Investment Policy

1. Background

Section 102(2)(c) of the Local Government Act 2002 (the "Act") requires the Council to adopt an investment policy (the "Policy"). Section 105 of the Act outlines the contents of such a policy.

A policy adopted under Section 102(2)(c) must state the local authority's policies in respect of investments, including;

(a) the mix of investments; and
(b) the acquisition of new investments; and
(c) an outline of the procedures by which investments are managed and reported on to the local authority; and
(d) an outline of how risks associated with investments are assessed and managed.

2. Strategic alignment

The development of the Policy statement aligns with the Council's strategy to establish a high-performing organisation with a focus on customer service, prudent financial management, quality processes, and a skilled and motivated work force.

Furthermore, Section 101(1) of the Act states:
A local authority must manage its revenues, expenses, assets, liabilities, investments, and general financial dealings prudently and in a manner that promotes the current and future interests of the community.

3. Implementation

In implementing the Policy, the Council is guided by the principles set out in Section 14(1) (f) and (g) of the Act that state;

- *a local authority should undertake any commercial transactions in accordance with sound business practices, and,*
- *a local authority should ensure prudent stewardship and the efficient and effective use of its resources in the interests of its district or region.*

4. Delegated authorities (as approved by the Council)

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 (LTP) remains the sole responsibility of the Council. This responsibility cannot be delegated.

Approved delegations to officers are contained within the Council's delegations register. The Investment Policy related delegations are outlined in Appendix 1.

5. Risks

Adoption of the Policy is a statutory requirement and failure to do so would place the Council in breach of its statutory obligations and undermine the validity of all future Council investments.

6. Measurement and review

The Policy is reviewed in alignment with the LTP.

Measuring the effectiveness of the Policy will be achieved through a mixture of subjective and objective measures.

The predominant subjective measure is the overall quality of investment information. The Chief Executive has prime responsibility for determining this overall quality.

7. Policy statements

7.1. General policy including objectives

The Policy is to be consistent with the LTP and Annual Plans. The Council generally holds investments for strategic reasons where there is some community, social, physical or economic benefit accruing from the investment activity. Generating a commercial return on strategic investments is considered a secondary objective. The Council's overriding investment objectives are to:

- Manage investments in a manner consistent with current governing legislation and Council's strategic and commercial objectives.
- Optimise returns while minimising credit and liquidity risks.
- Manage the overall cash position of the Council's operations.
- Hold investments that are necessary to carry out Council operations consistent with Annual Plans, to implement strategic initiatives, or to support inter-generational allocations.
- Hold assets for commercial returns.
- Provide ready cash in the event of a natural disaster. The use of which is intended to bridge the gap between the disaster and the reinstatement of normal income streams and assets.
- Invest amounts allocated to accumulated surplus, Council created restricted reserves and general reserves.
- Invest proceeds from the sale of assets.
- Maintain professional relationships with the Council's bankers, the Local Government Funding Agency (LGFA) and financial institutions.
- Monitor, evaluate and provide timely and accurate reporting of treasury activity and performance.
- Ensure adequate internal controls exist to protect Council’s financial assets and to prevent unauthorised transactions.

The Council's philosophy on the management of investments is to optimise returns in the long term while balancing risk and return considerations. The Council recognises that as a responsible public authority any investments that it does hold should be low risk where the primary objective when investing is the protection of its investment capital. Accordingly, only approved creditworthy counterparties are acceptable and Council recognises that lower risk generally means lower returns in its investment activity, Council will act effectively and appropriately to;

- protect the Council’s investments;
- ensure the investments benefit the Council’s ratepayers;
- maintain a prudent level of liquidity and flexibility to meet both planned and unforeseen cash requirements.

7.1.1. Strategic Investment Fund

The Strategic Investment Fund (SIF) is managed in line with a separate Statement of Investment Policy and Objectives (SIPO) document. External fund managers will be appointed to operate the portfolio according to the investment guidelines outlined in the SIPO.

