Chairperson and Committee Members
AUDIT AND RISK COMMITTEE

8 FEBRUARY 2018

Meeting Status: **Public**

Purpose of Report: For Information

QUARTERLY TREASURY MANAGEMENT COMPLIANCE

PURPOSE OF REPORT

1 This report provides confirmation to the Audit and Risk Committee of Council's compliance with its Treasury Management Policy (Policy) for the quarter ended 31 December 2017.

DELEGATION

2 The Audit and Risk Committee has delegated authority to consider this report under the following delegation in the Governance Structure, Section B.3.

Ensuring that Council has in place a current and comprehensive risk management framework and making recommendations to the Council on risk mitigation.

BACKGROUND

3 The Policy is required to be reviewed at least every three years. The last review was undertaken in September 2017 and a new Policy was adopted by the Council on 19 October 2017 (Report Corp-17-339 refers). The Policy sets out a framework for the Council to manage its borrowing and investment activities in accordance with Council objectives and incorporates legislative requirements.

4 The Policy maintains regular reporting obligations to management and Council's Operations and Finance Committee, but now also mandates quarterly compliance reporting to be provided to the Audit and Risk Committee (please refer to Appendix 1).

DISCUSSION

Treasury Performance

5 Since October 2015 the Council's treasury strategy has included a significant prefunding programme. The policy allows pre-funding of Council debt maturities up to 18 months in advance, including re-financing. Market conditions have been favourable for this approach, where the Council draws down debt early and is able to invest the funds for a positive net return.

6 A key objective in commencing this approach was to prepare for managing a concentration of liquidity risk. The Council had $60 million of debt maturing in December 2017 with another $20 million in May 2018. If the Council were to wait until that maturity date before refinancing, assuming full refinancing is possible, the Council is exposed to the risk that market conditions are unfavourable at that time, and is forced to refinance a significant portion of its debt portfolio at high interest rates.

7 Assessment of the Council's Treasury performance is in the context of this strategy, and considers four reporting benchmarks/measures, which are covered in the following sections.

Cash/Debt Position

8 Table 1 below shows the Council's net debt position as at 31 December 2017 against full year budget and the prior year closing balance.

Table 1	December YTD Actual $000's	Full Year Budget $000's	Full year Variance $000's	Full Year 2015/16
External debt	195,000	186,548	(8,452)	210,000
less borrower notes	(3,120)	(2,960)	160	(3,360)
less cash investments	(42,644)	(15,200)	27,444	(60,455)
Net debt	**149,236**	**168,388**	**19,153**	**146,185**

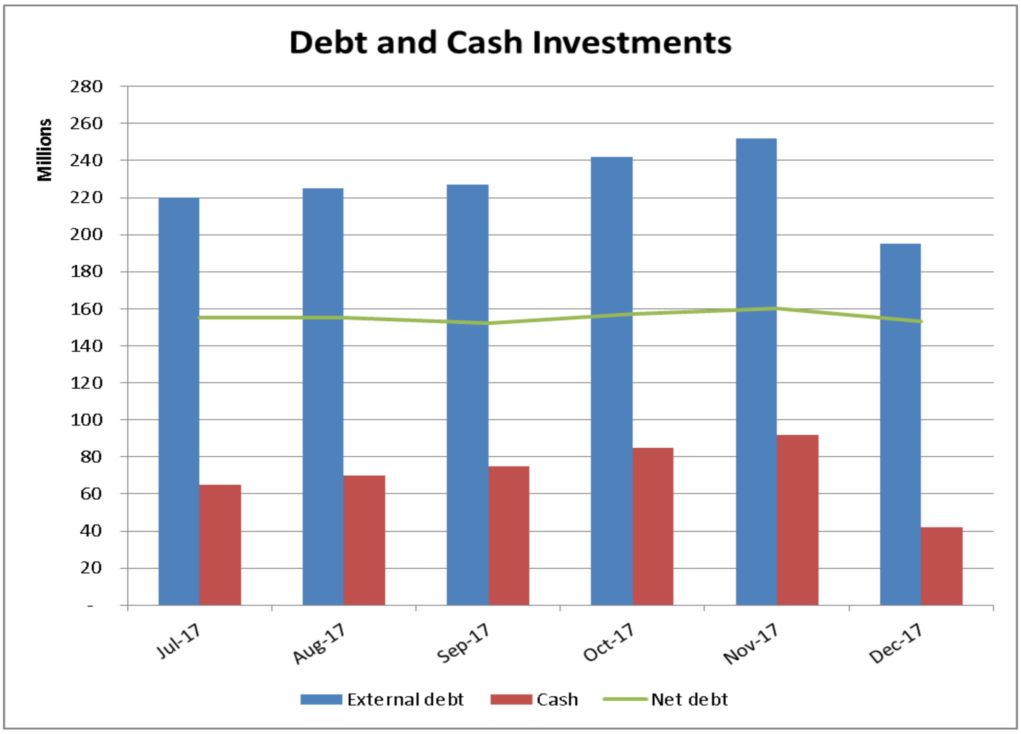
9 Council's maximum gross borrowings limit cannot exceed $200 million (excluding any existing debt prefunding). In mid-December 2017, $60 million of borrowings matured, making it the single, most significant debt roll-over in the history of the Council. $50 million of the maturity was prefunded and placed on term deposits, with the remaining $10 million refinanced on the day.

10 Council Officers worked very closely with the Council's three banking institutions, the Local Government Funding Agency (LGFA) and Computershare (Council's Registrar), to ensure that $50 million of Council's term deposits were repaid to the Council on time and that $10 million of new debt was issued to the Council to ensure Council successfully discharged its contractual obligation to repay $60 million of debt to the LGFA. On the same day in excess of $120 million was processed through the Council's bank account without any issues and the daily banking transaction limits were re-instated to $20 million the following day.

