement to match the funding of assets over their economic life/period of benefit to best achieve intergenerational equity objectives.

4.6 Borrowing Mechanisms

Council is able to borrow externally through a variety of different market mechanisms including issuing directly into the short and long term wholesale/retail debt capital markets (e.g. FRNs, bonds, and commercial paper), direct bank borrowing, and accessing the LGFA. In evaluating strategies for new borrowing (in relation to source, term, size and pricing), Council takes into account the following:

- Available terms from banks, the LGFA and debt capital markets.
- Council's overall debt maturity profile, to ensure concentration of debt is avoided at re-issue/rollover.
- Prevailing interest rates and bank/credit margins relative to term for debt issuance.
- The outlook on future interest rate and borrowing margin movements.
- Legal documentation and financial covenants together with security and credit rating considerations.
- For internally funded projects, to ensure that finance terms for those projects are at least as equitable as with those terms from external borrowing.
- Alternative funding mechanisms such as leasing should be evaluated with financial analysis in conjunction with traditional on balance sheet funding. The evaluation should take into consideration, ownership, redemption value and effective cost of funds.

Council's ability to readily attract cost effective borrowing is largely driven by its ability to:

- Maintain a strong balance sheet and ultimately its ability to rate. This means that in general terms, Council debt has a perceived credit quality just below that of the New Zealand Government.
- Service loans as interest and principal amounts fall due.
- Have diversified funding sources and maturity dates to avoid one off event risk unduly impacting on overall interest expense levels.
- Manage its image in the marketplace and its relationship with banks, brokers and investors.

Council will not enter into any borrowings in denominated in a foreign currency.

4.7 New Zealand Local Government Funding Agency Limited (LGFA)

Despite anything earlier in this Policy, the Council may borrow from the 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, e.g. LGFA borrower notes.
- Provide guarantees of the indebtedness of the 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.
- 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.
- Subscribe for shares and uncalled capital in the LGFA.

4.8 Debt Repayment

The funds from all asset sales, operating surpluses, grants and subsidies will be applied to the reduction of debt and/or a reduction in borrowing requirements, unless Council specifically directs that funds will be put to another use.

Debt will be repaid as it falls due in accordance with the applicable loan agreement. Subject to the debt limits, a loan may be rolled over or renegotiated, as and when, appropriate. In certain circumstances (where market interest rates allow), Council may repurchase and cancel existing borrowings before maturity.

4.9 Security

Security will usually be provided to banks for the provision of debt facilities and treasury products and also to other investors in Council's debt. Council's external borrowings and interest rate management instruments will generally be secured by way of a charge over rates and rates revenue, 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 Rating Act. This security offered by Council ranks equally (pari passu) with other lenders.

From time to time, and only with Council approval, security may be offered by providing a charge over one or more of Council's assets.

Physical assets will only be charged where:

- There is a direct relationship between the debt and the purchases or construction of the asset that it funds (e.g. project finance).
- Council considers a charge over physical assets to be appropriate.

Any pledging of physical assets must comply with the terms and conditions contained within the security arrangement.

Utilisation of internal funds for internal borrowing purposes will be on an unsecured basis.

4.10 Guarantees/Contingent Liabilities and Other Financial Arrangements

The Council may act as a guarantor to financial institutions on loans or enter into incidental arrangements for organisations, clubs, Trusts, or Business units when the purposes of the loan are in line with Council's strategic objectives. Council is not allowed to guarantee loans to Council controlled trading organisations (CCTOs) under Section 62 of the Local Government Act.

Financial arrangements include advances to community organisations.

Council will ensure that sufficient funds or lines of credit exist to meet amounts guaranteed. Guarantees given will not exceed any amount agreed by Council or an appropriate council committee in aggregate. All guarantees will be reported as part of the Quarterly Treasury Report.

4.11 Borrowing Intra Group

Council's debt is managed on a centralised basis as the parent of its subsidiaries.

Where Council has a borrowing requirement for specific projects or activities, internal cash resources may be utilised first before any funds are borrowed externally.

Council is able to facilitate cost effective external borrowings if required for Council Controlled Organisations (CCOs) by way of its standing in the market place, and can accordingly provide a financial benefit to CCOs. Council can pass funding on to CCOs at cost, or include a margin to reflect its support as approved by Council.

If funds are raised by Council for the specific purpose of funding a CCO, then these funds cannot be provided below cost to Council.

