

Ku-ring-gai Council

Policy

Investment Policy

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1	28/08/07	20/04/10	Manager Finance	Original
2	21/04/2010	09/12/2013	Manager Finance	Revision following Ministerial Order 31/07/8 & DLG draft Guidelines 2009
3	10/12/2013	07/02/2017	Manager Finance	Revised Minister's Order and updated risk / governance

1. Purpose

The purpose of this document is to establish the framework within which investment principles are to apply to the investment of Council funds. It details:

- Council Funds covered by this Investment Policy Statement;
- Council's objectives for its investment portfolio/s;
- how investments are to be undertaken;
- the applicable risks to be managed;
- any constraints and other prudential requirements to apply to the investments of Funds having regard to the applicable legislation and regulations governing Council investment;
- the manner in which compliance with the Policy will be monitored and reported;
- appropriate benchmarks for each category of investments.

2. Objectives

The purpose of this Policy is to provide a framework for the optimum investment of Ku-ring-gai Council's Funds at the most favourable rate of interest available to it at the time to maximise returns, whilst having due consideration of risk tolerance, liquidity and security for its investments.

While exercising the power to invest, consideration is to be given to the preservation of capital, liquidity and the return of investment. Council therefore has several primary objectives for its investment portfolio:

- Compliance with legislation, regulations, the prudent person tests of the Trustee Act and best practice guidelines;
- The preservation of the amount invested;
- To ensure there is sufficient liquid funds to meet all reasonably anticipated cash flow requirements; and
- To generate income from the investment that exceeds the performance benchmarks mentioned later in this document.

3. Legislative Framework

All Council investments are to comply with the following:

- Local Government Act (1993);
- Local Government (General) Regulation (2005);
- Ministerial Investment Order dated 12/01/2011, and its successors;
- The Trustee Amendment (Discretionary Investments) Act (1997) – s14;
- Local Government Code of Accounting Practice and Financial Reporting;
- Australian Accounting Standards;
- Office of Local Government Investment Policy Guidelines; and
- Office of Local Government Circulars

4. Principles

4.1 Authorised Investments

All investments must be denominated in Australian Dollars.

Authorised Investments are limited to those allowed by the Ministerial Investment Order as follows:

- Commonwealth / State / Territory Government securities e.g. bonds;
- Interest bearing deposits / senior securities issued by an eligible ADI;
- Bills of Exchange (no more than 200 days duration) guaranteed by an ADI;
- Debentures issued by a NSW Council under Local Government Act (1993);
- Deposits with T-Corp &/or Investments in T-Corp Hour-Glass Funds; and

4.2 Prohibited Investments

While Council may only invest in the above types of investment, for clarity, this investment policy prohibits the following types of new investment :

- Derivative based instruments;
- Principal only investments or securities that provide potentially nil or negative cash flow; and
- Stand-alone securities issued that have underlying futures, options, forwards contracts and swaps of any kind.
- Other investments excluded by the Ministerial Investment Order.

This policy also prohibits the use of leveraging (borrowing to invest) of an investment. However, nothing in the policy shall prohibit the short-term investment of loan proceeds where the loan is raised for non-investment purposes and there is a delay prior to the expenditure of loan funds.

Exclusion of an investment by replacement regulation would not normally require divestment unless specifically directed. Generally, existing holdings are grandfathered, and nothing in this Policy is intended to imply a presumption of divestiture. However, in such cases it is appropriate to formally review the investments affected, and formulate a strategic approach to maximising their value. The decision on when to exit such investments are based on a range of criteria specific to the investments – including but not limited to factors such as:

- Returns expected over the remaining term
- Fair values
- Competing investment opportunities
- Costs of holding
- Liquidity and transaction costs
- Outlook for future investment values

Professional advice will be sought before transacting in “grandfathered investments”. The overriding principle used in dealing with grandfathered assets is maximising public interest (having regard to risk of the assets).