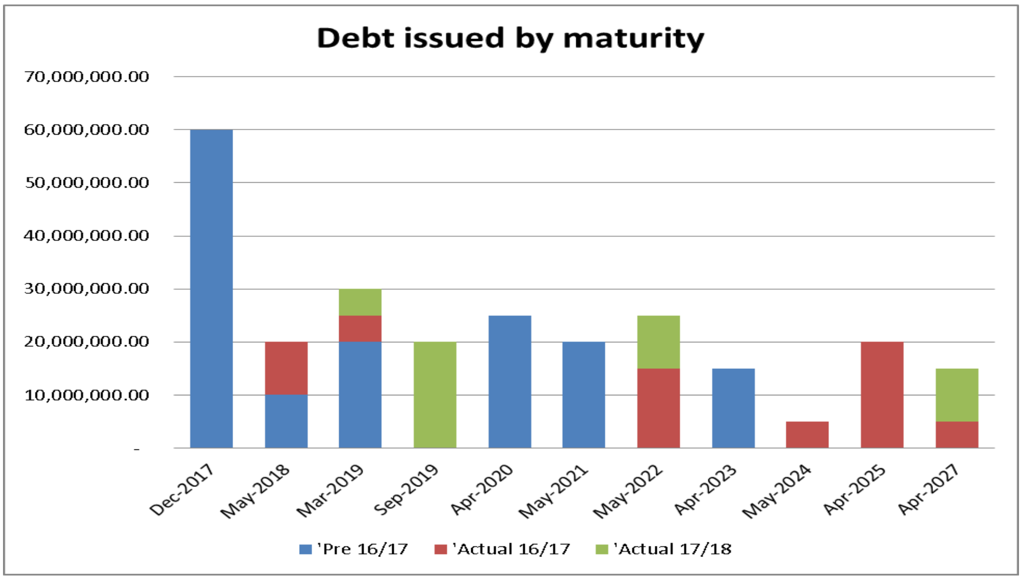
11 Beyond this transaction, the Council had $42 million invested on term deposits as at 31 December 2017. This is broken down as follows:

	$ Amount	$ Prefunding
LGFA debt maturing in May 2018	$20 million	$20 million
LGFA debt maturing in March 2019	$30 million	$10 million
2018/19 Capital Works Programme to 30 June 2018	$27.1 million	$12 million
Total	**$57.1 million**	**$42 million**

12 Excluding prefunding, the Council has not breached its upper borrowing limit as demonstrated in the chart below:



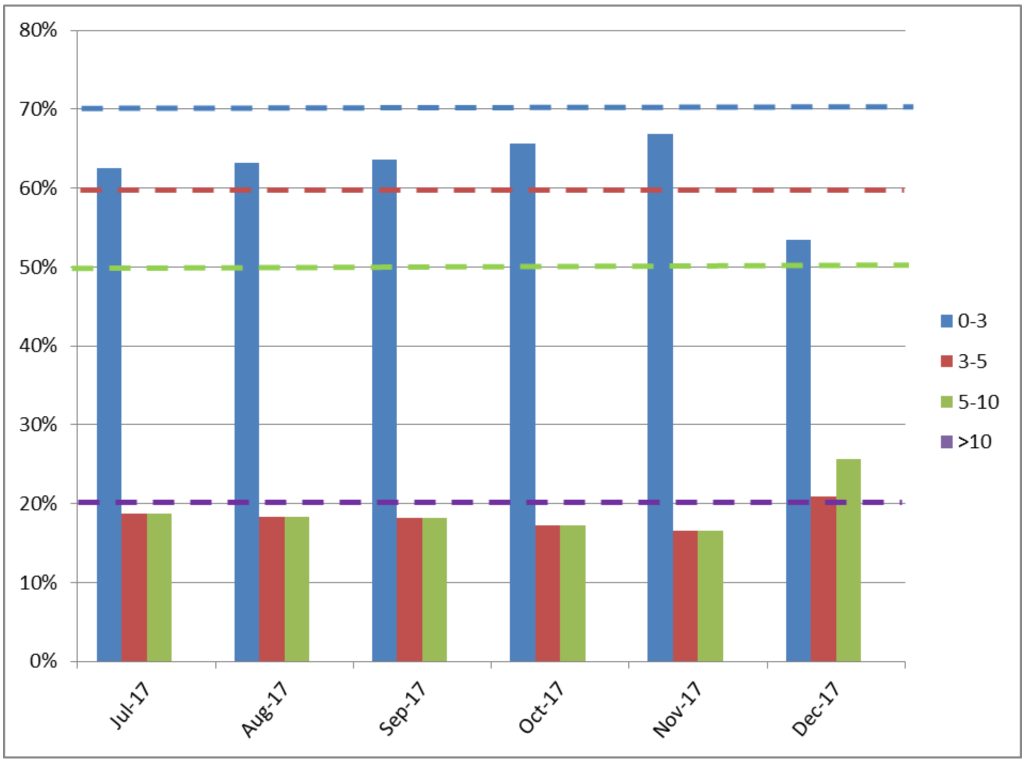
13 The graph below presents Council's debt maturity dates in relation to the financial year in which the debt was issued in.



14 Debt maturities must fall within compliance buckets. The buckets are:

Period	Minimum	Maximum
0 to 3 years	10%	70%
3 to 5 years	10%	60%
5 to 10 years	10%	50%
10 years plus	0%	20%

15 For the quarter ending 31 December 2017, the Council has been fully compliant with its debt maturity limits, as shown by the chart below. The upper limits, as shown by dashed lines, relate to the bars of the same colour. For example, the 0-3 year upper limit of 70% is in blue. Actual maturities in the 0-3 year bucket are represented by the blue bars.



16 The high proportion in the 0-3 years bucket reflects the $80 million of debt maturing in 2017/18, with $60 million that matured in December 2017.

