

SOUTH WAIRARAPA DISTRICT COUNCIL

15 MAY 2019

AGENDA ITEM C4

JOINING THE LOCAL GOVERNMENT FUNDING AGENCY (LGFA) AS A GAURANTOR

Purpose of Report

To inform councillors of the legal requirements in regard to becoming a Local Government Funding Agency (LGFA) guarantor.

Recommendations

Officers recommend that the Council:

1. *Receive the information.*
2. *Notes the contents of the report*
3. *Confirms Council's intention to join LGFA as a guarantor (noting it has already acceded as a borrower in 2016) as per Council's 3 April 2019 resolution (DC2019/47).*
4. *Delegates authority to the Acting Chief Executive to execute the following documents for the purposes of recommendation 3. above:*
 - a. *Security Stock Certificate (in relation to the Equity Commitment Deed);*
 - b. *Security Stock Certificate (in relation to the Guarantee);*
 - c. *Stock Issuance Certificate;*
 - d. *Section 118 Chief Executive Certificate; and*
 - e. *Officer's Certificate.*
5. *Authorises any two of the Council's elected members to execute the following deeds for the purposes of recommendation 3. above:*
 - a. *Accession Deed to Equity Commitment Deed; and*
 - b. *Accession Deed to Guarantee and Indemnity.*
6. *Delegates authority to the Acting Chief Executive to execute such other documents and take such other steps on behalf of Council as the Chief Executive considers it is necessary or desirable to execute or take to give effect to recommendation 3. above.*
7. *Approves the amendments to the Investment Policy as shown in Appendix 1.*
8. *Approves the amendments to the Liability Management Policy as shown in Appendix 1.*

1. Executive Summary

The Council joined the New Zealand Local Government Funding Agency (LGFA) borrowing scheme as a borrower in 2016. In order to increase the amount it may borrow through LGFA, Council now wishes to accede to the LGFA programme as a guarantor and thereby guarantee the indebtedness of LGFA. Any council that borrows in aggregate NZ\$20 million or more from LGFA must be a guarantor.

2. Discussion

In order to accede as a guarantor, Council must execute the following legal documents:

- *Accession Deed to Equity Commitment Deed;*
- *Accession Deed to Guarantee and Indemnity;*
- *Security Stock Certificate (in relation to the Equity Commitment Deed);*
- *Security Stock Certificate (in relation to the Guarantee);*
- *Stock Issuance Certificate;*
- *Section 118 Chief Executive Certificate; and*
- *Officer's Certificate.*

2.1 Documents in the form of deeds should be executed by two elected members.

2.2 The documents and certificates at 2.1, 2.2, 2.6 and 2.7 will be reviewed and approved by Council's solicitors at Simpson Grierson prior to their execution. The certificates at 2.3, 2.4 and 2.5 have been prepared by Simpson Grierson. Simpson Grierson has extensive LGFA experience, both with Council and with other local authorities.

2.3 It is appropriate to have clear authority for the execution of the documents and certificates. It is proposed that authority be specifically delegated to two elected members to sign deeds and to the Acting Chief Executive to sign all other necessary documentation and certificates.

3. Council Policy Amendments

Council's Investment Policy and Liability Management Policy have been amended to allow Council to become a guarantor with LGFA.

4. Conclusion

Council officers recommend that all legal documents required are executed, that Simpson Grierson act on behalf of SWDC in this matter, and that the Acting Chief Executive be given authority to sign all necessary documentation.

The draft legal documents will be available electronically and on Council's website [Council Agenda and Minutes 2019 | South Wairarapa District Council](#) and available in hard copy on request.

5. Appendices

Appendix 1 – Investment Policy and Liability Management Policy

Contact Officer: Katrina Neems, Finance Manager

Reviewed By: Jennie Mitchell, Acting Chief Executive

Appendix 1 – Investment Policy and Liability Management Policy

INVESTMENT POLICY

1. General Policy

The investment policy will be consistent with Council's overall objectives and plans. Council acknowledges that there are financial risks associated with its investment activities but is risk averse. The treasury function is based on managing risk and protecting investments. There is no involvement in speculative transactions.

The management of trusts, special funds and reserves will be reviewed on a regular basis. This will ensure that their holding complies with any statutory or other special requirements and that their use is consistent with these requirements and with Council policy at the time.

Investments generally will be made having regard to the following objectives:

- To manage short term cash flows in an efficient and prudent manner providing cash for approved expenditure needs and in the event of urgent requirements.
- To provide cash for the future retirement of debt on maturity.
- To maximise interest income and minimise risk to the capital invested.