4.3 Risk Management Guidelines

Investments obtained are to be considered in light of the following key criteria:

Preservation of Capital	The requirement for preventing losses in an investment portfolio's total value.
Credit Risk	The risk that a party or guarantor to a transaction will fail to fulfil its obligations. In the context of this document it relates to the risk of loss due to the failure of an institution/entity with which an investment is held to pay the interest and/or repay the principal of an investment.
Diversification	The requirement to place investments in a broad range of products so as not to be over exposed to a particular sector of the investment market.
Liquidity Risk	The risk an institution runs out of cash, is unable to redeem investments at a fair price within a timely period, and thereby Council incurs additional costs (or in the worst case is unable to execute its spending plans).
Market Risk	The risk that fair value or future cash flows will fluctuate due to changes in market prices, or benchmark returns will unexpectedly overtake the investment's return.
Maturity Risk	The risk relating to the length of term to maturity of the investment. The longer the term, the greater the length of exposure and risk to market volatilities.
Interest Risk	The risk that income will not meet expectations or budgeted requirement because interest rates are lower than expected in future

4.4 Credit Ratings

The portfolio credit guidelines to be adopted will primarily reference the Standard & Poor's (S&P) ratings system criteria and format - however, references in previous Minister's Orders also recognises Moody's and Fitch Ratings, and these may be used where an S&P rating is not available.

However, the primary control of credit quality is the prudential supervision and government support and explicit guarantees of the ADI sector, not ratings.

The maximum holding limit in each rating category (based on the investment's own rating, where different to the issuer's) for Council's portfolio shall be:

Long-Term S&P Rating Range	Maximum Holdings
AAA category	100%
AA Category or Top Level bank*	100%
A Category	70%
BBB Category	25%
Lower, and Unrated^	10%

*For the purposes of this Policy, "Top Level Banks" are currently defined as:

The Approved Deposit Institution (ADI) deposit or senior guaranteed principal and interest ADI securities issued by the major Australian Banking Groups:

- *Australia and New Zealand Banking Group Limited*
- *Commonwealth Bank of Australia*
- *National Australia Bank Limited*
- *Westpac Banking Corporation*

including ADI subsidiaries (such as BankWest) whether or not explicitly guaranteed, and brands (such as St George).

^ The lower and unrated ADIs represents the banks, credit unions and building societies that are regulated by Australia’s banking regulator, the Australian Prudential Regulation Authority (APRA), consistent with the higher rated ADIs. These ADIs are officially “not rated” by the ratings agencies as they are relatively small (asset size). Despite not having an official credit rating, they generally remain financially solid and tend to hold higher levels of capital adequacy compared to the higher rated ADIs. Overall, they are not speculative institutions and are not associated as being high risk, particularly for the purposes of Council’s investments, which would predominately only be invested in short-dated fixed term deposits amongst these ADIs.

4.5 General Policy Guidelines

(A) Counterparty Limits

Exposure to individual counterparties/financial institutions will be restricted by their rating so that single entity exposure is limited, as detailed in the table below. It excludes any government guaranteed investments.

Individual Institution or Counterparty Limits	
Long Term S&P Rating Range	Limit
AAA Category ¹	40%
AA Category or Top Level bank*	30%
A Category	20%
BBB Category	10%
Lower, and Unrated ²	3%

(B) Accounting for Investments

Council will comply with appropriate accounting standards in valuing its investments and quantifying its investment returns.

In addition to recording investment income according to accounting standards, published reports may show a break-down of its duly calculated investment returns into realised and unrealised capital gains and losses, and interest.

Other relevant issues will be considered in line with relevant Australian Accounting Standards, such as discount or premium, designation as held-to-maturity or on a fair value basis and impairment (AASB136).

¹ 100% Commonwealth Government and Government-guaranteed deposits are included in this category, but without any upper limit applying to the government as counterparty. TCorp Hour-glass Cash is treated as AAA Category, with TCorp as the notional counterparty

² This category includes unrated ADI’s such as some Banks, Credit Unions and Building Societies to the extent not Commonwealth-guaranteed.