Risk Exposure Position

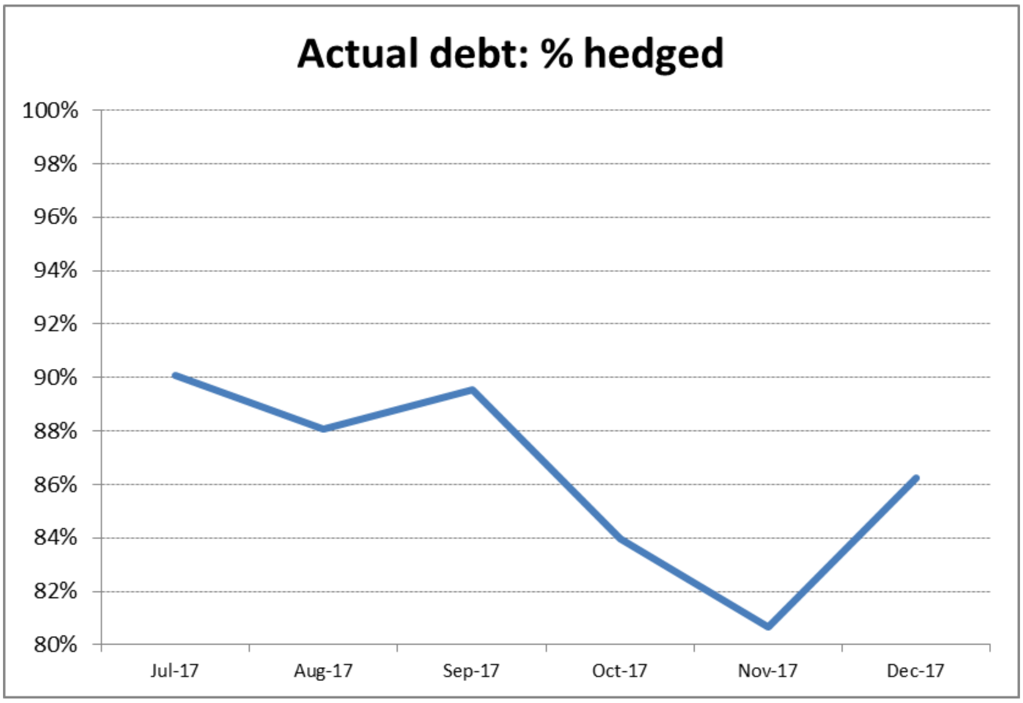
17 Council issues all debt on a floating rate basis, as lower interest rates are realised this way, and uses fixed interest rate swaps to minimise exposure at any one time to interest rate fluctuations.

18 Without such hedging, the Council would have difficulty absorbing adverse interest rate movements. A 1% increase in interest rates on $150 million in net debt would equate to additional interest expense of $1.50 million per annum. Conversely, fixing interest rates does however reduce Council’s ability to benefit from falling and/or more favourable interest rate movements.

19 The objectives of any treasury strategy are therefore to smooth out the effects of interest rate movements, while being aware of the direction of the market, and to be able to respond accordingly.

20 The Policy ensures that, at any point in time, the total notional amount of all interest rate risk management instruments (i.e. interest rate swaps) must not exceed Council’s total actual debt.

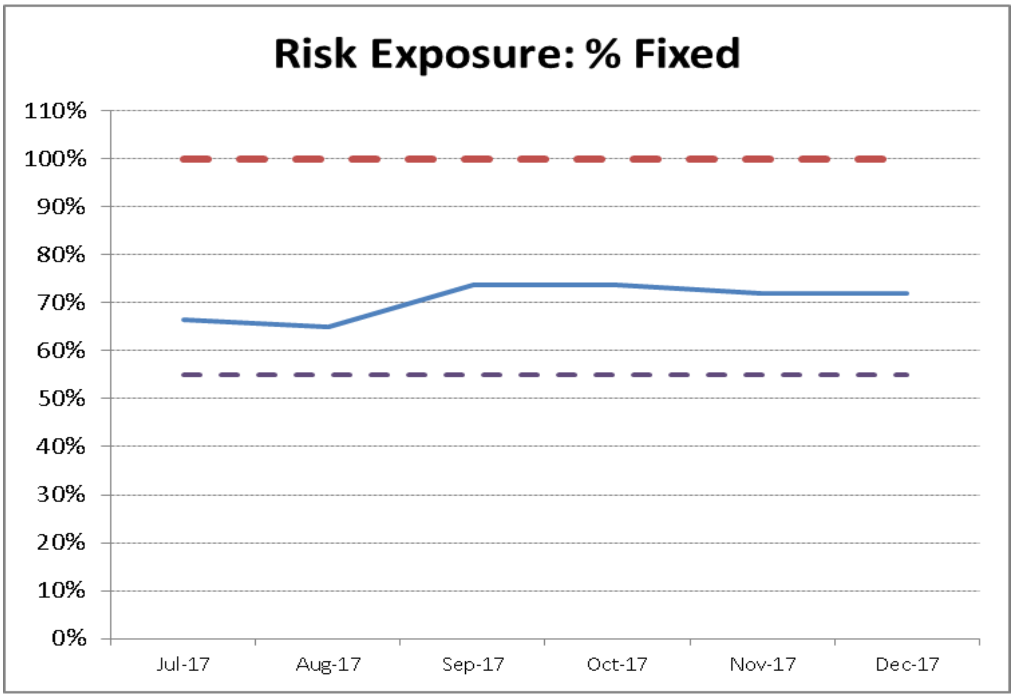
21 The following graph shows that the Council's hedging for the quarter ended 31 December 2017 was fully compliant with the Policy.



22 Hedging of Council's debt must be within the following fixed/floating risk control limits:

	Minimum	Maximum
Council's fixed/floating risk control limits	55% Fixed	100% Fixed

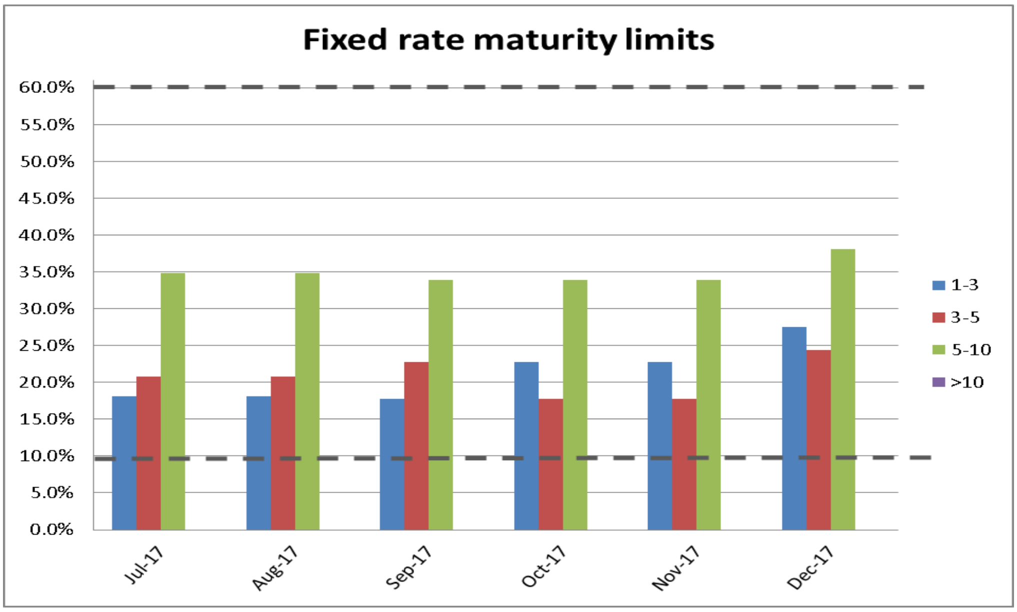
23 The following graph shows that the Council's hedging for the quarter ended 31 December 2017 was fully compliant with these limits.



