



Treasury Policy Kaupapa here Kaupapa Rawa

The purpose of the Treasury Policy is to outline approved policies and procedures in respect of all treasury activity to be undertaken by Western Bay of Plenty District Council.

The formalisation of such policies and procedures will enable treasury risks within Council to be prudently managed.

1. Policy objective

Council has Treasury risks arising from debt raising, investments and associated interest rate management activity.

Treasury activities are:

- compliance with the Local Government Act 2002
- develop and maintain professional relationships with the financial markets
- invest surplus cash in liquid and creditworthy investments
- raise appropriate finance, in terms of both maturity and interest rate
- manage the overall cash position of Council's operations.

2. General approach

2.1 Council is a risk-averse entity and does not wish to seek risk from its Treasury activities.

2.2 Activity which may be construed as speculative in nature is expressly forbidden.

2.3 Council manages both liabilities and cash investments through an internal Treasury activity. Funds are advanced by the Treasury activity for a specific period. Loans are repaid to the Treasury activity based on standard loan lives, depending on the useful lives of the assets.

2.3.1 Interest for loans is based on Council's weighted cost of funds.

2.3.2 Interest is credited to activities based on investment rates.

3. Liability management policy

3.1 Council approves borrowing by resolution during the Annual Planning process.

3.2 Council raises borrowing for the following primary purposes:

3.2.1 General debt to fund Council's Balance Sheet.

3.2.2 Specific debt associated with "special one-off" projects and capital expenditure.

3.2.3 To fund assets with inter-generational qualities.

3.3 Specific borrowing limits

In managing borrowing, Council will adhere to the following limits:

- the net interest expense of all external borrowings will not exceed 20% of total revenues
- the net interest expense of all external borrowings will not exceed 25% of annual rates revenue
- liquid ratio of $\geq 1:1.10$
- current ratio ≥ 1.25
- liquidity ratio (external term debt plus committed loan facilities plus available liquid short term financial investments divided by existing external debt) to be greater than 110%
- The percentage of net external debt to total revenue to be less than 180% in 2021 to 2031.

'Revenue' is defined as earnings from rates, government grants and subsidies, user charges, interest and other revenue.

'Rates' is defined as all revenue under the Local Government (Rating) Act 2002, excluding rates collected on behalf of the Bay of Plenty Regional Council.

'Total revenue' for the purposes of this policy includes: earnings from rates revenue; grants and subsidies; user charges; interest and other operating revenue (excluding vested assets and financial contributions).

3.4 Liquidity and credit risk management

3.4.1 Council's ability to readily attract cost-effective borrowing is largely driven by its ability to maintain a strong balance sheet, as well as its ability to rate, manage its image in the market and its relationships with bankers. Where possible, Council seeks a diversified pool of stock and bank borrowing and ensures that bank borrowings are only sought from the approved list of registered banks.

3.4.2 To minimise the risk of large concentrations of debt maturing or being reissued in periods where credit margins are high for reasons within or beyond Council's control, Council ensures debt maturity is spread widely over a band of maturities. Council manages this specifically by ensuring that:

- No more than 35% of total borrowing is subject to refinancing in any financial year. Total borrowing includes any forecast borrowing.

3.4.3 Council's liquidity ratio includes both cash and cash equivalents, and Council's guaranteed external facilities (2021:\$30m).

3.4.4 New Zealand Local Government Funding Agency Limited investment

The Council may borrow from the New Zealand Local Government Funding Agency Limited (LGFA) and, in connection with that borrowing, may enter into the following related transactions to the extent it considers necessary or desirable:

- (a) Contribute a portion of its borrowing back to the LGFA as an equity contribution to the LGFA.
- (b) Provide guarantees of the indebtedness of other local authorities to the LGFA and of the indebtedness of the LGFA itself.
- (c) Commit to contributing additional equity (or subordinated debt) to the LGFA if required.
- (d) Subscribe for shares and uncalled capital in the LGFA; and
- (e) 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.

3.5 Risk recognition

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

A key factor of funding risk management is to spread and control the risk to reduce the concentration of risk at one point in time. This is so that if any of the above events occur, the overall borrowing cost is not unnecessarily increased and the desired maturity profile is not compromised due to market conditions.

3.6 Liquidity/funding risk control limits (borrowings)

3.6.1 Term debt and committed debt facilities must be maintained at an amount that exceeds 110% of projected peak net debt levels over the next year (per long term cash and debt forecasts).

3.6.2 Disaster recovery requirements are met through the liquidity ratio.

3.6.3 The maturity profile of the total committed funding in respect to all loans and committed facilities is to be controlled by the following system and apply when external debt exceeds \$25 million:

Council has the ability to pre-fund up to 18 months forecast debt requirements including re-financings. Debt refinancing that have been prefunded, will remain included within the funding maturity profile until their maturity date

A maturity schedule outside these limits requires specific Council approval.
 A 12-month phase-in, non-compliance period is permitted.