The Council will be responsible for the following:

- Setting the fund's investment strategy, including the level of risk and investment performance objectives, and investment policies.
- Determining the appropriate number of investment managers, and selecting and changing those managers as appropriate after having taken advice from the investment consultant.
- Reviewing the SIPO annually, including the investment strategy, policies and external investment manager configuration.
- Ensuring that the level of redemptions from the fund is consistent with the fund's objective to maintain equity, in terms of amounts available for distribution, between present and future generations.
- Providing cash flow information with respect to future deposits and redemptions.

Financial instruments and credit restrictions for funds under management in the SIF are separate to that within the Policy as per the Council approved SIPO.

7.1.2. Equity investments

Council does not hold equity investments in its own name, rather all equity investments are externally managed by Council's appointed investment manager in accordance with the SIPO. However, the Council may hold equity for non-investment purposes, provided that the holding is in furtherance of its community well-being objectives as outlined in the LTP, and may include investments held in CCO/CCTO and other shareholdings.

7.1.3. Property investments

The Council's first objective is to only own property that is strategically necessary for the economic, physical and social development of Thames-Coromandel District, and secondly, to achieve an acceptable rate of return.

Under the Council's Leasing Policy, property held for social development purposes, is leased out to qualifying organisations at set rental rates considerably below that which could be achieved if commercial rental rates were applied.

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. Proceeds from the disposition of property investments are used firstly for retirement of debt relating to such property.

7.1.4. Loans and advances

The Council is not generally involved in providing loans or advances. However, on occasion it may be appropriate for the Council to be involved in this activity in which case a resolution of the Council is required to approve the loan or advance.

The Council may also lend money internally to its activity centres as set out in the Liability Management Policy Section 7.5.

As outlined in Section 63 of the Act, the Council does not lend money, or provide any other financial accommodation, to a council controlled trading organisation (CCTO) on terms and conditions that are more favourable to the CCTO than those that would apply if the Council were (without charging any rate or rate revenue as security) borrowing the money or obtaining the financial accommodation.

7.1.5. Postponed rates

This "investment" in postponed rates is secured by way of a statutory land charge on the individual properties upon which rates postponement has been granted. Interest is charged on postponed rates at the Council's base rate of borrowing plus a 1% management fee and a 0.25% reserve contribution. Postponed rates are disclosed separately in the Council's statement of financial position.

7.1.6. Treasury financial investments

The Council maintains financial investments to;

- invest surplus cash and working capital funds;
- invest amounts allocated to trust funds and special funds.

Normally financial investments are held to maturity date. Proceeds from the disposition of financial investments are used for operational expenditure purposes, or other purposes approved by the Council in the annual planning process.

Treasury financial investment parameters
The Council's primary objective when investing is the protection of its investment. Accordingly, only creditworthy counterparties are acceptable. Creditworthy counterparties (excluding government and LGFA) are selected on the basis of their current Standard and Poor’s (S&P) or equivalent rating (by Fitch or Moody’s), which must be strong or better[1].

Within the above credit constraints, the Council also seeks to;

- maximise investment return;
- ensure investments are liquid.
- spread investments in line with cash flow requirements to avoid the need for realisation prior to maturity;
- manage potential capital losses due to interest rate movements if investments need to be liquidated before maturity.

Therefore, to have funds available when needed Council ensures that:

- there is sufficient available operating cash flow and committed bank facilities to meet cash flow requirements between rates instalments as determined by the Finance Manager;
- external term debt plus committed bank/loan facilities plus available liquid investments/cash equivalents are maintained at 110% over existing external debt levels.;
- investments have a maturity of no more than 180 days (unless linked to a pre-funding strategy).

7.2. New Zealand LGFA investment

Despite anything earlier in this Policy, Council may invest in shares and other financial instruments of the LGFA, and may borrow to fund that investment.

7.3. Mix of investments (Section 105(b) of the Act)

The Council invests in the following mix of investments that include;

- strategic investment fund (refer section 7.1.1);
- equity investments (refer Section 7.1.2);
- property investments (refer Section 7.1.3);
- loans and advances (including internal borrowing) (refer Section 7.1.4);
- postponed rates (refer Section 7.1.5);
- treasury financial investments (refer Section 7.1.6).