24 Similarly to debt maturities, hedging instrument maturities must also fall within compliance buckets. These compliance buckets are as follows:

Period	Minimum	Maximum
1 to 3 years	10%	60%
3 to 5 years	10%	60%
5 to 10 years	10%	60%
10 years plus	0%	20%

25 The Council has been fully compliant, as shown by the following chart. Note that maturities falling within 1 year are not included. There is a significant amount of hedging in place for the $80 million of debt that is maturing within the 2017/18 financial year.



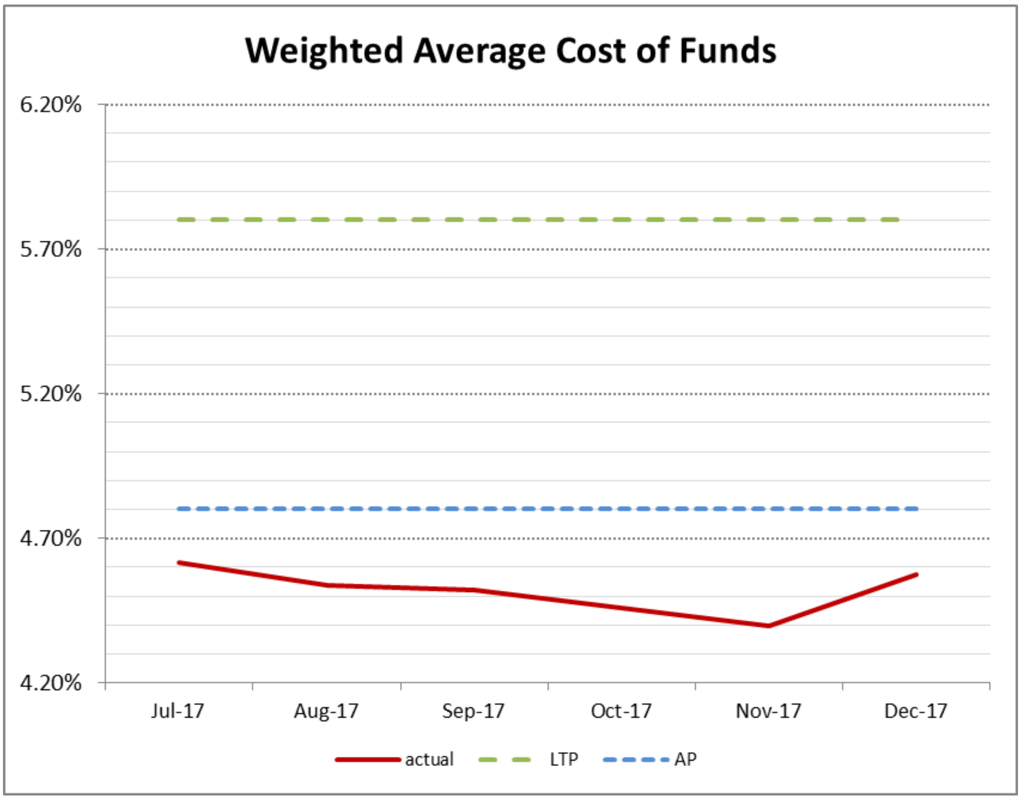
Risk Management Performance

26 The following table shows the Council's interest income and expense for the quarter, along with the weighted average cost of borrowing (WACB).

Table 2	December YTD actuals	YTD Budget	YTD Variance
	$000	$000	$000
External Interest Expense	5,111	5,060	(51)
less: Interest Income	(1,304)	(1,030)	274
Net Interest Cost	3,807	4,030	223
Weighted Average Cost of Borrowings	4.52%	4.80%	0.28%

27 To provide some context regards Council's treasury management effectiveness, the net interest costs year to date are $223,000 less than budget.

28 The following graph shows the cost of borrowing each month. The uplift in the WACB in December 2017 is primarily due to less interest income being realised post 15 December 2017 as Council's total term deposits were reduced by $50 million on the same date.



Counterparty Credit Risk

29 The policy sets limits for the maximum that can be traded per counterparty. The purpose of this is to ensure the Council does not concentrate its investments with a single party.

30 The policy sets the gross counter party limits as follow:

Counterparty/ Issuer	Minimum Standard and Poor's long term	Investments maximum per counterparty	Risk management instruments maximum per counterparty	Borrowing maximum per counterparty
NZ Government	N/A	Unlimited	None	Unlimited
LGFA	AA- / A-1	$20m	None	Unlimited
NZ Registered Bank	A+ / A-1	60% of total investments or $25m; whichever is greater.	50% of total instruments or $80m; whichever is greater.	$50m

31 The tables below show Council's investments and risk management instruments holdings per counter party during the quarter.