2. Treasury Investments

Council's treasury investments comprise sums reserved for special purposes and funds held for working capital requirements. These funds are managed using the following guidelines:

- Funds are invested only with institutions which offer an excellent degree of security. These include the New Zealand Government, State Owned Enterprises, Local Authorities (including itself) and New Zealand registered banks.
- The maximum amount to be invested with any one approved institution is 30% of Council's total investments except for the Wairarapa Building Society which shall be 10%.
- Occasional and short term exceedances of the 30% rule are allowed, such exceedances are to be reported to the Audit and Risk Working Party.

3. Equity Investments

Council has small shareholdings in the following organisations:

- Civic Financial Services Limited
- AIRTEL Limited
- Farmlands Trading Society Limited

A Council resolution is required to dispose of these shares.

Council is risk averse and does not wish to expose itself to the risks associated with equity investments. It will not as a general rule seek to acquire further equity investments.

4. Emissions trading scheme

Council has a number of "New Zealand Emissions Units" that were issued as a result of the introduction of the emissions trading scheme.

A Council resolution is required to transact these units.

5. Local Government Funding Agency

Council may borrow funds from the [New Zealand Local Government Funding Agency \(LGFA\)](#) and also may provide guarantees in respect of the indebtedness of LGFA.

Council holds Borrower Notes with the LGFA. Borrower notes are subordinated debt instruments which are required to be held by each local authority that borrows from LGFA in an amount equal to 1.6% of the aggregate borrowings by that local authority.

Under certain very limited circumstances, the borrower notes can convert to shares. Council may also be required to subscribe for shares or other financial instruments in respect of LGFA, in connection with its LGFA borrowing and guarantees.

If this were to occur, a Council resolution will be required to manage these shares.

The Council may therefore be required to invest in LGFA shares and other instruments in circumstances in which the return on its investment is potentially lower than the return it could achieve with alternative investments.

6. Property

Council holds a limited amount of real property for investment purposes. It may and does purchase property from time to time to assist in the provision of its core services to the community. Surplus properties will be disposed of wherever possible. Council will review its property holdings on a regular basis.

6.1 Mix of Investments

The mix of investments will be determined having regard to the overall funding needs of Council. Investment mix is also influenced by risk management considerations. Council will maintain sufficient general funds for day to day operational needs.

Council may establish, alter or dissolve a fund for a particular purpose by ordinary resolution.

6.2 Acquisition of New Investments

Treasury investments are acquired under delegated authority to the Chief Executive.¹

It is unlikely that Council will invest in shares in the foreseeable future. Any such acquisitions would require a resolution by Council.

When acquiring treasury investments Council seeks to:

- Optimise return on investments.
- Ensure investments are secure.

1 The Chief Executive and/or other officers to whom the Chief Executive may delegate from time to time.

- Manage potential interest rate movement losses.

6.3 Disposition of Revenue from Investments

All dividends, interest and other income from investments will be available for Council's general use except where Council has resolved that interest earned on funds invested in an account shall be reinvested in that account. These accounts shall be subject to review each year.

6.4 Disposition of Proceeds of Sale of Investments

Equity and property investments may be disposed of by resolution of Council. In general terms, these proceeds will not be available for operational purposes unless Council resolves otherwise. These proceeds will normally be used for capital investments or the retirement of debt.

On maturity, treasury investments may be realised for Council's general use or reinvested under delegated authority by the Chief Executive.

6.5 Procedures

Equity and property investments will be reviewed by Council each year.

Treasury investments will be managed under delegated authority by the Chief Executive. All realisations, transfers and reinvestments will comply with this policy. The Audit and Risk working party will receive a schedule of all treasury investments for each month. A schedule of investments will be provided to Council on a regular basis as part of the financial statements included in the Chief Executive Officer's report.

6.6 Investment Risk Assessment and Management

Council has no investment properties and only one equity investment. [Council does hold shares in Airtel Ltd and Farmlands Trading Society Limited, however these are not held for investment purposes]. The exposure to risk in these areas is minimal.

Council's primary objective in respect of treasury investments is the protection of those investments. Only credit worthy counter parties are acceptable. Council will manage its exposure to credit risk by maintaining a diverse investment portfolio with prescribed limits for each counter party. The exposure to interest rate risk will be managed by a mix of terms and staggered maturity dates to mitigate the effect of market fluctuations.

6.7 Objectives for holding and managing financial investments and equity securities

The objectives of holding financial investments are:

- To maintain sufficient cashflow to meet current and future needs.
- To ensure sufficient funding is available to meet future loan repayments as they fall due.