[1] A strongly rated counterparty is defined in section 7.4

Treasury financial investments are managed within the limits outlined in 7.4. Typical treasury financial investment issuers include;

- New Zealand government;
- LGFA;
- registered New Zealand banks.

Approved financial instruments are;

- call and short term bank deposits;
- bank certificates of deposit (RCD's);
- LGFA commercial paper (CP), bills, secured bonds, or borrower notes;
- bank CP and secured bonds.

Any term greater than 181 days requires the Council's approval; an exception to this is the holding of LGFA borrower notes and any term deposit investments linked to pre-funding activity. For further information and definitions see Section 8 of this policy.

7.4. Investment and interest rate risk management

The Council ensures that all investment and interest rate risk management is undertaken with institutions that are of high quality credit to ensure amounts owing to the Council are paid fully and on due date.

More specifically, the Council minimises its credit exposure by;

- ensuring all investment, cash management, interest rate risk management and any foreign exchange transactions are undertaken with entities (excluding government and some local authorities) that have a strong S&P credit rating;
- limiting total exposure to prescribed amounts;
- spreading exposures amongst a number of counterparties to avoid concentrations of credit exposure;
- monitoring compliance against set limits.

The following table summarises credit requirements and limits.

Institution	Minimum S&P Short-term Credit Rating	Minimum S&P Long-term Credit Rating	Total Exposure Limit for each Counter- party	Portfolio Limit (up to)
Government	N/A	N/A	Unlimited	100%
Local Government Funding Agency	N/A	N/A	Unlimited	100%
NZ Registered Bank Financial Investments	A-1	A	$8 million	100% (while total financial investments do not exceed $20 million and thereafter 80%)
NZ Registered Bank Risk Management Instruments	A-1	A	$8 million	N/A

*Counterparty credit risk for investments made within the SIF are managed in line within the SIPO rather than the above table.

If any counterparty's credit rating falls below the minimum specified in the above table, then all practical steps are taken to reduce the credit exposure to that counterparty to zero as soon as possible. Counterparties exceeding limits are reported to Council.

Exposures to each counterparty are computed as follows:

Financial investments

- Total amounts invested with that counterparty.

Risk management instruments (see Section 8.2 of this policy)

- Credit exposure on interest rate contracts computed by multiplying face value of outstanding transactions by an interest rate movement factor of 3% per annum. i.e. Notional amount * maturity (years) * 3%.
- Credit exposure on foreign exchange contracts computed by multiplying the face value amount by the (square root of the remaining maturity (years) x 15% per annum).

Each transaction is entered into a reporting spreadsheet and a monthly report prepared to show assessed counterparty actual exposure versus limits.

7.5. Acquisition of new investments (Section 105(c) of the Act)

The Council's policy for acquisition of new financial instruments is the same as for the mix of investments (Section 7.3) and within the counterparty limits as outlined in 7.4.

Acquisition of new equity investments must be by Council resolution. New advances or loans must be by Council resolution. Property purchases will be approved in the LTP or Annual Plan, or, by resolution of the Council.

Nothing in this policy should limit the application of the Council's Policy on partnerships with the private sector.

7.6. Procedures for management and reporting (Section 105(d) of the Act)

7.6.1. Cash management

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 cash requirements are determined by reference to the daily money management report and appropriate adjustments are made to money market balances.

Generally cash flow surpluses from timing differences are available for periods less than 181 days and in approved instruments and counterparties.

Cash management activities must be undertaken within the following parameters:

- An optimal daily range of zero 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 commercial paper (promissory notes). Amounts invested must be within limits specified in 7.4.
- The Council has a committed bank overdraft facility with a limit of $250,000. However, this facility is used only in exceptional circumstances.
- The use of interest rate risk management instruments on cash management balances is not permitted.

Cash management reports are set out in Section 7.6.6.