3.7 Interest rate risk management

Council’s borrowing gives rise to direct exposure to interest rate movements. Generally, given the long-term nature of Council’s assets, projects and inter-generational factors and Council’s preference to avoid an adverse impact on rates, there is a general tendency to have a high percentage of long-term fixed rate or hedged borrowing.

3.8 Approved financial instruments

Dealing in interest rate products must be limited to financial instruments approved by the Council. Any other financial instrument must be specifically approved by Council on a case-by-case basis and only be applied to the one singular transaction being approved.

Category	Instrument
Cash management and borrowing	<ul style="list-style-type: none"> • Bank overdraft • Committed cash advance and bank accepted bill facilities (term facilities) • Uncommitted money market facilities • Loan stock / bond issuance • Commercial paper (CP) / bills / promissory notes • Finance leases
Interest rate risk Management	Forward rate agreements (‘FRAs’) on: <ul style="list-style-type: none"> • Bank bills • Government bonds. Interest rate swaps including: <ul style="list-style-type: none"> • Forward start swaps (start date <24 months) • Amortising swaps (whereby notional principal amount reduces) • Swap extensions and shortenings Interest rate options on: <ul style="list-style-type: none"> • Bank bills (purchased caps and one for one collars) • Government bonds • Interest rate swaps (purchased only).

3.9 Interest rate risk control limits

Exposure to interest rate risk is managed and mitigated through the risk control limits below. Council’s forecast core external debt should be within the following fixed/floating interest rate risk control limit, and will apply when forecast core debt exceeds \$25 million.

- Core external debt is defined as gross external debt. When approved forecasts are changed, the amount of fixed rate cover in place may have to be adjusted to ensure compliance with the Policy minimums and maximums.

Debt Interest Rate Policy Parameters (calculated on a rolling basis)

Period	Minimum Fixed	Maximum Fixed
0 - 2 Yrs	40%	100%
2 - 5 Yrs	20%	80%
5 - 10 Yrs	0%	60%

“Fixed Rate” is defined as an interest rate repricing date beyond 12 months forward on a continuous rolling basis.

“Floating Rate” is defined as an interest rate repricing within 12 months.

The percentages are calculated on the rolling projected core debt level calculated by management (signed off by the CFO).

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- A fixed rate maturity profile that is outside the above limits, however self corrects within 90-days is not in breach of this Policy. Maintaining a maturity profile beyond 90-days requires specific approval by Council.
 - Floating rate debt may be spread over any maturity out to 12 months. Bank advances may be for a maximum term of 12 months.
 - Any interest rate derivatives with a maturity beyond 16 years must be approved by Council. The exception to this will be if council raises LGFA funding as fixed rate and this maturity is beyond 16 years.
 - Hedging outside the above risk parameters must be approved by Council.
 - Interest rate options must not be sold outright. However, one for one collar option structures are allowable, whereby the sold option is matched precisely by amount and maturity to the simultaneously purchased option. During the term of the option, only the sold side of the collar can be closed out (i.e. repurchased) otherwise, both sides must be closed simultaneously. The sold option leg of the collar structure must not have a strike rate “in-the-money”.
 - Purchased borrower swaptions mature within 12 months.
 - Interest rate options with a maturity date beyond 12 months that have a strike rate (exercise rate) higher than 2.00% above the appropriate swap rate, cannot be counted as part of the fixed rate hedge percentage calculation.
 - The forward start period on swap/collar strategies is to be no more than 24 months, unless the forward start swap/collar starts on the expiry date of an existing fixed interest rate instrument (i.e. either derivative or fixed rate borrowings) and has a notional amount which is no more than that of the existing fixed interest rate instrument

3.10 Loan payments

External loans are repaid on due date. The lengths of external loans are based on projected internal loans and cash requirements.

4. Investment policy

4.1 Council maintains investments in the following financial assets:

- Equity investments including shareholdings and loan advances to trading and service enterprises, charitable trusts and incorporated societies; for example sporting and community organisations
- Property investments, including land and buildings
- Treasury instruments incorporating longer term and liquidity investments.

4.2 Equity investments and loan advances

Investments include shareholdings in trading and service enterprises and loan advances to charitable trusts, incorporated societies, residential and rural housing which are consistent with Council's Long Term Plan. Council operates an internal borrowing system for funding infrastructural improvements as well as funding current accounts. This information is reported to Council on a quarterly basis.

4.2(a) New Zealand Local Government Funding Agency Limited Investment:

- The Council may invest in shares and other financial instruments of the New Zealand Local Government Funding Agency Limited (LGFA) and may borrow to fund that investment
- The Council's objective in making any such investment will be to:
 - (a) obtain a return on the investment; and
 - (b) ensure that the LGFA has sufficient capital to become and remain viable, meaning that it continues as a source of debt funding for the Council.
- Because of this dual objective, 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.

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

4.3 Property investments

Council's overall objective is to only own property that is necessary to achieve its strategic objectives.

Council reviews property ownership through assessing the benefits of continued ownership in comparison to other arrangements which could deliver the same results.

