SOUTH WAIRARAPA DISTRICT COUNCIL
Kia Reretahi Tātau

Treasury & Liability Management Policy

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Treasury & Liability Management Policy

1. Introduction

- The South Wairarapa District Council's (Council) Treasury Management Policy (the Policy) comprises a Liability Management Policy and an Investment Policy, as required by the Local Government Act 2002 (the Act).

- Part 6, section 104 of the Act states that the Liability policy must state the local authority's policies in respect of the management of both borrowing and other liabilities, including interest rate exposure, liquidity, credit exposure and debt repayment.

- Part 6, section 105 of the Act states that the investment policy must state the local authority's policies in respect of investments, including the mix of investments, the acquisition of new investments, procedures for managing and reporting investments and assessment and management of risks.

2. Purpose

- The Policy provides the framework for all of the Council's treasury management activities and defines key responsibilities and the operating parameters within which treasury activity is to be carried out.

3. General Policy Objectives

- This document identifies the policies of the Council with respect to investment and liability management activities. The Policy has not been prepared to cover other aspects of the Council's operations, particularly transactional banking management, systems of internal control and financial management. Other policies and procedures cover these matters.

- The objective of the Policy is to control and manage borrowing costs, investment returns, liquidity requirements and risks associated with treasury management activity.

- The Policy notes that the Council is governed by the following relevant legislation:
    - Local Government Act 2002, in particular Part 6 including sections 101,102, 104 and 105;
    - Local Government (Financial Reporting and Prudence) Regulations 2014, in particular Schedule 4; and
    - Trustee Act 1956.

- The Policy also notes that the Council is a risk averse entity and wishes to minimise risk from its treasury management activities. Interest rate risk, liquidity risk, funding risk and credit risk are risks that the Council seeks to manage, not capitalise on. Accordingly, any activity that may be construed as speculative in nature is expressly forbidden.

4. Governance

- The elected Council has ultimate responsibility for ensuring that there is an effective policy for the management of its treasury risks. In this respect the Council decides the level and nature of risks that are acceptable. The full Council is responsible for approving this Treasury Management Policy and any changes to it that may be required from time to time, but in any case, must arrange for and approve the three yearly review.

- Changes to the Policy will be recommended by the CEO after a review is completed by the General Manager Corporate Services. The authority to change the Policy rests with the Council or an appropriate committee if the Council has made such a delegation.

- A list of delegated authorities as they relate to this Policy is attached as Appendix 2.

5. 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. This risk is minimised by having standing dealing and settlement instructions being sent to counterparties, matching of third-party confirmations and the immediate follow-up of any anomalies.

6. Operational Risk

- This is the risk of loss as a result of human error (or fraud), system failures and inadequate procedures and controls. Operational risk, particularly relevant to dealing with financial instruments, is minimised through appropriate segregation of duties, recording and reporting procedures and system controls.

- Treasury risk is minimised for the treasury activities by ensuring that there is adequate segregation of duties among the core functions of deal execution, confirmation, settling and accounting / reporting.

7. Foreign Exchange Risk

- The Council has limited foreign exchange risk through the occasional purchase of foreign exchange denominated plant and equipment. All foreign exchange exposures greater than NZD50,000 must be hedged using forward exchange contracts. The Council does not borrow or enter into incidental arrangements within or outside New Zealand in any foreign currency, other than New Zealand dollars.

8. Reporting

» The table below summarises the key reporting outputs in relation to treasury management:

Report Type	Audience	Frequency	Format
Management	Strategic Leadership Team	Monthly	Report compliance with all limits and thresholds
Governance	Assurance, Risk and Finance Subcommittee	Quarterly	Overview of quarterly performance
Annual Report	Council	Annually	Review of Annual performance

9. Liability Management Policy

9.1. Objectives

» The Council's liability management objectives in relation to borrowings are to:

- minimise borrowing costs within approved risk parameters;
- prudently manage the Council's exposure to interest rate changes;
- ensure sufficient levels of liquidity are available to meet planned and unforeseen cash requirements;
- ensure that funding risks are managed by maintaining an appropriate spread of maturities;
- prudently manage the Council's credit exposures;

» The Council's liabilities comprise borrowings and various other liabilities. The Council raises borrowings for the following primary purposes:

- General debt to fund the Council's balance sheet, including working capital requirements;
- Specific debt associated with 'one-off' projects and capital expenditure;
- To fund assets where their useful lives extend over several generations of ratepayers;

» Any new borrowings or roll-over of existing borrowing needs to be budgeted for as part of the Council's current approved Long Term or Annual Plans or have specific Council approval.

9.2. Specific borrowing limits

- In managing debt, the Council will adhere to the following limits:

Item	Borrowing Limit
Net Debt/Total Revenue	< 175%
Net Interest/Total Revenue	< 20%
Net Interest/Annual Rates Income	< 30%
Liquidity	> 110%

(See definitions of above items in Appendix 1)

10. Security

- The Council's external borrowings and interest rate risk 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, the Council's borrowing is secured by a floating charge over all Council rates levied under the Local Government Rating Act. The security offered by the Council ranks all secured lenders equally on a pari passu basis.