Term deposits

Counter party	Oct-2017		Nov-2017		Dec-2017		Compliance
	$000	%	$000	%	$000	%	
NZ Registerd Bank 1	25,000	29.41%	25,000	27.17%	15,000	35.71%	✔
NZ Registerd Bank 2	45,000	52.94%	52,000	56.52%	17,000	40.48%	✔
NZ Registerd Bank 3	15,000	17.65%	15,000	16.30%	10,000	23.81%	✔
	85,000	100%	92,000	100%	42,000	100%	

*Policy Limit: 60% of total investments or $25million; whichever is greater

Interest rate swaps

Counter party	Oct-2017		Nov-2017		Dec-2017		Compliance
	$000	%	$000	%	$000	%	
NZ Registerd Bank 1	65,000	31.99%	65,000	31.99%	50,000	29.72%	✔
NZ Registerd Bank 2	93,213	45.87%	93,213	45.87%	73,213	43.52%	✔
NZ Registerd Bank 3	45,000	22.14%	45,000	22.14%	45,000	26.75%	✔
	203,213	100%	203,213	100%	168,213	100%	

*Policy Limit: 50% of total instruments or $80million; whichever is greater

32 Council was in full compliance with all counterpart credit limits during the quarter ended 31 December 2017.

CONSIDERATIONS

Policy considerations

33 There are no policy considerations other than those already noted in this report.

Legal considerations

34 There are no legal considerations arising from this report.

Financial considerations

35 There are no financial considerations other than those already noted in this report.

Tāngata whenua considerations

36 There are no tāngata whenua considerations arising from this report.

SIGNIFICANCE AND ENGAGEMENT

37 This matter has a low level of significance under Council Policy.

Publicity

38 There are no publicity considerations arising from this report.

RECOMMENDATIONS

39 That the Audit and Risk Committee notes that the Council was fully compliant with its Treasury Management Policy for the quarter ended 31 December 2017.

Report prepared by

Anelise Horn
Manager, Financial Accounting

Approved for submission	**Approved for submission**
Natasha Tod **Group Manager** **Regulatory Services**	**Janice McDougall** **Acting Group Manager** **Corporate Services**

ATTACHMENT

Appendix 1: Treasury Management Policy (October 2017)

TREASURY MANAGEMENT POLICY

October 2017

Table of Contents

Introduction 4
Purpose 4
General Policy Objectives 4
Governance 5
Liability Management Policy 6
Objectives 6
General Policy 6
Specific Borrowing Limits 6
Security 7
Borrowing Mechanisms 7
Debt Repayment 7
The LGFA 7
Internal Borrowing 8
Guarantees / contingent liabilities and other financial arrangements 8
Investment Policy 9
General Policy 9
Investment Mix 9
Equity Investments 9
Property Investments 9
Loan Advances 9
Development and Financial Contributions 10
Financial Investments 10
The LGFA 10
Treasury Risk Management 11
Liquidity / Funding Risk 11
Interest Rate Risk 11
Credit Risk 11
Liquidity / Funding Risk 11
Interest Rate Risk 12
Interest Rate Risk Control Limits 13
Counterparty Credit Risk 14
Legal Risk 15
Operational Risk 16
Foreign Exchange Risk 16

Concentration Risk 16
Volatility Risk 16
Carbon Credit Risk 16
Treasury Performance 16
Policy review 17
Appendix 1: Glossary of terms 18
Appendix 2: Delegated Authorities 20
Appendix 3: Current approved interest rate instruments...................................... 22

First adopted	*October 2017*
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Document number:	3457122
Associated documents:	
Policy Owner:	Group Manager, Corporate Services

Introduction

1. The Kāpiti Coast District Council's Treasury Management Policy comprises a liability management policy and an investment policy, as required by the Local Government Act 2002 (the Act).

2. 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.

3. 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.

Purpose

4. The Treasury Management 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.

General Policy Objectives

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

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

7. 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.

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

Governance

9. The 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 Council is responsible for approving this Treasury Management Policy and any changes to it required from time to time.

10. The authority to make or change the Policy has been delegated to the Operations and Finance Committee. The Policy can be reviewed by other persons, and changes recommended but the authority to make or change the policy rests with the Operations and Finance Committee.

11. The Council may delegate its responsibilities under this Policy to its committees, subcommittees and officers in accordance with its Governance Structure and Delegations.

12. The full list of delegated authorities as they relate to the Treasury Management Policy is attached as Appendix 2.

13. 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.

Liability Management Policy

Objectives

14. 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 to meet planned and unforeseen cash requirements;
- prudently manage the Council's credit exposure;
- monitor and report on the risk and the performance of debt portfolios against predetermined limits and benchmarks;
- maintain a credit rating of at least A- from Standard & Poor's.

General Policy

15. The Council's liabilities comprise borrowings (internal / external) 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.

16. Any new borrowings or roll-over of existing borrowing needs to be budgeted for as part of Council's approved Long Term Plan or Annual Plan, or be subject to Council approval. Debt will be repaid as it falls due in accordance with the applicable loan agreement.

17. Any debt with a maturity beyond 12 years must be approved by the Operations and Finance Committee at its next meeting.

Specific Borrowing Limits

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

Item[1]	Borrowing Target	Borrowing Limit
Net interest expense over total operating income	< 10%	< 20%
Net external debt over total operating income	< 200%	< 240%
Liquidity	> 110%	> 110%

[1] Definitions of these and other terms are given in the glossary of terms attached as Appendix 1.

Security

19. 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, Council's borrowing is secured by a floating charge over all Council rates levied under the Local Government Rating Act. The security offered by Council ranks equally with other lenders.

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

Borrowing Mechanisms

21. The Council is able to borrow through a variety of market mechanisms including issuing stock / debentures and commercial paper, direct bank borrowing, the Local Government Funding Agency (LGFA) 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;
    - Consideration of counterparty credit risk by spreading borrowings across a number of counterparties to avoid concentrations of credit exposure.

22. 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 its investors, the LGFA and financial institutions / brokers.

Debt Repayment

23. The Council repays borrowings from refinancing or surplus general funds. Borrowings may be refinanced by further borrowings with a 30 year maximum term.

24. 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.

The LGFA

25. 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.

Internal Borrowing

26. The internal borrowing relates to Council borrowing from its reserves, special funds and equity that the Council would otherwise have in cash. Council has borrowed these funds to fund capital works which would otherwise be funded from external borrowers.

27. Any internal borrowing of reserve and special funds used must be reimbursed for interest revenue lost. Except where a specific rate has been approved for particular circumstances, interest is charged annually in arrears on all internal loans using the Council's current cost of borrowings.

Guarantees / contingent liabilities and other financial arrangements

28. The Council, from time to time, provides financial guarantees to local organisations, groups or bodies for recreational and community purposes. Council is not allowed to guarantee loans to Council Controlled Trading Organisations under Section 62 of the Local Government Act.

29. 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 at any time shall be taken into account when calculating the Council's maximum borrowing limit.

30. Council will ensure that sufficient funds or lines of credit exist to meet amounts guaranteed.

Investment Policy

General Policy

31. Council may hold financial, property and equity investments if there are strategic, economic or other valid reasons for doing so, for example, where it is the most appropriate way to administer a Council function.

