Liability Management Policy

te kaunihera ā-rohe o
matamata-piako
district council

Our vision is

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

Council's commitment

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:

- Ensure that the following parameters are not exceeded:

Item	Borrowing limit
Net external debt[1] as a percentage of total revenue[2]	<175%
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%
Liquidity: (Liquid investments + external debt + unutilised committed debt facilities) / external debt	>110%

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
    - setting risk control limits on the use of interest rate instruments (under the guidance of independent external advisors) on a portfolio basis

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[1] Net external debt is defined as external debt less liquid financial assets and investments. Liquid financial assets and investments are defined as cash, bank deposits and any fixed interest and equity investments that are held for other than strategic purposes.

[2] Revenue is defined as earnings from rates, government grants and subsidies, user charges, interest, dividends, financial and other revenue. Revenue excludes non-government developer contributions and vested assets (including found assets and the revaluation of derivatives and 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.

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 including:
  - cashflow management and forecasting,
  - maintenance of unutilised committed debt facilities and liquid funds,
  - having risk control limits that enforce spreading of funding maturities,
  - pre-funding of existing and forecast debt requirements,
  - accessing long term debt where available and cost effective, to assist with spreading of term profile of funding risk

Credit exposure

Prudent credit management can reduce Council's risk of loss from a counterparty failing to meet its obligations. Liquidity risk 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. Credit exposure from derivative and other financial contracts relates to the default of the counterparty leading to non-payment of their contractual obligations. To manage these risks, 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 considers 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 and bonds to the LGFA, LGFA stand-by facilities that is secured by the Debenture Trust Deed.

Borrowing mechanisms for Council Controlled Organisations and Council Controlled Trading Organisations.

To better achieve its strategic and commercial objectives, Council may provide financial support in the form of debt funding directly or indirectly to CCO/CCTO's. Indirect lending is where the CCO/CCTO becomes a member of the LGFA and Council provides the financial support.

Council guarantees of financial indebtedness to CCTO's are prohibited, but financial support may be provided by subscribing for shares as called or uncalled capital. Council will not transact with a CCTO on terms more favourable than that of Council, if Council were not providing rates as security.

All lending arrangements must be executed under legal documentation (e.g. loan, guarantee) reviewed by Council's independent legal counsel and approved by Council.

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 on borrowings on at least a quarterly basis.

The Risk and Assurance Committee will:

- Formally review this policy at least every three years in line with the review of the Long Term Plan.

Council will:

- Receive recommendations from the Risk and Assurance Committee and review and adopt this policy at least every three years in line with the review of the Long Term Plan.

A Wilcock
Mayor

D J McLeod
Chief Executive Officer

Version 6
Council resolution date: 24 January 2024

Appendix one

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

Forecast gross core external debt is the amount of total core external debt that is expected to remain outstanding for a period greater than one year. When approved forecasts are changed (signed off by the Group Manager Business Support or equivalent), the amount of interest rate fixing in place may have to be adjusted to ensure compliance with the policy minimum and maximum limits.

The Group Manager Business Support can consider and approve alternative debt forecast scenarios that make assumptions around such matters as, the delivery and timing of the capital expenditure programme when designing the interest rate hedging strategy. **However, the interest rate risk position is measured and reported against the base debt forecast approved by the Group Manager Business Support.**

Exposure to interest rate risk is managed and mitigated through the risk control limits below. Council's forecast gross core external debt should be within the following fixed/floating interest rate risk control limits.

Debt interest rate policy parameters (calculated on a rolling monthly basis)

Debt period ending	Minimum fixed	Maximum fixed
Current	40%	90%
Year 1	40%	90%
Year 2	35%	85%
Year 3	30%	80%
Year 4	25%	75%
Year 5	20%	70%
Year 6	0%	65%
Year 7	0%	60%
Year 8	0%	50%
Year 9	0%	50%
Year 10	0%	50%
Year 11 plus	0%	25%

A fixed rate maturity profile that is outside the above limits, but 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 all known interest rate obligations on forecast gross external debt, including where hedging instruments have fixed movements in the applicable reset rate.

“Floating Rate” is defined as any interest rate obligation subject to movements in the applicable reset rate.

Pre-hedging in advance of projected physical drawdowns of new debt is allowed.

Fixed interest rate percentages are calculated based on the average amount of fixed interest rate obligations relative to the average forecast gross core external debt amounts for the given period (as defined in the table above).