7.6.2. Foreign exchange

The Council generally has minor foreign exchange exposure arising through the occasional purchase of foreign exchange denominated services, plant and capital equipment. Foreign currency payments are converted at the spot exchange rate on the date of payment.

Where there are significant capital project related foreign exchange commitments (greater than NZD100,000 equivalent) these are hedged based on the following system. When the expenditure is committed the exposure must be hedged with forward exchange contracts.

Capital expenditure - Foreign exchange risk control limits		
Time - point	Exposure must be covered by forward exchange contracts	Exposure may be covered by purchased foreign exchange options
1. CAPEX budget approved		Up to 50%
2. Specific tender/item approved		Up to 100%
3. Expenditure committed	Maximum of 100%	

7.6.2.1. Approved foreign exchange instruments

- Foreign currency deposits.
- Purchased currency options.
- Forward foreign exchange contracts.
- One for one Collars.

7.6.2.2. Use of foreign exchange instruments

- Financial instruments other than those stipulated in section 7.6.2.1 require one-off Council approval prior to transacting.
- Foreign exchange options cannot be sold outright.
- The purchase price paid for an option (premium) is to be amortised (spread) over the period of cover and added to the actual average exchange rate achieved by Council.
- It is important that all significant tenders allow bidders the opportunity to select desired currencies and where possible allow for suppliers to transparently link price escalations to clear financial market references.

The Council does not borrow or enter into incidental arrangements within or outside New Zealand in currency other than New Zealand currency. Council does not hold investments denominated in foreign currency.

7.6.3. Performance measurements

Measuring the effectiveness of the Council's investment and cash management activities is achieved through a mixture of subjective and objective measures. The predominant subjective measure is the overall quality of treasury management information. The Council has prime responsibility for determining this overall quality. Objective measures are as follows:

- Adherence to policy.
- For short-term investments, comparison of actual monthly and year-to-date accrued returns, with actual returns based on the weekly average three-month bank bill offer rate.
- All treasury limits are complied with including (but not limited to) counterparty credit limits, dealing limits and exposure limits.
- All treasury deadlines are to be met, including reporting deadlines.

Accounting Treatment for Financial Investment Instruments
As a general rule a financial asset is held to maturity and consequently accounted at cost but subject to annual impairment assessment.

7.6.4. Internal controls for borrowing, investment and cash management activity

The Council's systems of internal controls over investment activity include adequate segregation of duties among the core treasury functions of deal execution, confirmation, settling and accounting/reporting. 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.
- Regular operational risk control reviews by an independent audit function.
- Organisational, systems, procedural and reconciliation controls to ensure all borrowing, investment, interest rate and cash management activity is bona fide and properly authorised.
- Checks are in place to ensure the Council's accounts and records are updated promptly, accurately and completely.

All outstanding transactions are revalued regularly and independently of the execution function to ensure accurate reporting and accounting of outstanding exposures and hedging activity.

More specifically, key internal controls are as follows:

Cheque/Electronic banking signatories

- Positions approved by the Chief Executive.
- Dual signatures are required for all cheques and electronic transfers
- Cheques must be in the name of the counterparty crossed “Not Negotiable, Account Payee Only” or“ Not Transferable, Account Payee Only”, via the Council bank account.

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.

Recording of deals

- The Management Accountant records all deals on properly formatted deal tickets and are approved by the Finance Manager. Deal summary records for borrowing, investments interest rate risk management and cash management transactions are maintained on spreadsheets and updated promptly following completion of the transaction.

Confirmations

- All inward letter confirmations including LGFA, bank and registry confirmations are received and checked by the Financial Assistant against completed deal tickets and summary spreadsheets records to ensure accuracy.
- All negotiable bearer securities are held in the Council’s safe.
- Deals, once confirmed, are filed (deal ticket and attached confirmation) by the Financial Assistant in deal date/number order.
- Any discrepancies arising during deal confirmation checks, which require amendment to the Council's records, are signed off by the Finance Manager.

Settlement

- The majority of borrowing and investment payments are settled by direct debit authority.