32. 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 Council's approved Long Term Plan or Annual Plan, or be approved through a Council resolution.

33. The authority to acquire and dispose of financial investments is delegated to the Group Manager, Corporate Services.

Investment Mix

Equity Investments

34. The Council currently maintains equity investments in Civic Financial Services Limited (formerly the New Zealand Local Government Insurance Corporation Limited). These shares were acquired by virtue of the Council insuring its past activities through these companies. They are held as they are not readily transferable, and the amount involved is immaterial, relative to the Council's total investment holdings.

35. New equity investments may be acquired if an opportunity arises and approval is given by Council, based on advice and recommendations from Council officers. Before approving any new investment, Council gives due consideration to the contribution the investment will make in fulfilling Council's strategic objectives, and the financial risks of owning the investment.

Property Investments

36. Strategic Land Purchase - the Council has adopted a strategy of purchasing land when the opportunity arises, where this has been identified as progressing the community's and Council's vision for the future.

37. Each individual property purchase is subject to consideration and / or approval by the Operations and Finance Committee.

Loan Advances

38. The Council will only advance loans to community organisations in exceptional circumstances. Where loan advances are secured against the assets of the borrower, those assets would revert to the Council in the event of loan default. New loan advances are by Council resolution only.

39. All loan advances are monitored to ensure that interest and principal repayments comply with the terms of the loan agreement. All loans in excess of $25,000 are reported on a quarterly basis to the Operations and Finance Committee.

Development and Financial Contributions

40. In order to make it easier for developers to finance large-scale developments, the Council may allow payment of development and financial contributions on some residential developments to be deferred for a period. Payment arrangements, for example, bank bonds can be used as security against the assets of the developer so that those assets would revert to the Council in the event of default of the payment of development / financial contributions.

Financial Investments

41. Council's primary objective when investing is the protection of its investment capital. Accordingly, Council may only invest in approved creditworthy counterparties. Counterparties and limits can only be approved on the basis of long-term Standard & Poor's, credit ratings (or equivalent Fitch or Moody's rating) being A+ and above and / or short term rating of A-1 or above.

42. With the exception of cash investments that are sourced from pre-funding, all other cash investments must be restricted to a term of no more than 91 days to ensure that future cash flow requirements and capital expenditure projections are met. Cash investments from pre-funding can be invested for up to a maximum of 18 months.

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

The LGFA

44. The Council may invest in shares and other financial instruments of the LGFA, and may borrow to fund that investment. The Council's objective in making any such investment will be to:

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

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

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

Treasury Risk Management

47. Borrowing exposes the Council to three principal risks:

Liquidity / Funding Risk

48. Liquidity risk is the risk that the Council does not have the ability to access committed funding at a future time as required. Funding risk centres on the ability to re-finance or raise new debt at acceptable pricing and maturity terms.

Interest Rate Risk

49. Interest rate risk is the risk that the Council will be exposed to changes in market conditions, particularly wholesale interest rates, prevailing at any time. It is important to consider this on a forward looking basis when issuing new debt and refinancing existing debt on an on-going basis. It may impact on the maturity profile of issued debt and the process of re-financing.

Credit Risk

50. Credit risk is the risk that a party to a transaction, such as a counterparty or a financial intermediary / institution, may not settle or provide committed funding as and when required. This risk is applicable where the Council is both a borrower and an investor, with the more significant risk arising when the Council is an investor.

51. Other risks include legal risk, operational risk, foreign exchange risk, concentration risk, volatility risk and carbon credit risk.

Liquidity / Funding Risk

52. A key factor in the management of liquidity 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.

53. The following control limits apply to Council's management of liquidity risk:

    a. The Council will ensure that it has sufficient funds available to:

        - fund all roll-over debt, and
        - pay all financing costs.

    b. External term loans and committed debt facilities together with available liquid investments must be maintained at an amount of 110% over existing external debt.

    c. Council has the ability to pre-fund up to 18 months forecast debt requirements including re-financings.

    d. The Chief Executive has delegated to the Group Manager Corporate Services the discretionary authority to re-package existing debt on more favourable terms. Such action is to be ratified and approved by the Operations and Finance Committee at its next scheduled meeting.

e. The Council can borrow for a maximum term of 30 years. Any debt issued for longer than 10 years will be reported to the Operations and Finance Committee at the next quarterly reporting period.

f. The maturity profile of the total committed funding with respect to all external loans / debt and committed facilities, calculated monthly on a rolling basis is to be within the following limits:

Period	**Minimum**	**Maximum**
0 to 3 years	**10%**	**70%**
3 to 5 years	**10%**	**60%**
5 to 10 years	**10%**	**50%**
10 years plus	**0%**	**20%**

A maturity schedule 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 for a period beyond 90 days requires specific approval by the Operations and Finance Committee not later than the next available meeting.

Interest Rate Risk

54. Interest rate risk is the risk that funding costs (due to movements in market interest rates) will materially exceed adopted Annual Plan and Long Term Plan interest cost projections, so as to adversely impact cost control, capital investment decisions, returns and feasibility.

55. The primary objective of interest rate risk management is to reduce uncertainty of interest rate movements through fixing of wholesale market interest costs. Certainty around interest costs is to be achieved through the active management of underlying interest rate exposures.

56. Dealing in interest rate products must be limited to financial instruments approved by the Council as per an internally updated schedule. Credit exposure on these financial instruments is restricted by specified counterparty credit limits.

57. A list of the current approved interest rate instruments is attached as Appendix 3.

58. All bank deposits, registered certificates of deposits, treasury bills and commercial paper investments are limited to a term no greater than three months unless linked to a debt pre-funding strategy.

59. All unsecured investment securities must be senior in ranking. The following types of investment instruments are expressly excluded:

- structured debt where issuing entities are not a primary borrower / issuer;
- subordinated debt, junior debt, perpetual notes and debt / equity hybrid notes such as convertibles.

60. Any other financial instrument not on the approved list must be specifically approved by the Council on a case-by-case basis and only be applied to the one singular transaction being approved.

Interest Rate Risk Control Limits

61. Major control limit – at any point in time the amount of all current interest rate risk management instruments must not exceed the total amount of gross debt.