4.4 Treasury investments

Council maintains treasury investments for the following primary reasons:

- provide ready cash in the event of a natural disaster. This cash is intended to bridge the gap between the disaster and the reinstatement of normal revenue streams and assets
- invest amounts allocated to accumulated surplus, Council created and restricted reserves, sinking funds and general reserves
- invest funds allocated for approved future expenditure, to implement strategic initiatives or to support inter-generational allocations
- invest proceeds from the sale of assets
- invest surplus cash and working capital funds.

4.5 Counterparty credit risk

Counterparty credit risk is the risk of losses (realised or unrealised) arising from a counterparty defaulting on a financial instrument where Council is a party.

The credit risk to Council in a default event will be weighted differently depending on the type of instrument entered into.

Council will regularly review credit risk. Treasury related transactions would only be entered into with organisations specifically approved by Council.

Counterparties and limits can only be approved on the basis of long term credit ratings (Standard and Poor's or Moody's) being A- and above or short term rating of A-1 or above.

Council is not a long-term investor in Treasury investments.

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

The following matrix guide below will determine limits:

The combined holdings of entities rated BBB to A shall not exceed \$10 million.

The combined holdings of corporates and financials shall not exceed \$10 million.

Authorised Asset Classes	Overall Portfolio Limit as a Percentage of the Total Portfolio	Approved Financial Market Investment Instruments (must be denominated in NZ dollars)	Credit Rating Criteria - Standard and Poor's (or Moody's or Fitch equivalents)	Limit for each issuer
New Zealand Government	100%	Government Stock/Treasury Bills	Not Applicable	Unlimited
Supranationals	50%	Bonds/MTNs/FRNs	AAA	Maximum of \$10 million
New Zealand Registered Banks	100%	Call/Deposits/Bank Bills/ Commercial Paper Bonds/MTNs/FRNs	Short term S&P rating of A-1+ Short term S&P rating of A-1 Long term rating of A+ or better	Maximum of \$30 million Maximum of \$10 million Maximum of \$10 million
Rated Local Authorities ("RLA")	50%	Commercial Paper/Bonds/MTNs/ FRNs	Minimum short term S&P rating of A-1 or minimum long term S&P rating of A+	Maximum of \$10 million
State Owned Enterprises ("SoE")	50%	Commercial Paper/ Bonds/ MTNs/FRNs	Short term S&P rating of A-1+ or long term rating of A+ or better Short term S&P rating of A-1 or long term rating of BBB to A	Maximum of \$10 million Maximum of \$5 million
Corporates	30%	Commercial Paper/Bonds/MTNs/ FRNs	Short term S&P rating of A-1+ or long term rating of A+ or better Short term S&P rating of A-1 or long term rating of BBB to A	Maximum of \$7 million Maximum of \$3 million
Financials	30%	Commercial Paper/ Bonds/MTNs/FRNs	Short term S&P rating of A-1+ or long term rating of A+ or better Short term S&P rating of A-1 or long term rating of BBB to A	Maximum of \$5 million Maximum of \$2 million

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4.5.1 Treasury investment objectives

Council's primary objective when investing is the protection of its investment. Accordingly, only creditworthy counterparties are acceptable.

Council also seeks to:

- Monitor investment return
- Ensure investments are liquid
- Manage potential capital losses due to interest rate movements if investments need to be liquidated before maturity.

4.5.2 Credit risk is minimised by limiting investments to registered banks, strongly rated State Owned Enterprises (SOE) and corporates within prescribed limits.

4.6 Interest rate risk management

Council's investments give rise to a direct exposure to a change in interest rates, impacting the return and capital value of its fixed rate investments.

Interest rate risk will be managed by reviewing rolling cashflow forecasts and using risk management instruments to protect investment returns and/or to change interest rate and maturity profile.

4.7 Special funds, sinking funds, reserve and endowment funds

Liquid assets are not required to be held against special funds and reserve funds. Instead Council will internally borrow or utilise these funds where ever possible.

4.7.1 Acquisition and disposal of assets

Any disposal of assets requires the approval of Council except those assets within delegated authority.

4.8 Security

Generally, Council does not offer assets or deemed rates as security for general borrowing programmes.

In some circumstances, with prior Council approval, security may be offered:

- On borrowings by granting a rates charge under the Council's Debenture Trust Deed.
- By providing a charge over one or more of the Council's assets.

4.9 Repayment

The Council repays borrowings from the specific sinking fund allocated to that borrowing or from general funds.

4.10 Contingent liabilities

Council from time to time provides financial guarantees to recreation and service organisations. Where possible Council shall obtain cross guarantees. Management ensures that the business plan of the guaranteed party furthers the strategic objectives of Council and that financial statements are received on a regular basis. Should the guarantee be called up, Council will take immediate steps to recover the money.

5. **Foreign exchange policy**

Council has foreign exchange exposure through the occasional purchase of foreign exchange denominated plant, equipment and services.

Generally, all commitments for foreign exchange greater than \$100,000 are hedged using foreign exchange contracts, once expenditure is approved. Council uses both spot and forward foreign exchange contracts.

The use of other foreign exchange risk management products is not permitted.