- For electronic payments, batches are set up electronically. These batches are checked by the Financial Accountant to ensure settlement details are correct. Payment details are authorised by two approved signatories as per Council registers or by direct debit as per setup authority by Council.

Reconciliations

- A general bank reconciliation is performed monthly by the Accounts Payable Administrator and checked by the Financial Accountant. Any unresolved un-reconciled items arising during bank statement reconciliation which require amendment to the Council's records are signed off by the Finance Manager.
- A monthly reconciliation of the investment spreadsheet to the general ledger is carried out by the Financial Assistant and reviewed by the Finance Manager.

7.6.5. 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;
- matching of third party confirmations and the immediate follow-up of anomalies;
- use of expert advice.

Agreements

- Financial instruments can only be entered into with banks that have in place an executed ISDA Master Agreement with Council.
- Council's internal/appointed legal counsel must sign off on all documentation.

Financial covenants and other obligations

- 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.

7.6.6. Reports

The following reports are produced to monitor cash management and investment activity.

Report Name	Frequency	Prepared by	Recipient
Daily money management report Limits report	Reported daily on an exceptions basis	Finance	Management Accountant Finance Manager
Quarterly treasury report	Per Council meeting schedules	Finance	Council Chief Executive
Treasury strategy paper	6-monthly	Corporate Services Group Manager	Council Chief Executive
Cash flow report	Annually with the annual plan	Financial Accountant	Council Finance Manager

7.7. Risk Assessment and Management (Section 105(e) of the Act)

Credit risk is minimised by placing maximum limits for each broad class of issuer, and by limiting investments to government, LGFA, and NZ registered banks within prescribed limits (see Section 7.4 of this Policy).

Risks are controlled by first setting an overall investment strategy taking into account counterparty and cash flow requirements.

The use of interest rate risk management instruments is approved by the Council for borrowing related activities only. A current list of approved interest rate risk management instruments with appropriate definitions are included in Section 8 of this policy.

All investment activity is reported against policy parameters as outlined in Section 7.6.3.

Government stock/bond is registered securities issued by the Debt Management Office (DMO) on behalf of the Government. They are available for terms ranging from one year to twelve-year maturities. Government stock/bond has fixed coupon payments payable by the DMO every six months. They are priced on a semi-annual yield basis and are issued at a discount or premium to face value. They are readily negotiable in the secondary market.

8. Definitions

8.1. Approved Financial Investment Instruments

Investment instruments available in the market (excluding equities and property) can generally be discussed under four broad categories relating to the issuer of these instruments.

8.1.1. New Zealand Government

Treasury bills are registered securities issued by the DMO on behalf of the Government. They are usually available for terms up to a year but generally preferred by investors for 90 day or 180 day terms. They are discounted instruments, and are available in the secondary market, although most banks hold them for liquidity management purposes.

8.1.2. New Zealand LGFA

The LGFA issues, commercial paper (CP), also known as Promissory Notes, is issued by borrowers who usually have a credit rating and standing in the market that is sufficient to enable the CP to be issued without endorsement or acceptance by a bank. In this instance the LGFA being highly credit rated. Commercial paper is issued with maturities ranging from 7 days to over one year. The common maturities are for 30 and 90 days. Council is restricted to investing in CP with maturities of no more than 181 days. CP is generally preferred over term deposits because investors can sell them prior to maturity without suffering the penalty interest costs common to term deposits.

The LGFA issues bonds that are similar in structure to New Zealand Government stock/bonds.

Borrower Notes
On occasion when Council borrows from the LGFA it will be required to contribute part of that borrowing back as equity in the form of “Borrower Notes”. A Borrower Note is a written, unconditional declaration by a borrower (in this instance the LGFA) to pay a sum of money to a specific party (in this instance the Council) at a future date (in this instance upon the maturity of the loan). A return is paid on the Borrower Notes.