From time to time Council may provide direct financing to CCOs to assist in cash flow management, which will be advanced at Council's average cost of funds.

4.12 Lending to Council Controlled 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 on-lending arrangement to a CCO or CCTO must be approved by Council. In recommending an arrangement for approval the CFO 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), lending covenants 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 or 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 of on-lending arrangement.

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

5.0 Investment Management Policy

5.1 Introduction

Council seeks to minimise the risks associated with its investments to avoid placing the capital value of individual investments at risk. Council does not undertake any unnecessary or speculative investment activity.

Investments and associated risks are monitored, managed and regularly reported to Council.

Specific purposes for maintaining investments include:

- For strategic purposes consistent with Council’s LTP.
- To reduce the current ratepayer burden.
- The retention of vested land.
- Holding short term investments for working capital and liquidity requirements.
- Holding investments that are necessary to carry out Council operations consistent with Annual Plans and the Long Term Plan, to implement strategic initiatives, or to support inter-generational allocations.

Invest amounts allocated to accumulated surplus, Council created restricted reserves and general reserves.

- Invest proceeds from the sale of assets.

Council recognises that as a responsible public authority, all investment held should be low risk. Council also recognises that low risk investments generally mean lower returns.

5.2 Objectives

The objectives contained within this Investment Policy are consistent with market best practices, and will take into account the requirements of Council’s Annual and Long Term Plans. Council's key investment policy objectives are to:

- Prudently manage its financial investments by seeking to maximise investment income within acceptable investment risk parameters. Council, as a public entity, is risk averse and as such will have a primary focus on preservation of capital, despite this meaning a level of return that may be lower than could be achieved by investing in 'speculative riskier' assets.
- Manage investments in accordance with the Local Government Act 2002 and the Trusts Act 2019; administer, manage and account for its funds and exercise the care, diligence and skill that a prudent person of business would exercise in the managing affairs of others.
- Invest in only those investments that are approved under this policy maintain an appropriate level of diversity. Accordingly, only creditworthy counterparties are acceptable.
- Support the Council's liquidity requirements.

- Minimise the potential risk due to adverse interest rate movements.
- Enable regular reviews of the performance (risk and return) of investments.
- Maintain operational controls and procedures that protect the Council against financial loss, opportunity cost and other inefficiencies.

5.3 Policy

Council's general policy on investments is that

- Council may hold financial, property, forestry, and equity investments if there are strategic, economic or other valid reasons (e.g. where it is the most appropriate way to administer a Council function).
- Council will keep under review its approach to all investments and the credit rating of approved financial institutions.
- Council will review its policies on holding investments at least every three years.

5.4 Mix of Investments

Council has investments in equity and debt securities. The Council's equity investments include holdings in CCOs and other entities where there is a specific strategic objective for holding the investment, or the investment is required to comply with legislation. Council may invest in shares of the LGFA and may borrow to fund that investment.

Council's debt investments include treasury assets, such as cash or cash equivalent investments, loan advances and LFGA equity related requirements. Council holds other debt investments, each tagged for specific purposes, which may include loans to CCOs.

5.5 Specific Investments

Council considers its specific equity investments (presented in the table below) as representing the best interests of the community and ratepayers. Council's exposure to risk would be that of any other financial shareholder. Specific investments include the following:

Company	Council Shareholding	Principle Reason for Investment	Budgeted Return
Rotorua Economic Development Limited	100%	Economic Development	Nil
Rotorua Regional Airport Limited	100%	Economic Development	Nil
Infracore Limited	100%	Efficient Government	Nil
Waikato Local Authority Shared Services Limited	6.14%	Efficient Government	Nil
BOP LASS Limited	16.13%	Efficient Government	Nil
Civic Financial Services Limited	<1%	Risk Management	Nil
Mountain Bike Events Limited	49%	Economic Development	Nil

5.6 Acquisition of New Investments

New equity investments are approved by Council acting on the recommendation of the appropriate Council committee. In general, it is not Council's policy to acquire equities solely for investment purposes, except where those equities are purchased as a part of a perpetual or externally managed investment portfolio, or where arrangements are entered into that mitigate financial risks associated with the investment.

Loan advances may be made from time to time to assist Council to achieve its investment objectives and Council outcomes. Council approval is required for all loan advances, and all advances must meet statutory requirements including the requirements of Section 63 of the Local Government Act 2002 in relation to concessionary interest rates. Any loans related to community organisations will be on a commercial basis.

