




Liability Management Policy

Council Resolution Date: 12 April 2017

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Vision

To minimise the cost of borrowing used to fund the capital development of the Community's assets.

Objectives

Council's commitment is to:

- Minimise our long term borrowing costs within approved risk parameters.
- Minimise our exposure to adverse wholesale interest rate and credit margin, movements, maturity and interest rate re-pricing concentrations.
- Maintain appropriate liquidity levels and manage cash flows to meet known and reasonable unforeseen funding requirements.
- Minimise exposure to credit risk.
- Comply with, monitor and report on financing/borrowing covenants and ratios, under the obligations of our lending/security arrangements and this policy.
- Comply with the requirements of the Local Government Act 2002.

Management of borrowings

Council will:

- Consider and approve its forecast borrowing requirements by approving its Long Term Plan and each Annual Plan.
- Manage financial assets and debt on a net portfolio basis (borrowings less cash instruments).
- Prudently and effectively manage borrowings and liabilities having regard to:
  - Interest rate and credit margin exposure
  - Liquidity and funding exposure
  - Counterparty credit exposure
  - Debt repayment
  - Borrowing limits and financial covenants
  - Security arrangements

  (Procedural guidance on each of these matters is set out in appendix one).
- Delegate authority to the Chief Executive Officer to initiate any actions in terms of this policy, including the authority to execute any documents on behalf of Council.

This policy covers internal and external borrowings. Any other Council liabilities are managed in the course of the Council's day-to-day operations.

Borrowing limits

Council will:

- Manage to ensure that the following parameters are not exceeded:

Item	Borrowing limit
Net external debt[1] as a percentage of total revenue[2]	<150%
Net interest[3] on external debt as a percentage of total revenue	<15%
Net interest on external debt as a percentage of annual rates income[4] (debt secured under debenture)	<20%

Interest rate exposure

Movements in interest rates can affect Council's financial performance and funding requirements. Interest rate risk management seeks to minimise interest costs and risks as interest rates change.

To manage interest rate risk on debt Council will:

- Utilise mechanisms including setting risk control limits on fixed and floating rates and the use of interest rate instruments (under the guidance of independent external advisors) on a portfolio basis.

Liquidity and funding

Financial assets and funding sources need to be managed to ensure that Council can meet all of its obligations as they fall due.

Council will:

- Utilise mechanisms to manage liquidity and funding risk include cashflow management and forecasting, maintenance of available committed bank facilities and liquid funds, risk control limits to spread funding maturities and pre-funding of forecast debt requirements.

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[1] Net external debt is defined as total debt less unencumbered cash or cash equivalents.

[2] Revenue is defined as earnings from rates, government grants and subsidies, user charges, interest, dividends, financial and other revenue. Revenue excludes developer contributions and vested assets.

[3] Net Interest is defined as the amount equal to all interest and financing costs less interest income for the relevant period.

[4] 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 Government Authorities (LGAs) for services provided and for which the other LGAs rate.

Credit exposure

Prudent credit management can reduce Council's risk of loss from a counterparty failing to meet its obligations. Credit exposure for borrowings is relevant for the undrawn portion of any committed, standby or bank facility, where the counterparty has a contractual obligation to provide funds to Council. To manage this risk, Council will:

- Set limits on the acceptable credit rating for counterparties.
- Ensure legal documentation is independently reviewed by Council's legal counsel.

Debt repayment

Council will:

- Make debt repayment decisions driven by Council's liquidity profile, contractual terms, debt levels and sustainable funding needs. External debt is managed on a net portfolio basis.
- Only borrow externally when it is commercially prudent to do so.
- Determine the cashflows to be used for the repayment of debt or reduction in borrowing requirements.

Security for debt

Council will:

- Offer security over borrowing by way of a charge over rates and rates revenue through the Debenture Trust Deed.
- From time to time, may offer alternative security over specific assets, with approval by Council and Trustee.

Source of funds

Council consider the following to be appropriate sources of funds:

- Any New Zealand registered bank of suitable credit worthiness (as defined within the credit exposure section of the policy).
- Council reserves, special funds, or surplus cash available for internal borrowing
- Borrowing secured by the Debenture Trust Deed.
- Lease to own arrangements – the counter parties shall be the open market
- Council issued commercial paper, bonds, stock and debentures to the LGFA and wholesale/retail debt capital markets that are secured by the Debenture Trust Deed.