Interest rate risk management instruments may be used to convert fixed rate borrowing into floating rate, floating rate borrowing into fixed or hedged borrowing. Independent external advisors will be consulted when using interest rate risk management products.

The following instruments may be used and are approved 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 the maximum LGFA bond maturity 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 36 months, unless the start date of the new swap coincides with the maturity date of an 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.

Interest rate instruments are only sought from strongly credit rated New Zealand registered banks. Banks must have a minimum long term credit rating of single "A" (Standard & Poor's', Fitch, or Moody's).

Liquidity/Funding

Objective

To ensure that we have adequate committed financial resources to meet all 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. External borrowing is sought from the LGFA and bank facilities.

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 and/or with the LGFA.
- Maintaining financial investments in liquid instruments counterparties within credit risk limits.
- Liquid investments, available committed bank/loan facilities and external debt are maintained at greater than 110% over the existing external debt amount.
- Maintaining 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 18 months of forecast debt requirements including debt re-financing and pre-funded capital expenditure.

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%	60%
3 to 7 years	25%	85%
7 years plus	0%	60%

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.

Once debt has been refinanced with a contracted term deposit (pre-funded), the term deposit amount will net off the maturing debt instrument from the funding maturity profile percentage calculation.

To minimise concentration risk, the LGFA require that no more than the greater of NZD 100 million or 33% of a council's borrowings from the LGFA will mature in any 12 month period.

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

- Overnight bank, call deposits at 100% of principal amount
- Bank term deposits no greater than 30 days at 100% of principal amount
- Bank registered certificates of deposit (RCD's) maturing in less than 181 days at 100% prevailing market value

Borrowing Mechanisms for CCO and CCTO organisations

Any debt funding arrangement directly or indirectly to a CCO/CCTO must be approved by Council. In recommending an arrangement for approval the following is considered:

- Credit risk profile of the borrowing entity, and the ability to repay interest and principal amount outstanding on due date
- Impact on Council's credit standing, debt cap amount (where applied), lending covenants with the LGFA and other lenders and Council's future borrowing capacity.
- The form and quality of security arrangements provided
- The lending rate, given factors such as: CCO or CCTO credit profile, external Council borrowing rates, borrower note and liquidity buffer requirements, term etc
- Lending arrangements to CCO/CCTO must be documented on a commercial arm's length basis. A term sheet, including matters such as borrowing costs, interest payment dates, principal payment dates, security and expiry date is agreed between the parties
- Accounting and taxation impact of on-lending arrangements.

All lending arrangements must be executed under legal documentation (e.g. loan, guarantee) reviewed by Council's independent legal counsel and approved by Council.

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 counterparties to borrowing transactions will be assessed to ensure that there is reasonable certainty that obligations under borrowing facilities 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 & Poor's', or equivalent Fitch or Moody's) and/or a short-term credit rating of A-1 or above.

In conjunction with the Investment Policy, positions should be spread amongst a number of counterparties to avoid concentrations of credit exposure. The following matrix guide will determine limits:

Counterparty	Minimum long term credit rating	Total maximum per counterparty ($m)[5]
NZ Government	N/A	Unlimited
NZ Local Government Funding Agency (LGFA)	AA-	Unlimited
NZ Registered Bank	A	15.0

Note these limits are a total across both the Investment Policy and Liability Management Policy and are not cumulative.

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%.

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

Debt repayment

Objective

To ensure that we can 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
- 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]	<175%
Net interest[8] on external debt as a percentage of total revenue	<15%

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6 Net external debt is defined as external debt less liquid financial assets and investments. Liquid financial assets and investments are defined as cash, bank deposits and any fixed interest and equity investments that are held for other than strategic purposes.

7 Revenue is defined as earnings from rates, government grants and subsidies, user charges, interest, dividends, financial and other revenue. Revenue excludes non-government developer contributions and vested assets (including the revaluation of derivatives and assets).

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

Net interest on external debt as a percentage of annual rates income[9] (debt secured under debenture)	<20%
Liquidity: (Liquid investments + external debt + unutilised committed debt facilities) / external debt	>110%

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 offers 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).
- 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 liquidity and terms on offer by the LGFA and banks

[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.

- our overall debt maturity profile, to ensure concentration of debt is avoided at reissue/rollover time
- the outlook on LGFA and bank 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 financial institutions/LGFA.

Policy review

Objective

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

Policy parameters

Each external loan will be monitored on an annual 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, approves 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.