5.7 New Zealand Local Government Funding Agency Limited Investment

Despite anything earlier in this Policy, Council is able to enter into a commitment that could result in it becoming a shareholder in the New Zealand Local Government Funding Agency Limited (LGFA). In borrowing from the LGFA, Council can agree to the issue of borrower notes to the value of 1.6% of the total amount borrowed (if drawn down between the period 2011 and May 2020) thereafter the value is increased to 2.5% for any additional lending from that date. These will be held by the LGFA while the borrowing is outstanding and may in certain scenarios convert to shares in the LGFA. Also, as a Guaranteeing Local Authority, Council is required to commit to subscribe for redeemable shares in the LGFA in certain circumstances. As the LGFA is a Council Controlled Organisation (CCO), Council has undertaken specific consultation to satisfy the requirements of Section 56 of the Local Government Act 2002.

Council's objective in making any such investment will be to:

- Obtain a return on the investment.
- Ensure the LGFA has sufficient capital to remain viable, meaning that it can continue to be a source of debt funding for Council,

Because of these dual objectives, Council may invest in LGFA shares in circumstances where the return on that investment is potentially lower than the return available with alternative investments.

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

5.8 Investment Risks

This Treasury Policy sets operating parameters for financial investment activity including approved counterparties, instruments and limits. The following principles form the key assumptions of the operating parameters contained in the investment framework:

Credit risk is minimised by placing maximum limits for each broad class of non-government issuer (excluding LGFA), and by limiting investments to local authorities and registered banks within prescribed limits

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

Council may only make financial investments in approved creditworthy counterparties.

Council's financial investments give rise to a direct exposure to a change in interest rates, impacting the return and capital value of its investments. For investments in excess of 12 months the Treasury Management Group implements an interest rate risk management strategy by reviewing rolling cash flow forecasts and adjusting the maturity of its investments, as appropriate.

6.0 Risk Recognition, Identification and Management

The definition and recognition of interest rate, liquidity, funding, counterparty credit, market, operational and legal risks of Council is detailed below and applies to both the Liability Management Policy and the Investment Policy.

7.0 Interest Rate Management

Council's ongoing borrowing requirement gives rise to direct exposure to interest rate movements. Interest rate risk management refers to managing and minimising the impact that unfavourable movements in market interest rates can have on Council's cash flows, underpinning its Annual Plan and Long-term Plan. This impact can be both favourable and unfavourable

The primary objective of interest rate risk management is to reduce uncertainty relating to interest rate movements through fixing of debt funding costs. Certainty around interest costs is to be achieved through the ongoing management of underlying interest rate exposures.

Interest rate risk can be managed by way of fixed and floating rate term debt, and also by using interest rate risk management instruments that allow the re-profiling of the floating rate part of the debt portfolio.

Fixed rate, longer term borrowing can mitigate interest rate re-pricing risk. This risk exists where a long-life asset is funded by floating rate and either the asset produces a fixed income stream that cannot be easily re-priced in line with changing interest rates, or debt repayments which are funded from a fixed income source (e.g. a targeted rate) which will not be re-priced regularly.

All risk management activity must relate to the underlying external debt forecast amounts of the Council .The buying and selling of risk management instruments for the primary purpose of generating premium income is not permitted because of its speculative nature.

7.1 Interest Rate Risk Control Limits

The following table details control limits for the allowable floating/fixed rate mix. The table reflects Council's preference for a reasonable level of certainty over interest costs, over multiple time periods, given the long term inter-generational nature of assets being funded. The fixed rate percentage at any point in time should be within the following maturity bands:

Debt Interest Rate Policy Parameters (calculated on a rolling monthly basis):		
Term of Exposure	**Minimum Fixed Rate Exposure**	**Maximum Fixed Rate Exposure**
Current Year	0%	90%
Year 1	40%	90%
Year 2	35%	85%
Year 3	30%	80%
Year 4	25%	75%
Year 5	0%	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 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.

A fixed rate maturity profile that is outside the above limits, however self corrects within 90 days is not in breach of this Policy. Maintaining a maturity profile that is outside the above limits for longer than 90 days requires specific approve by Council.

Gross forecast external core debt is the amount of 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. Forecast debt does not include pre-funded debt amounts.