New Zealand Local Government Funding Agency Limited (LGFA)

Despite anything in this Policy, Council may borrow from the LGFA and, in connection with that borrowing, may enter into the following related transactions to the extent we consider necessary or desirable:

- Contribute a portion of our borrowing back to the LGFA as an equity contribution to the LGFA. For example in the form of 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 our borrowing from the LGFA and the performance of other obligations to the LGFA or our creditors with a charge over our rates and rates revenue.
- Subscribe for shares and uncalled capital in the LGFA.

Financial exposure to the LGFA is to be reviewed annually and reported to the Audit and Risk Committee and Council.

Management procedures, reporting and policy review

The Group Manager Business Support will:

- Approve documented treasury and operational procedures for borrowing activities, which will be administered by the Finance and Business Services Manager.

The Chief Executive Officer will:

- Report to Council or the Corporate and Operations Committee of Council on borrowings on at least a quarterly basis.

Council will:

- Formally review this policy on annual basis.

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J E Barnes Mayor	D J McLeod Chief Executive Officer

Version 1

LIABILITY MANAGEMENT POLICY PARAMETERS

Interest rate exposure

Objective
To manage and minimise our costs and risks arising out of interest rate movements associated with our borrowing activities.

Policy parameters
Our borrowings must be within the following fixed/floating interest rate risk control limit:

Master fixed/floating risk control limit	
Minimum fixed rate	**Maximum fixed rate**
55%	90%

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

Fixed rate maturity profile limit		
Period	**Minimum Hedge %**	**Maximum Hedge %**
1 to 3 years	15%	60%
3 to 5 years	15%	60%
5 to 10 years	15%	60%

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.

"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 date within 12 months.

The percentages are calculated on the rolling 12 month projected external core debt level calculated by management (signed off by the Chief Executive Officer). External core debt is debt that is expected to remain outstanding for a period beyond 12 months. . This allows for pre-hedging in advance of projected physical drawdown of new debt and re-financing of existing debt. When approved forecasts are changed, the amount of fixed rate hedges in place may have to be adjusted to ensure compliance with the policy minimums and maximums.

Interest rate risk management products may be used to convert fixed rate borrowing into floating rate, floating rate borrowing into fixed or hedged borrowing. Floating rate debt may be spread over any maturity out to 12 months. Bank advances may be for a maximum term of 12 months. Independent external advisors will be consulted when using interest rate risk management products.

The following instruments may be used for interest rate risk management activity:

Forward rate agreements ("FRA") on:
- Bank bills
- Government bonds

Interest rate swaps including:
- Forward start swaps
- Amortising swaps (whereby notional principal amount reduces)
- Swap extensions and shortenings

Interest rate options on:
- Bank bills (purchased caps and one-for-one collars)
- Interest rate swaptions (purchased swaptions and one-for-one collars with matching notional amounts, and maturity dates only)

Use of interest rate instruments:

- Any interest rate swap with a maturity beyond 12 years must be approved by Council.
- Selling interest rate options for the primary purpose of generating premium income is not permitted, because of its speculative nature.
- 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 out simultaneously.
- 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 percentage calculation.
- Forward start period on swaps and collar strategies to be no more than 24 months, unless the start date of the new swap coincides with the maturity date of the existing swap. The new swap's notional amount must be no greater than that of the existing swap.
- Buying and selling of financial futures is not permitted due to the administrative burden.
- 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.

Liquidity/Funding

Objective
To ensure that we have adequate committed financial resources to meet all of our obligations as and when they arise our liquidity and funding risk management centres on the ability to re-finance or raise new debt at a future time, at acceptable pricing (fees and borrowing margins) and terms.

Our ability to readily attract cost effective borrowing is largely driven by our ability to maintain a strong financial position, raise general rates and manage relationships with investors, financial institutions/brokers and the LGFA. Where practical, we seek a diversified pool of external borrowing and ensure bank borrowings and incidental arrangements (risk management products) are only sought from strongly rated New Zealand registered banks. Banks must have a minimum long term credit rating of single "A".