11. Borrowing Mechanism

- The Council is able to borrow through a variety of market mechanisms including borrowing via the Local Government Funding Agency (LGFA), direct bank borrowing, or accessing the short and long-term debt capital markets directly or indirectly. In evaluating strategies for new borrowing, consideration should be given to the following:
  - available rates and terms from lenders;
  - the Council's overall debt maturity profile;
  - the outlook on future interest rate movements;

- The Council's ability to readily attract cost-effective borrowing is largely driven by its ability to rate, maintain a strong financial standing and manage its relationships with the LGFA and financial institutions.

12. Debt Repayment

- The Council repays borrowings from refinancing or surplus general funds. Borrowings may be refinanced by further borrowings as per the current Annual or Long-Term Plan.

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

13. The LGFA

» The Council may borrow from the New Zealand Local Government Funding Agency Limited (LGFA) in accordance with its shareholding agreement with them. In connection with that borrowing, the Council may enter into the following related transactions to the extent that it considers necessary or desirable:

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

14. Guarantees / Contingent Liabilities and Other Financial Arrangements

» The Council may provide financial guarantees to local organisations for recreational and community purposes. The Council is not allowed to guarantee loans to Council Controlled Trading Organisations under Section 62 of the Local Government Act.

» The total value of guarantees at any one time, excluding LGFA guarantees, will not exceed 3% of the total annual rates levied during that year. Total loan guarantees held are included in calculation of the Council’s maximum borrowing limit.

» The Council will ensure that sufficient funds or committed lines of credit exist to meet any amounts guaranteed.

15. Funding, Liquidity, and Interest Rate Risk Management

Borrowing exposes the Council to three principal risks:

Funding / Liquidity Risk

» Funding risk centres on the ability to re-finance or raise new debt at acceptable pricing and maturity terms.

» Liquidity risk is the risk that an unforeseen event or miscalculation in the required liquidity level may lead to council being unable to meet its day-to-day obligations. Liquidity risk management has the objective of ensuring that adequate liquid assets and funding sources are available at all times to meet both the short and long-term commitments of Council as and when they arise, in an orderly manner.

Interest Rate Risk

- Interest rate risk is the risk that the Council will be exposed to adverse changes in interest rates. For example, increased interest rates could see funding costs materially exceed adopted Annual Plan and Long-Term Plan interest cost projections. This would adversely impact cost control, capital investment decisions, returns and feasibility, if there was no hedging is in place.

- A key factor in the management of funding risk is to spread and control the risk to reduce the concentration of risk at any point so that the overall borrowing cost is not increased unnecessarily and / or the desired maturity profile compromised due to market conditions. Council's ability to readily attract cost effective borrowing is largely driven by its ability to maintain a strong balance sheet, levy rates and manage its relationships with the LGFA and the banking sector. Council also seeks to have a diversified maturity profile for external borrowing but, in any case, no more than $30.0 million or 50% of outstanding debt (whichever is the greater, can mature over the next 12-months or any subsequent 12-month period, on a rolling basis.

- To manage liquidity risk, the Council will ensure that external debt plus committed but unutilised loan facilities, and / or available liquid investments will be maintained at an amount of 110% of projected external debt over the ensuing 12-month period.

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17. Interest Rate Risk Control Limits

- The primary objective of interest rate risk management is to reduce uncertainty of interest rate expense but at the same time balance the need to have some flexibility to react to the impact on interest rate levels from ongoing economic and monetary policy cycles and one-off events, such as COVID.

- Interest rate risk is managed by fixing a portion of debt through an ongoing process of active management of underlying interest rate exposures.

- Interest rate expense can only be hedged by entering into fixed rate loans from the LGFA or a banking counterparty, unless otherwise approved by Council.

- Hedging of the Council's external debt / borrowings must be within the following fixed / floating interest rate risk control limits However, if total debt is less than $30.0 million the actual level of hedging required is at the discretion of the CEO.

Fixed/Floating Interest Rate Risk Control Limits		
	Minimum Fixed Rate	**Maximum Fixed Rate**
Years 1 and 2	50%	100%
Years 3, 4 and 5	30%	80%
Years 6 and 7	0%	60%

- The percentages are based on the projected external debt levels in the Council's current approved budget (Annual Plan or Long-Term Plan). However, the actual forecast debt level is subject to approval by the CEO, as being a fair and reasonable forecast. Any hedging beyond these limits needs the approval of the full Council.

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

18. Investment Policy

18.1. General Policy

- The investment policy will be consistent with the Council's overall objectives and plans. The management of trusts, special funds and reserves will be reviewed at least annually within the Annual Plan or Long-Term Plan process. 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.

- With the exception of financial investments, the acquisition of a new investment or disposal of an existing investment needs to be budgeted for as part of the Council's approved Long-Term Plan or Annual Plan or must be approved through a Council resolution.
- Equity and property investments will be reviewed annually by Council.
- The authority to acquire and dispose of financial investments is delegated to Chief Executive.