8.1.3. Registered banks

Call and term deposits are funds accepted by the bank on an overnight basis (on call) or for a fixed term. Interest is usually calculated on a simple interest basis. Term deposits are for a fixed term and are expected to be held to maturity. Term deposits are not negotiable instruments. Termination prior to maturity date can involve penalty interest costs.

Registered certificates of deposits (RCD) are securities issued by banks for their funding needs or to meet investor demand. They are registered or held on behalf of by the dealing bank. Details include, the name of the investor, face value and maturity date. They are able to be transferred by registered transfer only. RCDs are priced on a yield rate basis and issued at a discount to face value or a grossed up basis. They are generally preferred over term deposits because investors can sell them prior to maturity.

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8.2. Risk management instruments and terms (From an investor's perspective)

8.2.1. BKBM

The bank bill mid-market settlement rate as determined at 10:45am each business day on Reuters page BKBM. This is the standard rate for the settlement of interest rate swaps, forward rate agreements and interest rate caps and collars.

8.2.2. Forward exchange contract

A contract to buy and sell one currency against another at a fixed price for delivery at some specified future date.

Forward points
The difference in interest rates between two currencies expressed as the exchange rate points i.e. 300 forward points is a 0.0300 adjustment to the 0.7500 NZ$/US$ exchange spot rate.

8.2.3. Forward rate agreement

An agreement between the Council and a counterparty (usually a bank) protecting the Council against a future adverse interest rate movement for a specified period of time (up to a year). The Council and the counterparty agree to a notional future principal amount, the future interest rate, the benchmark dates and the benchmark rate (usually BKBM). This definition includes the bond forward rate agreement where the benchmark rate is the underlying government bond yield.

Interest rate options
The purchase of an interest rate option gives the holder (in return for the payment of a premium) the right but not the obligation to borrow (described as a cap) or invest (described as a floor) at a specified interest rate for a specified period. The Council and the counterparty agree to a notional future principal amount, the specified interest rate, the rate-setting dates and the benchmark rate (usually BKBM). Interest rate option products include caps, floors and bond options.

Interest rate or currency collar strategy
The combined purchase (or sale) of a cap or floor with the sale (or purchase) of another floor or cap.

Interest rate swap
An interest rate swap is an agreement between the Council and a counterparty (usually a bank) whereby the Council pays (or receives if an investor) a fixed interest rate and receives (or pays) a floating interest rate. The parties to the contract agree notional principal, start

date of the contract, term of the contract greater than one year), fixed interest rate and the benchmark rates (usually BKBM).

The swap can have a forward start date directly matching the contract to the underlying investment cash flow.

8.2.4. Liquidity

Liquidity refers to negotiable instruments that have an underlying market where buyers and sellers are available to transact and readily convert the investment into cash.

8.2.5. Negotiable

These instruments can be bought and sold prior to their legal maturity date.

8.2.6. Spot rate

The current market rate for currencies, interest rates for immediate delivery/settlement - normally two business days after the transaction is agreed.

Appendix 1 - Delegations

Activity	Responsibility	Limits
Approve and amend policy document	Council	NA
Open/close bank accounts	Corporate Services Group Manager	Unlimited to be reported to Council
Approving transactions outside policy	Council	Unlimited
Approving allowable risk management instruments	Council	Unlimited subject to legislative limitations
Approve authorised cheque/electronic signatory positions	Chief Executive	Unlimited
Overall day to day investment management	Chief Executive (delegated by Council) Corporate Services Group Manager (delegated by Chief Executive) Finance Manager	Subject to policy
Cash and liquidity management	Chief Executive (delegated by Council) Corporate Services Group Manager (delegated by Chief Executive) Finance Manager	Subject to policy
Approving allowable risk management instruments for investment activity	Council	Unlimited subject to legislative limitations
Maximum daily transaction amount (approved investment cash management, daily fund management)	Chief Executive Corporate Services Group Manager Finance Manager Financial Accountant Management Accountant	Unlimited $15 million $10 million $1 million $1 million
Triennial review of policy	Corporate Services Group Manager	NA
Ensuring compliance with policy	Corporate Services Group Manager	N/A