(C) Safe Custody Arrangements

Where necessary, investments may be held in safe custody on Council's behalf, as long as the following criteria are met:

- Council must retain beneficial ownership of all investments;
- Adequate documentation is provided, verifying the existence of the investments at inception, in regular statements and for audit;
- The Custodian conducts regular reconciliation of records with relevant registries and/or clearing systems; and
- The Institution or Custodian recording and holding the assets will be:
 - The Custodian nominated by TCorp for Hour-Glass facilities;
 - Austraclear;
 - An institution with an investment grade Standard and Poor's, Moody's or Fitch rating; or
 - An institution with adequate insurance, including professional indemnity insurance and other insurances considered prudent and appropriate to cover its liabilities under any agreement.
- Council's assets must be entirely separate, and not be mingled with the assets of the advisor or any other counterparty in a sub-account.
- Council will have regard to costs and other consequences of any arrangements.

(D) Performance Benchmarks

The performance of each investment will be assessed against the benchmarks listed in the table below.

It is Council's expectation that the performance of each investment will be greater than or equal to the applicable benchmark by sufficient margin to justify the investment taking into account its risks, liquidity and other benefits of the investment.

It is also expected that Council will take due steps to ensure that any investment is executed at the best pricing reasonably possible.

Investment	Performance Benchmark	Time Horizon
At-Call Account, short dated bills, deposits issued by financial institutions of appropriate term.	AusBond Bank Bill Index (BBI)	Working Capital 3 months or less
Term Deposits of appropriate remaining term, FRN's nearing maturity.	AusBond Bank Bill Index (BBI)	Short Up to 1 year
FRN's, Bonds, Term deposits with a maturity date beyond the financial year and up to 4 Years.	AusBond Bank Bill Index (BBI)	Medium 1+ Years
T-Corp Hour Glass Managed Funds	Fund's Benchmark Internal	3 Years (M/T Growth) 4+ Years (L/T Growth)

(E) Investment time frame

Council's investment portfolio shall be structured around the time horizon of investment to ensure that liquidity and income requirements are met.

Once the primary aim of liquidity is met, Council will ordinarily diversify its maturity profile as this will ordinarily be a low-risk method of obtaining additional return as well as reducing the risks to Council's income. However, Council always retains the flexibility to invest as short as required by internal requirements or the economic outlook.

The factors and/or information used by Council to determine minimum allocations to the shorter durations include:

- Council's liquidity requirements to cover both regular payments as well as sufficient buffer to cover reasonably foreseeable contingencies;
- Medium term financial plans and major capex forecasts;
- Known grants, asset sales or similar one-off inflows;
- Seasonal patterns to Council's investment balances.

Investment Description	Horizon	Investment Horizon - Maturity Date	Maximum Allocation
Working capital funds		0-3 months	100%
Short term funds		0-12 months	100%
Short-Medium term funds	term	13-24 months	70%
Medium term funds		25-48 months	50%
Long term funds		49-120 months	25%

Within these broad ranges, Council relies upon assumptions of expected investment returns and market conditions that have been examined with its investment advisor.

Investments can be made for longer durations to the extent that Council expects net portfolio drawdowns over the horizon will not result in those funds being required. This is based on the current term remaining, or the horizon of funds.

Investments that will not be drawn during the 4 year Delivery Program & Operational Plan can be allocated to long-term assets.

Council can at any time invest shorter than the projected drawdowns in the Delivery Program & Operational Plan – due to reasons of prudence, market conditions, relative value or availability of assets.

(F) Reporting

Documentary evidence must be held for each investment and details thereof maintained in an investment register. The documentary evidence must provide Council legal title to the investment.

For audit purposes, certificates must be obtained from the banks/fund managers/custodian confirming the amounts of investment held on Council's behalf at 30th June each year.

All investments are to be appropriately recorded in Council's financial records and reconciled at least on a monthly basis.

A monthly report will be provided to Council.

The report will detail the investment portfolio in terms of holdings and impact of changes in market value since the previous report – including investments divested during the financial year. However, reporting market values can be for information purpose only – it does not preclude use of a held-to-maturity accounting treatment where permitted by AASB139.

The monthly report will also detail the investment performance against the applicable benchmark, investment income earned versus budget year to date and confirm compliance of Council's investments within legislative and policy limits.

Council may nominate additional content for reporting.

(G) Delegations and Variation to Policy

Authority for implementation of the Investment Policy is delegated by Council to the General Manager in accordance with the *Local Government Act (1993)*.