62. Hedging of Council's external debt / borrowings must be within the following fixed/ floating interest rate risk control limit:

Master Fixed / Floating Risk Control Limit	
Minimum Fixed Rate = 55%	Maximum Fixed Rate = 100%

The percentages are calculated on the projected external debt levels in the Council's approved financial statements (Long Term Plan or Annual Plan). The forecast debt level is subject to approval by the Group Manager, Corporate Services as being a fair and reasonable forecast.

a. External debt is the total amount of gross debt. 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 comply with the Treasury Management Policy minimums and maximums.

b. Floating rate debt may be spread over any maturity up to 12 months. Bank advances may be for a maximum term of 12 months.

c. The Council can hedge up to 15 years; any hedge longer than 10 years will be reported to the Operations and Finance Committee at the next quarterly reporting period.

63. The fixed rate amount at any point in time must be within the following maturity bands:

Fixed Rate Maturity Profile Limit (% of External debt)		
Period	Minimum Cover	Maximum Cover
1 to 3 years	15%	60%
3 to 5 years	15%	60%
5 to 10 years	15%	60%*
10 years plus	0%	20%**

**Maximum cover in the five to ten year period may be extended up to 70% during periods of historical low long term interest rates subject to approval by the Chief Executive and reported to the Operations and Finance Committee at its next meeting.*

***Maximum cover in the over ten year period may be extended up to 30% during periods of historical low long term interest rates subject to approval by the Chief Executive and reported to the Operations and Finance Committee at its next meeting. The definition of 'historical low long term interest rate' is where the 10-year swap rate is more than 15% below its rolling ten year average.*

a. 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 beyond 90 days requires specific approval by Council at the next available meeting.

b. Any interest rate swaps with a maturity beyond 12 years must be approved by the Operations and Finance Committee at its next meeting.

64. For individual types of interest rate risk management instruments Council must adhere to the following control limits at all times:

a. Forward rate agreements outstanding at any one time must not exceed 75% of the total floating rate debt.

b. With the exception of 1:1 collar option structures, interest rate options must not be sold outright because of the speculative nature of doing this.

c. Borrower swaptions held by Council must mature within 12 months.

d. Interest rate options with a maturity date beyond 12 months that have a strike rate higher than 2.00% above the appropriate swap rate, cannot be counted as part of the fixed rate cover percentage calculation.

e. The forward start period on swap / collar strategies to be no more than 24 months.

Counterparty Credit Risk

65. Counterparty credit risk is the risk of losses (realised or unrealised) arising from a counterparty defaulting on a financial instrument where the Council is a party. The credit risk to the Council in a default event will be weighted differently depending on the type of instrument entered into.

66. Counterparties and limits can only be approved on the basis of a minimum long term credit rating (Standard & Poor’s or Moody’s Investor Services) being A+ and a minimum short term rating of A-1.

67. Limits should be spread amongst a number of counterparties to avoid concentrations of credit exposure. The approval process to allow the use of individual financial instruments must take into account the liquidity of the market the instrument is traded in and repriced from.

68. The following table shows the gross counterparty limits:

Counterparty/ Issuer	Minimum Standard and Poor's long term / short term credit rating	Investments maximum per counterparty	Risk management instruments maximum per counterparty	Borrowing maximum per counterparty
NZ Government	N/A	Unlimited	None	Unlimited
LGFA	AA- / A-1	20.0	None	Unlimited
NZ Registered Bank	A+ / A-1	60% of total investments or $25m; whichever is greater.	50% of total instruments or $80m; whichever is greater.	$50m

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

a. Money Market (e.g. Bank Deposits) – Transaction Notional x Weighting 100%.

b. Interest Rate Risk Management (e.g. swaps, FRA's) – Transaction Notional x Maturity (years) x 3%.

c. Foreign Exchange - Transactional face value amount x the square root of the Maturity (years) x 15%.

70. A counterparty profile that is outside the above limits, but self-corrects within 90-days is not in breach of this Policy. Any departures from the above limits will be reported to the Operations and Finance Committee at its next meeting.

Legal Risk

71. 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.

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

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

Operational Risk

74. 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.

Foreign Exchange Risk

75. Council has limited Foreign exchange risk through the occasional purchase of foreign exchange denominated plant and equipment. Larger amounts may be hedged using foreign exchange contracts and smaller payments are converted at the spot exchange rate on the date of payment. The Council does not borrow or enter into incidental arrangements within or outside New Zealand in any foreign currency other than New Zealand dollars.

Concentration Risk

76. This is the risk of a loss arising as a result of a heavily lopsided exposure to one or more counterparties. The risk is managed through adherence to the gross counterparty limits.

Volatility Risk

77. This is the risk of a change of price of a portfolio as a result of changes in the volatility of a risk factor. The risk is managed through ensuring that the asset allocation is continuously reviewed to ensure that it stays diversified over the long term.

Carbon Credit Risk

78. The Council needs to minimise the financial impact of movements in the carbon credit prices by balancing the need for price stability with the benefit of realising market opportunities to reduce costs as they arise.

Treasury Performance

79. In order to assess the effectiveness of Council's treasury management activities, benchmarks and performance measures have been prescribed to assess operational performance and the management of debt and interest rate risk. The Council undertakes regular reporting which includes the following four major information/ reporting objectives:

    a. Cash / Debt Position.

    b. Risk Exposure Position.

    c. Risk Management Performance.

    d. Treasury Management Policy Compliance.

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

Report type	Audience	Frequency	Format
Management	Senior Leadership Team	Quarterly	Report compliance with all limits and thresholds
Governance	Audit and Risk Committee	Quarterly	Overview of quarterly performance
Annual Report	Operations and Finance Committee	Annually	Review of Annual performance and of the Policy and policy limits to ensure they are fit for purpose

Policy review

81. The Policy is to be formally reviewed on at least a triennial basis by the Operations and Finance Committee. The Group Manager, Corporate Services will manage the review process and the final report will be presented by to the Operations and Finance Committee for its consideration.

82. In addition, any Policy changes arising from the annual report to the Operations and Finance Committee provided by the Group Manager, Corporate Services or other sources may be considered by the Audit and Risk Committee as required, but the delegation rests with the Operations and Finance Committee.