The CFO or delegate can consider alternative debt forecast scenarios that make assumptions around such matters as, the delivery and timing of the capital expenditure programme when designing and approving the interest rate strategy.

Any debt raised and on-lent to CCO/CCTOs is included in the forecast gross external debt amount and the related interest rate risk is managed within the limit framework. If fixed rate debt was raised, then the fixed rate amount would be included within the fixed rate/hedging interest rate risk position.

Interest rate swap maturity is limited by the maximum offered LGFA Bond maturity, beyond this approval is required by Council.

8.0 Liquidity Risk/Funding Risk

8.1 Risk Recognition

Cash flow deficits in various future periods based upon long term financial forecasts are reliant upon the maturity structure of cash, financial investments, term loans and bank facilities. Liquidity risk management focuses on the ability to access committed funding at that future time to fund the gaps. Funding risk management centres on the ability to refinance or raise new debt at a future time at acceptable pricing (fees and borrowing margins) and maturity terms. .

The prudent management of Council's borrowings is important because several risk factors can arise, which cause adverse movements in borrowing margins, term availability and general flexibility including:

- Local government risk is priced to a higher fee and margin level.
- Council's own credit standing or financial strength as a borrower deteriorates due to financial, regulatory or other reasons.
- An individual lender to the Council experiences their own financial/exposure difficulties resulting in Council not being able to manage their debt portfolio as optimally as desired.
- New Zealand investment community experiences a substantial 'over supply' of Council investment assets.
- Financial market shocks from domestic or global events.

Where possible, Council seeks a diversified pool of borrowing and ensures that bank borrowings are only sought from approved strongly rated New Zealand registered banks.

A key factor of funding risk management is to spread and control the risk to reduce the concentration of funding maturities at one point in time so that if one off external negative credit events occur, the overall borrowing cost (through adverse credit margin movement) is not materially increased and general flexibility reduced.

8.2 Liquidity/Funding Risk Control Limits

Council must approve all external borrowing through the adoption of the Annual Plan.

Alternative funding mechanisms such as leasing should be evaluated with financial analysis in conjunction with traditional on-balance sheet funding. The evaluation should take into consideration, ownership, redemption value and effective cost of funds.

The following guidelines have been established to provide Council with appropriate levels of liquidity at all times:

- Cash flow forecasts are produced to assist in the matching of operational and capital expenditure to revenue streams and borrowing requirements.

- Council will maintain its financial investments in liquid instruments and within credit exposure limits detailed in this Policy.
- To minimise the impact of unexpected cash surpluses, Council will take advantage of the efficiencies of maintaining floating rate bank facilities to assist in overall working capital management.
- External debt, together with liquid funds and unutilised committed debt facilities must be maintained at an amount of at least 110% over the Plan current external debt.

Council has the ability to prefund up to 18 months forecast external debt requirements including debt re-financings and invest any cash surpluses with approved counterparties for a term of no more than 18 months.

Once debt has been refinanced with a contracted term deposit (pre-funded), the term deposit amount, will net off the maturing debt amount, from the funding maturity profile percentage calculation.

External debt that is raised by Council to be on-lent debt to CCO/CCTO's is included in the funding maturity profile percentage calculation. The offsetting CCO/CCTO loan asset is not included in the debt funding maturity profile.

The CFO or delegate has the discretionary authority to refinance existing debt on more favourable terms. Such action is to be reported and ratified by Council at the earliest opportunity.

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

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 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, a maturity schedule outside these limits for greater than 90 days will require specific Council approval.

9.0 Approved Financial Instruments

Category	Instrument
Cash management and borrowing	Bank overdraft Committed cash advance and bank accepted bill facilities Fixed Rate Bond (Medium Term Note/Bond) and Floating Rate Note (FRN) Retail and wholesale debt security Commercial paper (CP) Financial and operating leases
Investments (term <12 months)	Call deposits Bank term deposits Registered Certificates of Deposit (RCD)
Investments (>12 months)	LGFA borrower notes Bank term deposits (linked to prefunding activity)

Interest rate risk management	Forward rate agreements (FRAs) on bank bills Interest rate swaps including: Forward start swaps (start date <36 months, unless linked to existing maturing swaps with notional amounts not exceeding maturing swap. Amortising swaps (whereby notional principal amount reduces). Swap extensions 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 with matching notional values only).
Foreign exchange risk management	Spot exchange contracts Forward exchange contracts

Conditions of instrument use:

Interest rate options must not be sold outright. However, 1:1 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, one side of the collar cannot be closed out by itself, both must be closed simultaneously. The sold option leg of the collar structure must not have a strike rate "in-the-money".