18.2. Equity Investments

- The Council currently maintains small equity investments in Civic Financial Services Limited, Farmlands Trading Society Limited, and Wellington Water Limited.
- In general, Council does not wish to expose itself to the risks associated with equity investments and is not seeking to acquire further equity exposures. In any case any new equity investments would need to be approved by Council resolution.

18.3. Property Investments

- 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 over whenever possible. Council will review its property holdings on a regular basis.

18.4. Local Government Funding Agency

- The Council borrows from the LGFA and holds borrower notes linked to these borrowings. 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 2.5% of the aggregate borrowings by that local authority. Under certain, very limited circumstances, the borrower notes can convert to shares. If this were to occur, a Council resolution will be required to manage these shares.

18.5. Emissions Trading Scheme

- Council has a number of 'New Zealand Units' (NZU) or carbon credits, that were issued as a result of the introduction of the emissions trading scheme. A council resolution is required to transact these units.

18.6. Treasury Investments

- Council's treasury investments comprise sums reserved for special purposes and funds held for working capital requirements. In general terms, Council wants to minimise cash holdings and whenever possible apply surplus funds to reduce debt levels.

- The Council's primary objective when investing is the protection of its investment capital. Accordingly, the Council may only invest in approved creditworthy counterparties. Counterparties must be a Bank registered by the Reserve Bank of New Zealand, with a long-term S&P Global Ratings (or equivalent Fitch or Moody's rating) credit rating of A+ and above.

- With the exception of cash investments that are sourced from the pre-funding of approved capital expenditure, surplus cash must, if possible, be applied to reducing debt and if this is not possible, any investments must be restricted to a term of no more than 6 months. Cash investments linked to the pre-funding of approved capital expenditure can be invested for up to a maximum of 18 months.

- Approved treasury investments are bank call and term deposits with a maximum term of 18 months. Total treasury investments with any one entity are restricted to $5.0 million or 50% of total treasury investments, whichever is the greater.

- Special Funds and Funding Reserves - liquid assets are not required to be held against special funds. Instead, the Council will internally utilise these funds.

19. Appendices

- Appendix 1: Covenant Definitions (Source: LGFA)
- Appendix 2: Delegated Authorities

Appendix 1: Covenant Definitions *(Source: LGFA)*

For covenant calculation and borrowing limit purposes:

- Total Revenue is defined as cash earnings from rates, grants and subsidies, user charges, interest, dividends, financial and other revenue and excludes non-government capital contributions (e.g. developer contributions and vested assets).
- Net Debt is defined as total debt less liquid financial assets and investments.
- Liquidity is defined as external debt plus committed loan facilities plus liquid investments divided by external debt.
- Net Interest is defined as the amount equal to all interest and financing costs less interest income for the relevant period.
- 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 received from other local authorities for services provided (and for which the other local authorities rate).
- Financial covenants are measured on Council only basis and not consolidated group basis, unless requested by a local authority and approved by the LGFA Board.

Appendix 2: Delegated Authorities

	Activity	Delegated Authority	*Limit
1	Approving and changing Treasury Management Policy	Council	Unlimited
2	New annual borrowing as set out in the Annual Plan/Long Term Plan	Council	Unlimited
3	Approval for charging assets as security over borrowing	Council	Subject to the requirements of Debenture Trust Deed
4	Acquisition and disposition of investments other than financial investments	Council	Unlimited
5	Approving transactions outside Treasury Management Policy	Council	Unlimited
6	Re-financing existing debt	Chief Executive	Subject to Policy
7	Negotiate bank facilities	Chief Executive (and/or) General Manager Corporate Services	Subject to Policy
8	Manage cash / liquidity requirements	Chief Executive (and/or) General Manager Corporate Services	Per risk control limits
9	Approving counterparty credit limits	Chief Executive	Within the prescribed limits set out in the Treasury Management Policy
10	Adjust interest rate risk profile	Chief Executive (and/or) General Manager Corporate Services	Fixed rate debt ratio as per risk control limits; Fixed rate maturity profile limit as per risk control limits
11	Managing funding and investment maturities in accordance with the Council's approved facilities	Chief Executive (and/or) General Manager Corporate Services	Per risk control limits
12	Maximum daily transaction amount (borrowing, investing and interest rate risk management)	Council Chief Executive General Manager Corporate Services	Unlimited $20 million $5 million
13	Authorising lists of signatories	Chief Executive	Unlimited

	Activity	Delegated Authority	*Limit
14	Opening/closing bank accounts	Chief Executive	Unlimited
15	At least triennial review of Treasury Management Policy	General Manager Corporate Services	N/A
16	Ensuring compliance with Treasury Management Policy	General Manager Corporate Services	N/A

**All activity limits in the above table are subject to the limits contained in the Council approved Annual Plan / Long Term Plan. The Council can approve changes to the limits.*