The General Manager has in turn delegated the Director Corporate and the Manager Finance to make Council's investment decisions who must ensure adequate skill, support and oversight is exercised in the investment of Council funds.

Officers' delegated authority to manage Council's investments shall be recorded and they are required to acknowledge they have received a copy of this policy and understand their obligations in this role.

(H) Prudent Person Standard

The investments will be managed with the care, diligence and skill that a prudent person would exercise. As trustees of public monies, officers are to manage Council's investment portfolios to safeguard the portfolio in accordance with the spirit of this Investment Policy and not for speculative purposes.

(I) Ethics and Conflicts of Interest

Officers shall refrain from personal activities that would conflict with the proper execution and management of Council's investment portfolio. This policy requires officers to disclose any conflict of interest to the General Manager.

Independent advisors are also to declare that they have no actual or perceived conflicts of interest and receive no inducements in relation to Council's investments.

(J) Independent Advice

Council's investment advisor is appointed by Council and must be licensed by the Australian Securities and Investment Commission – the role shall not extend beyond advice to a discretionary or dealing mandate. The advisor must be independent and must confirm in writing that they have no actual or potential conflict of interest in relation to investment products being recommended and is free to choose the most appropriate product within the terms and conditions of investment policy.

This includes receiving no commissions or other benefits in relation to the investments being recommended or reviewed, and having no involvement in the structuring or distribution. All remuneration received from investments must be rebated to Council in full.

5. Accountabilities

The General Manager, Director Corporate and Manager Finance have authority to invest surplus funds.

Officers are to exercise the care, diligence and skill that a prudent person would exercise in investing Council funds.

6. Associated Documents and Information

- The Code of Accounting Practice and Financial Reporting
- <http://www.apra.gov.au> - current list of ADIs

7. Review of Policy

The Investment Policy will be reviewed every second year and as required in the event of legislative change or as a result of significantly changed economic/market conditions.

Any proposed amendment to the Investment Policy must be approved by Council.

8. Definitions

Term / Abbreviation	Definition
Act	<i>Local Government Act, 1993.</i>
ADI	Authorised Deposit-Taking Institutions (ADIs) are corporations that are authorised under the <i>Banking Act 1959 (C'wlth)</i> to take deposits from customers
Bill of Exchange	A bill of exchange is an unconditional order in writing, addressed by one person to another, signed by the person giving it, requiring the person to whom it is addressed to pay on demand, or at a fixed or determinable future time, a sum certain in money to or to the order of a specified person, or to bearer.
BBSW	The Bank Bill Swap reference rate (BBSW) is the average of mid-rate bank-bill quote from brokers on the BBSW Panel. The BBSW is calculated daily. Floating rate securities are most commonly reset quarterly to the 90-day BBSW.
Council Funds	Surplus monies that are invested by Council in accordance with section 625 of the Act.
Debenture	A debenture is a document evidencing an acknowledgement of a debt, which a company has created for the purposes of raising capital. Debentures are issued by companies in return for medium and long-term investment of funds by lenders.
OLG	NSW Office of Local Government and its predecessors.
FRN	A Floating Rate Note (FRN) is a medium to long term fixed interest investment where the coupon is a fixed margin ("coupon margin") over a benchmark, also described as a "floating rate". The benchmark is usually the BBSW and is reset at regular intervals – most commonly quarterly.
LGGR	<i>Local Government (General) Regulation 2005 (NSW).</i>
NCD	Is a short term investment in an underlying security being a negotiable certificate of deposit (NCD) where the term of the security is usually for a period of 185 days or less (sometimes up to 2 years). NCDs are often discount securities, meaning they are issued and on-sold to investors at a discount to their face value.
ROA	Responsible Accounting Officer of a council means a member of the staff of the council designated by the General Manager. (LGGR, clause 196)
T-Corp	New South Wales Treasury Corporation.
AusBond BBI	Formerly the UBS Bank Bill Index (BBI). The UBS Australia index family was acquired by Bloomberg from Q3 2014, and while branding changed the benchmark is unaltered. The Bank Bill Index represents the performance of a notional rolling parcel of bills averaging 45 days and is the widely used benchmark for local councils and other institutional cash investments