Interest rate options with a maturity beyond 12 months that have a strike rate (exercise rate) higher than 2.0% above the appropriate swap rate, cannot be counted as part of the fixed rate cover percentage calculation.

Any other financial instrument must be specifically approved by Council on a case-by-case basis, and only applied to the one singular transaction being approved. Credit exposure on these financial instruments is restricted by specified counterparty credit limits. The following types of investment instruments are expressly excluded:

Structured debt where issuing entities are not a primary borrower/issuer.

Subordinated debt (other than Borrower Notes subscribed from the LGFA), junior debt, perpetual notes and hybrid notes such as convertibles.

10.0 Counterparty Credit Risk

Counterparty credit risk is the risk of losses (realised or unrealised) arising from a counterparty defaulting on a financial instrument where Council is a party. Prudent credit management can reduce Council's risk of loss from a counterparty failing to meet its obligations. The credit risk to Council in a default event will be weighted differently depending on the type of instrument entered into.

Credit exposure for borrowings is relevant for the undrawn portion of any committed standby or bank facility, where the counterparty has a contractual obligation to provide funds to Council. Where Council uses these facilities, the counterparty's minimum credit rating must be A1 (short term) or A (long term) as rated by S&P Global Ratings or equivalent credit ratings from Moody's or Fitch Ratings.

Credit risk will be regularly reviewed by Council. Treasury related instruments will only be entered into with organisations specifically approved by Council.

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

The following matrix guide will determine limits:

Counterparty/Issuer	Instruments	Minimum short term credit rating (<12 months)	Minimum long term credit rating (>12 months)	Maximum exposure per counterparty
NZ Government	Treasury Bills, NZ government bonds	N/A	N/A	Unlimited
LGFA	LGFA borrower notes, commercial paper	N/A	N/A	$34.0m
NZ registered bank	Bank deposits, interest rate and foreign exchange contracts	A-1	AA- A	$30.0m $21.0m

The equivalent dollar value for maximum counterparty credit exposures is updated annually based upon the most recent audited financial statements. The percentages used for these calculations are presented below:

- LGFA: 40%.
- NZ registered bank (AA-): 35%.
- NZ registered bank (A): 25%.

The calculation methodology for Council's exposures is outlined below. For the purposes of these calculations, when replacement cost (marked-to-market) is below zero (i.e. negative) the value used in the calculation will be zero (prescribed factors are displayed in the following table):

- Investments (such as bank deposits) – Replacement Cost + Notional x Prescribed Factor
- Interest rate risk management contracts (such as swaps, FRAs) – Replacement Cost + Notional x Prescribed Factor
- Foreign exchange risk management contracts (such as FECs) – Replacement Cost + Notional x Prescribed Factor

Current term to maturity	Treasury Investments	Interest rate contracts	Foreign exchange contracts
Less than one year	100%	0.0%	10.0%
Between one and five years	100%	0.5%	12.0%
Longer than five years	100%	1.5%	15.0%

11.0 Foreign Exchange Exposures

Council may have foreign exchange exposure through the occasional purchase of foreign exchange denominated assets or foreign currency denominated expenses in order to access particular assets or services. Individual commitments in excess of NZD 100,000 are defined as an exposure. Foreign exchange exposures may be hedged using spot and forward exchange contracts with approved New Zealand Registered banks once expenditure is approved by the CFO and/or Council.

12.0 Operational Risk

Operational risk is the risk of loss as a result of human error (or fraud), systems failures or inadequate processes, procedures or controls.

12.1 Dealing Authorities and Limits

Transactions will only be executed by those persons within limits approved by Council.

12.2 Segregation of duties

Adequate segregation of duties among the core borrowing and investment functions of deal execution, confirmation, setting and accounting/reporting. When there are a small number of people involved in borrowing and investment activity, the strict segregation of duties is not always achievable.

12.3 Legal risk

Legal and regulatory 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 also be exposed to such risks. Council will undertake the following to minimise legal risk:

- The use of standard dealing and settlement instructions (including bank accounts, authorised persons, standard deal confirmations, contracts 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 for any non-standardised transactions.