The objectives of holding equity investments are:

- Equity investments are held solely for strategic purposes and are not held for financial return.

- Equity investments will only be made to support companies that provide a service that may not otherwise be provided, for the benefit of either the three Wairarapa local authorities, or a wider base of local authorities.

6.8 Targets for returns on financial investments and equity investments

The targets for returns on financial investments are:

- The key rationale of the holdings of financial investments is risk minimisation. Due to the levels of cash holdings these are managed solely for cashflow purposes. Council policy limits investment to very low risk investment, which by its nature provides modest returns.

The objectives of holding equity investments are:

- Equity investments are held solely for strategic purposes and are not held for financial return.
- There is no quantified target for equity investments for the reasons outlined above.

LIABILITY MANAGEMENT POLICY

1. General policy

The borrowing management policy will be consistent with Council's overall objectives and plans. The amount of borrowing is driven on a project by project basis. Council approves borrowing by resolution as part of the Annual and Long Term Planning processes.

Council may borrow from itself, any registered bank or wholesale investor by the issue of local authority stock, or the Local Government Funding Agency ([LGFA](#)) or in any other manner which it considers appropriate.

2. [Local Government Funding Agency](#)

[Despite anything in this policy, the Council may borrow from the New Zealand Local Government Funding Agency \(LGFA\) and, in connection with that borrowing, may enter into the following related transactions to the extent it considers necessary or desirable:](#)

[\(a\) making equity \(whether called or uncalled capital\) or subordinated debt contributions to the LGFA;](#)

[\(b\) providing guarantees in respect of the indebtedness of the LGFA.](#)

2.3. [Interest rate exposure](#)

Council's borrowing gives rise to direct exposure to interest rate movements. Given the long term nature of Council's assets, projects and intergenerational factors, Council's policy is to have a high percentage of fixed rate borrowing, however in certain circumstances it may be prudent to consider a more even balance between floating and fixed rate instruments. Interest rate risk is managed by adjusting the maturity of borrowings to avoid a concentration of debt reissues or rollovers in line with interest rate predictions.

All matters concerning borrowing which can be lawfully delegated are delegated to the Chief Executive.

The use of hedging instruments for risk management on Council's borrowing is not appropriate. Should Council wish to use hedging instruments an ordinary resolution approving their use will be adopted by Council.

3.4. [Liquidity](#)

Liquidity refers to the availability of cash resources to meet all obligations as they arise.

Short term liquidity management is monitored and controlled through daily cash management activities with long term liquidity being monitored and controlled through the Annual Plan and Long Term Financial Strategy processes.

Council ensures debt maturity is spread widely to minimise the risk of large concentrations of debt maturing at any one time. Council may maintain an overdraft facility to meet short term cash requirements as and when necessary.

4.5. [Credit exposure](#)

Council is readily able to attract cost effective borrowing because of the strength of security offered by its powers to rate, and the very low historical incidence of default by local authorities.

5.6. Debt repayment

Council has traditionally entered into two types of loans. These comprise reducing balance and interest only loans. Reducing balance (table mortgage) loans are repaid from operational funds over the life of the loan. Council can liquidate these loans at any point of time if allowed under the terms of the loan agreement. Interest only loans are taken out over the life of the project and refinanced at three to five year intervals.

Council has not forecast to make any repayments of principal on interest only loans, as the loans are intended to be for the same length of time as the asset life. Most of the loans are for assets that have a life of between 7 years and 35 years and as a result some of these mature within the period of the current Long Term Plan (LTP).

Council's goal is to spread the principal and interest costs related to asset purchases evenly over the period of the assets life, and therefore achieve inter-generational equity for ratepayers. While the loan principal is not paid off progressively, Council sets aside deposits to accumulate progressively to prepare for repayment of the loans.

Council has introduced a policy of building up its cash reserves in order to meet future renewals of its assets and repayment of its interest only loans.

Terms of repayment should be determined after consideration of the cost of finance and any intergenerational benefits of the assets being financed.

The maximum period over which borrowings are to be repaid is the lesser of 35 years or the life of the project, unless otherwise resolved by Council.

6.7. Specific borrowing limits

The gross interest expense of all borrowings will not exceed 12% of rates income.

7.8. Security

[Council borrowings with the LGFA will be secured by the issue of security stock under the Council's Debenture Trust Deed \(conferring the benefit of the charge over Council's rates and rates revenue on the LGFA\).](#)

[Council has granted security over its rates and rates revenue under the Council's Debenture Trust Deed. Council does not offer other assets as security for borrowings.](#)
~~Council does not offer assets as security for borrowings.~~