Policy parameters
Council will manage liquidity and funding risk by:

- Appropriate cashflow management to ensure that sufficient funds are available to meet financial obligations as they fall due.
- Maintaining appropriate committed short-term borrowing facilities with Council's bank counterparties.
- Maintaining financial investments in liquid instruments counterparties within credit risk limits.
- Liquid funds, and committed bank/loan facilities and external term debt are maintained at 110% over the existing external debt amount.
- A spread of debt funding maturities to reduce concentration risk so that credit margins and overall borrowing costs are not unnecessarily increased due to market conditions.
- The Chief Executive Officer or delegate has the discretionary authority to re-finance existing debt on acceptable terms. Such action is to be reported and ratified by Council at the earliest opportunity.
- Council has the ability to pre-fund up to 12 months of forecast debt requirements including debt re-financing.

The funding maturity profile of the total committed funding in respect of all loans and committed facilities is set by the following risk control limits:-

Period	Minimum	Maximum
0 to 3 years	15%	50%
3 to 5 years	15%	60%
5 years plus	10%	40%

A funding maturity profile that is outside the above limits, but self corrects within 90-days is not in breach of this Policy. However, a maturity schedule outside of these limits will require specific Council approval. A maximum of

33% of total committed loans/bonds/FRNs and debt facilities are permitted to mature within an immediate 12 month period.

Liquid funds are defined as those funds which are held for operational requirements and/or used to meet liquidity buffer requirements and include:

- Overnight cash at 100% of principal amounts
- Wholesale /retail bank term deposits no greater than 30 days at 100% of principal amounts
- Bank certificates of deposit (RCD's) less than 365 days at 100% prevailing market value
- Commercial paper less than 365 days at 100% market value.

Credit exposure

Objective
To minimise our risk of default on the part of any counterparty that has a contractual obligation to make any payments to us.

Policy parameters
Proposed counter-parties to borrowing transactions will be assessed to ensure that there is reasonable certainty that obligations under borrowing contracts will be honoured. Financial related transactions will only be entered into with organisations specifically approved by the Council. Counterparties and limits can only be approved on the basis of long-term single "A" and above credit ratings (Standard & Poors', Fitch, or Moody's) and/ or short-term ratings of "A-1" or above. Positions should be spread amongst a number of counterparties to avoid concentrations of credit exposure following matrix guide will determine limits:-

Counterparty	Minimum long term / short term credit rating	Risk management instrument maximum per counterparty ($m)	Total maximum per counterparty ($m)[5]
NZ Local Government Funding Agency (LGFA)	N/A	N/A	N/A
NZ Registered Bank	A / A-1	10.0	30.0

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

- Investments (e.g. bank deposits) – transaction principal amount x weighting 100% (unless a legal right of set-off exists).
- Interest rate risk management (e.g. swaps, FRAs) – transaction Notional x maturity (years) x 3%.
- Foreign exchange – transactional face value amount x the square root of the maturity (years) x 15%.

Debt repayment

Objective
To ensure that we are able to repay debt in a timely manner from appropriate sources.

Policy parameters
We will manage external debt on a net portfolio basis and will only externally borrow when it is commercially prudent to do so. We may determine that all or any part of the following cashflows may be used for the repayment of debt or reduction in borrowing requirements:

- depreciation charges for activities
- the proceeds of asset sales if we consider it appropriate

[5] Total counterparty exposure includes; financial instruments for investments and risk management instruments.

- contributions from other parties in terms of any contractual arrangements
- renewal loans
- specific revenue streams as determined by us (e.g. repayment of rental housing loans from rental housing income or loan repayment rates).

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

Borrowing limits

Objective
To ensure that our debt is maintained within prudent limits.

Policy parameters
Borrowings will be managed to ensure that the following parameters are not exceeded:

Item	Borrowing limit
Net external debt[6] as a percentage of total revenue[7]	<150%
Net interest[8] on external debt as a percentage of total revenue	<15%
Net interest on external debt as a percentage of annual rates income[9] (debt secured under debenture)	<20%

Debt will be repaid as it falls due in accordance with the applicable loan agreement. Subject to the debt limits, a loan may be rolled over or re-negotiated as and when appropriate. Disaster recovery requirements are to be met through the liquidity ratio amount.