12.4 Agreements

Financial instruments can only be entered into with banks that have in place an executed ISDA Master Agreement with Council. All ISDA Master Agreements for financial instruments must be signed under seal by Council.

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

13.0 Performance Measurement

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

Those 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 basis.

13.1 Operational Performance

The performance of the borrowing activity will be measured against pre-determined benchmarks:

- Adherence to Policy and in particular borrowing limits.
- Comparison of actual monthly and year to date borrowing costs v budget borrowing costs.
- Comparison of actual monthly borrowings amounts with budgeted borrowings amounts.
- Comparison of actual borrowing limit ratios (both Council and LGFA) to budgeted borrowing limit ratios as per the Annual Plan and Long Term Plan.

14.0 Reporting

The CFO has responsibility for ensuring appropriate reporting of the Treasury function is completed for senior management and Council, to ensure they can meet their oversight requirements as detailed within this Policy, and to effectively monitor performance. Reporting requirements are agreed or confirmed annually with the CEO and Council.

Reporting is expected to include appropriate summaries showing compliance against key policy risk parameters with exception reporting, as soon as one is recognised. Commentary should be limited to that which assists recipients to readily understand the impact of any decisions they are being requested to make.

The following reports are to be produced:

Report Name	Frequency	Prepared by	Recipient
Daily Cash Position Treasury Spread Sheet	Daily	Accountant	Finance Manager
Treasury Exceptions Report	As required	Accountant	Director of FInance

Monthly Treasury Report (signalling significant changes in treasury management strategy)	Monthly	Finance Manager	Chief Financial Officer
Quarterly Treasury Report Policy limit compliance Borrowing limits Funding and interest rate position Funding facilities New treasury transactions Cost of funds v budget Cash flow forecast report Liquidity risk position Counterparty credit Treasury performance Outstanding guarantees and loan advances	Quarterly	Director of Finance Chief Financial Officer	Council
Half-Yearly Financial Statements	Six monthly		Council
Half Yearly Reporting Certificate	Six monthly		Council
Annual Report	Annual		Council
Annual Reporting Certificate	Annual		Council
Auditors Report	Annual		Council
Insurance Certificate	Annual		Council
Annual Plan/Long Term Plan	Annual/Triennially		Council
Revaluation of Financial Instruments	Quarterly		Council
LGFA Compliance Report	Annual / As required		Council

15.0 Treasury Management Group (TMG)

The TMG exists to ensure the following:

- Compliance with the Treasury Policy.
- Ensure operational controls and procedures protect Council against financial loss and opportunity cost, and ensure other inefficiencies are mitigated or maintained
- Monitor, evaluate and report on treasury performance.

A key responsibility is to evaluate borrowing opportunities. In evaluating borrowings, the TMG will consider the following:

- The overall structure of Council borrowings, having regard to the principle of intergenerational equity.
- The impact of the new debt on borrowing limits taking into account long term debt projections and the potential impact of new debt on Council financial ratios, and the impact of new debt on the sustainability of overall debt service costs.
- Relevant margins under each borrowing source.

- Prevailing interest rates relative to the term of borrowing.
- The term of borrowing.
- Legal compliance and financial covenants.
- Other terms and conditions.

The core members of the TMG are as follows:

- Chief Financial Officer.
- Financial Controller.
- Business Performance Manager.

The CEO is invited to attend all TMG meetings, but is not a permanent member, as are representatives of Council's independent treasury advisor (if one is appointed).Other Council officers and Council's internal treasury advisors are invited to attend as required.

16.0 Accounting Treatment of Financial Instruments and Valuations

Council uses financial market instruments for the primary purpose of reducing its exposure to fluctuations in interest rates. The accounting treatment for such financial instruments is to follow New Zealand Generally Accepted Accounting Practice and it detailed in the Accounting Manual.

Under NZ IPSAS accounting standards, changes in the fair value of derivatives go through the Income Statement unless derivatives are designated in an effective hedge relationship.

All financial instruments must be revalued (marked-to-market) quarterly for risk management purposes.

17.0 Policy Review

This Policy is to be formally reviewed at least every three years, in conjunction with the Long Term Plan process, or earlier if required.

The CFO has the responsibility for reviewing a review report to be presented to Council for consideration and approval.

The report should include:

- Recommendations as to changes, deletions and additions to the Policy.
- Overview of how the treasury function has been achieving its stated treasury objectives.
- Summary and review of breaches and one off approvals outside Policy to highlight areas of tension.