Appendix 1: Glossary of terms

Annual rates income: the amount equal to the total revenue from any funding mechanism authorised by the Local Government (Rating) Act 2002.

Borrower swaption: gives the holder of the swaption the right to enter into a swap where they pay interest on a notional loan amount at a fixed rate of interest and receive payments at a floating rate;

Call option: a financial instrument that gives the buyer the right, but not an obligation, to buy a set quantity of a security at a set strike price at some time on or before expiration.

Closing out: the cancellation / termination of a financial instrument or contract before its maturity date, resulting in a realised gain / loss if the current market rate differs from the contract rate.

Derivatives: investment vehicles whose price is dependent on an underlying asset. The most common forms of derivatives include stock options, futures & swaps.

Fixed rate: an interest rate repricing date beyond 12 months forward on a continuous rolling basis;

Floating rate: an interest rate repricing within 12 months;

Forward rate agreement: an agreement between two counterparties locking in an interest rate today, for money that one counterparty intends to borrow in the future. The counterparties agree to pay each other the interest difference between the agreed-upon rate (the "forward rate") and the actual interest rate on the future date (the "floating rate").

Forward start interest rate swap: a fixed-for-floating interest rate swap whereby the swap coupon is set at the contract date but the swap doesn't start on that date, that is it is delayed to some future date. This provides certainty as to interest rate cost on an agreed principal amount for an agreed period, commencing at a future point in time.

Futures contract: a financial contract obligating the buyer to purchase an asset (or the seller to sell an asset), such as a physical commodity or a financial instrument, at a predetermined future date and price.

In the money options: options which have intrinsic value of the security built into them. Call options are in the money when the strike price is lower than the price of the underlying stock, allowing one to buy the stock at a price lower than the market price. Put options are in the money when the strike price is higher than the price of the underlying stock, allowing one to sell the stock at a price higher than the market price.

Interest rate cap (ceiling): an interest rate derivative contract which has a maximum value (cap) – on a floating rate of interest on a specified notional principal amount for a specific term.

Interest rate collar: a security which simultaneously combines the purchase of an interest rate cap and the sale of an interest rate floor to specify a range in which an interest rate will fluctuate. The security insulates the buyer against the risk of a significant rise in a floating rate, but limits the benefits of a drop in that floating rate.

Interest rate floor: an interest rate derivative contract which has a minimum value (floor) – on a floating rate of interest on a specified notional principal amount for a specific term.

Interest rate option: a specific financial derivative contract whose value is based on interest rates and its value is tied to an underlying interest rate. Interest rate options give buyers the right, but not the obligation, to synthetically pay (in the case of a cap) or receive (in the case of a floor) a predetermined interest rate (the strike price) over an agreed period.

Interest rate swap: a financial derivative instrument in which two parties agree to exchange interest rate cash flows, based on a specified notional amount from a fixed rate to a floating rate (or vice versa) or from one floating rate to another;

Liquidity: external term loans plus committed debt facilities plus available cash / cash equivalents divided by external debt.

Net external debt: total external debt less cash / cash equivalent investments.

Net interest expense: the amount equal to all interest and financing costs less interest income for the relevant period.

Operating income: earnings from rates, government grants and subsidies, user charges, interest and other revenue and excludes non-government capital contributions (e.g. developer contributions and vested assets).

Options: contracts that give the holder the right but not the obligation to buy or sell a specific security at a pre-determined price on a pre-determined date. The two kinds of options are call and put options.

Options on a swap (Swaption): the option to enter into an interest rate swap. In exchange for an option premium, the buyer gains the right but not the obligation to enter into a specified swap agreement with the issuer on a specified future date.

Out of the money options: have no intrinsic value built into them. Call options are out of the money when the strike price is higher than the price of the underlying stock. Put options are out of the money when the strike price is lower than the price of the underlying stock.

Put option: a financial instrument that conveys the buyer the right, but not the obligation, to sell a specified quantity of a security at a set strike price on or before an agreed upon expiration date.

Spot price: the current market price of a product, usually a commodity, currency or rate, for the immediate delivery of said product.

Strike price: the price at which a derivatives contract can be exercised - the strike price is independent of the spot price and is agreed upon by the parties entering the contract.

Swap: a derivative in which two counterparties exchange cash flows of one party's financial instrument for those of the other party's financial instrument. The benefits in question depend on the type of financial instruments involved.

Appendix 2: Delegated Authorities

	Activity	Delegated Authority	*Limit
1	Approving and changing Treasury Management Policy	Operations and Finance Committee	Unlimited
2	New annual borrowing as set out in the Annual Plan/Long Term Plan	Operations and Finance Committee	Within the prescribed limits set out in the Financial Strategy
3	Approval for charging assets as security over borrowing	Operations and Finance Committee	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 (or) Group Manager, Corporate Services	Subject to Policy
8	Manage cash / liquidity requirements	Chief Executive (or) Group 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 delegated to the Group Manager, Corporate Services; each adjustment individually signed off by the Chief Executive	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 Group Manager, Corporate Services	Per risk control limits
12	Maximum daily transaction amount (borrowing, investing and interest rate risk management) excludes roll-overs on existing debt and interest rate swaps	Council Chief Executive Group Manager, Corporate Services CFO (delegated)	Unlimited $30 million $15 million $5 million

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

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

Appendix 3: Current approved interest rate instruments

Category	Instrument
Cash management and borrowing	1. Bank overdraft 2. Committed cash advance and bank accepted bill facilities (short term and long term loan facilities) 3. Uncommitted money market facilities 4. Retail and Wholesale Bond and Floating Rate Note (FRN) issuance 5. Commercial paper (CP) / Promissory Notes 6. NZD denominated Private Placements
Investments	1. Call and short term bank deposits 2. Bank bills 3. Bank registered certificates of deposit (RCDs) 4. Treasury bills 5. LGFA borrower notes / CP / bills / bonds/ FRNs 6. LGFA Redeemable Preference Shares (RPS)
Interest rate risk management	1. Forward rate agreements ("FRAs") on: • bank bills 2. Interest rate swaps including: • forward start swaps • amortising swaps (whereby notional principal amount reduces) • swap extensions and shortenings 3. Interest rate options on: • bank bills (purchased caps and one for one collars) • interest rate swaptions (purchased only)
Foreign exchange management	1. Spot foreign exchange 2. Forward exchange contracts