Security arrangements

Objective
To provide appropriate security that does not restrict our operations or limit control of Council community and strategic assets, whilst being sufficiently attractive to lenders to secure competitive borrowing margins, fees, interest rates and terms.

Policy parameters
Council offer security by way of a charge over rates and rates revenue through the 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 2002. From time to time, with Council and Trustee approval, specific security may be offered by providing a charge over one or more of our assets.

Physical assets will be charged only where:

- There is a direct relationship between the debt and the purchase or construction of the asset, which it funds (e.g. an operating lease, or project finance).

[6] Net external debt is defined as total debt less unencumbered cash or cash equivalents.

[7] Revenue is defined as earnings from rates, government grants and subsidies, user charges, interest, dividends, financial and other revenue. Revenue excludes developer contributions and vested assets

[8] Net Interest is defined as the amount equal to all interest and financing costs less interest income for the relevant period.

[9] 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 Government Authorities (LGAs) for services provided and for which the other LGAs rate

- We consider a charge over physical assets to be appropriate.
- Any pledging of physical assets must comply with the terms and conditions contained within the Debenture Trust Deed.

Source of funds

Appropriate sources of funds are specified in the policy. In evaluating strategies for new borrowing (in relation to source, term, size and pricing) we take into consideration the following:

- available terms from the LGFA, banks, brokers, debt capital markets including loan stock issuance
- our overall debt maturity profile, to ensure concentration of debt is avoided at reissue/rollover time
- prevailing interest rates and credit margins relative to the term for loan stock issuance, LGFA, debt capital markets and bank borrowing
- the outlook on LGFA, bank and debt capital market credit margins
- ensuring that the implied finance terms and conditions within the specific debt (e.g. project finance) are evaluated in terms such as cost/risk limitation compared to the terms and conditions we could achieve in our own right
- Legal documentation, security arrangements and financial covenants.

Alternative strategies for new borrowings considered in this evaluation process are documented for review purposes. Our ability to readily attract cost effective borrowing is largely driven by our ability to rate, maintain a strong financial position and manage our relationships with our investors and financial institutions/brokers/LGFA.

Policy review

Objective
To uphold and maintain current Liability Management Policy best practice standards.

Policy parameters
Each external loan will be monitored on a six-monthly basis over the term of the loan, and benchmarked against the other identified options at the time the loan was raised. This will enable Council's performance in the achievement of the objectives set out in this policy to be assessed and reported to Council.

This Policy is to be formally reviewed on an annual basis. The General Manager Business Support, or equivalent, has the responsibility to prepare a review report that is presented to the Council or Council sub-committee. The report will include:

- recommendation as to changes, deletions and additions to the Policy
- overview of the treasury function in achieving the stated treasury objectives, including performance trends in actual borrowing cost against budget (multi-year comparisons), and interest rate management instruments against benchmarks.
- summary of breaches of policy and one-off approvals outside policy to highlight areas of policy tension
- analysis of bank lender service provision, share of financial instrument transactions etc.
- comments and recommendations from our external auditors on the treasury function, particularly internal controls, accounting treatment and reporting
- an audit of the treasury system/spreadsheets and procedures should be undertaken
- adherence to borrowing limits specified in the covenants of bank lenders to Council

The Council receives the report, approve policy changes and/or rejects recommendations for policy changes.

Statutory matters

- All borrowing, investments and incidental financial arrangements (e.g. use of interest rate hedging financial instruments) will meet requirements of the Local Government Act 2002, and incorporate the Liability Management Policy and Investment Policy.
- We do not borrow in foreign currency in terms of section 113 of the Local Government Act 2002.
- We also ensure we are consistent with the Local Government (Financial Reporting and Prudence) Regulations 2014 and in particular, Schedule 4.
- All projected borrowings are to be approved as part of the Annual Plan process or resolution of Council before the borrowing is affected.
- All legal documentation in respect to borrowing, investments and financial instruments will be approved by our solicitors prior to the transaction being executed.
- We will not transact with any Council Controlled Trading Organisation (CCTO) on terms more favourable than those achievable by Council itself.
- A resolution of Council is not required for hire purchase, credit or deferred purchase of goods if:
    - The period of indebtedness is less than 91 days (including rollovers); or
    - The goods or services are obtained in the ordinary course of operations on normal terms for amounts not exceeding in aggregate, an amount determined by resolution of Council.