3.04 – INVESTMENT POLICY

1 INTRODUCTION

The purpose of this policy is to provide a framework for the investment of Council funds to maximise returns with due consideration of the risk and security of the investment; and liquidity requirements.

2 POLICY OBJECTIVE

Investments shall be allocated to ensure there is sufficient liquidity to meet all reasonably anticipated cash-flow requirements, as and when they fall due, taking into account the need to achieve best investment returns through management of credit and interest risks within agreed investment frameworks.

3 POLICY SCOPE

This policy applies to all Council Officers who have authority delegated to them to invest surplus funds on Council's behalf and is in accordance with the legislation and guidelines listed in part 5, Legal and Policy Framework.

4 DEFINITIONS

The Act	*Local Government Act 1993* (NSW) (NI)
Regulations	Local Government (General) Regulations 2005 (NSW) (NI)

5 LEGAL AND POLICY FRAMEWORK

- *Local Government Act 1993* (NSW)(NI), section 625
- *Local Government (General) Regulation 2005*, Clause 16
- Ministerial Investment Order 2011
- *Trustee Act 1925*, section 14
- Local Government Code of Accounting Practice and Financial Reporting
- Australian Accounting Standards
- NSW Division of Local Government Investment Policy Guidelines 2010
- NSW Division of Local Government Circulars

6 IMPLEMENTATION

6.2 Communication

This policy is to be communicated to all staff and the community via the Council's website.

6.3 Associated Documents

Bloomberg AusBond Indices

7 POLICY

7.1 Prudent Person Standard

The delegated officers will ensure that Council investments are managed with the care, diligence and skill expected of a qualified accountant. As trustees of public monies, officers are to safeguard the portfolio in accordance with the intent of this Investment Policy.

7.2 Ethics and Conflicts of Interest

Council's Code of Conduct provides guidance for recognising and disclosing any conflicts of interest in the execution and management of Council's investments.

7.3 Approved Instruments

Norfolk Island Regional Council approves the following investments included in the Ministerial Investment Order:

- any public funds or securities issued by or guaranteed by, the Commonwealth, any State of the Commonwealth or a Territory;
- any debentures or securities issued by a council (within the meaning of the *Local Government Act 1993* (NSW) (NI))
- interest-bearing deposits with, or any debentures or bonds issued by, an authorised deposit-taking institution (as defined in the *Banking Act 1959* (Cwth)), but excluding subordinated debt obligations
- a deposit with the New South Wales Treasury Corporation or investments in an Hour-Glass investment facility of the New South Wales Treasury Corporation;
- debt securities issued by Authorised Deposit-taking Institutions.

All investment instruments (excluding short-term discount instruments) referred to above include both principal and investment income and must be denominated in Australian dollars.

7.4 Prohibited Instruments

In accordance with the Ministerial Investment Order, this Investment Policy prohibits any high-risk investment including:

- derivative based instruments;
- principal only investments or securities that provide potentially nil or negative cash flow;
- stand-alone securities issued that have underlying futures, options, forward contracts or swaps of any kind;
- the use of leveraging (borrowing to invest) for an investment.

7.5 Risk Management Guidelines

All investments entail some risk. Generally, the higher the anticipated rate of return of an investment, the higher the risk and variability of investment returns. Investing should produce a diversified portfolio that reflects reasonable market rates of return.

This Investment Policy states a conservative, risk-adverse investment profile and recognises that Council has a low-risk tolerance for investments that would result in loss of funds, capital or returns.

The nature of a conservative approach to investments recognises that the expectation of returns on investments would also need to be conservative. A risk-adverse investment policy acts to preserve capital, but also affects the contribution of earnings from investments and the growth in value of the investment portfolio. This approach accepts that Council's return on investment could be lower than average market expectations, particularly where average market expectations are based on rates of returns of risk-diversified portfolios.

One of the key objectives of this Investment Policy is to provide guidance on risk minimisation.

The following discussion provides a background, but not an exhaustive list, of risk exposures to be considered when managing Council's investment portfolio:

- Market Risk – One of the most prominent exposures recognised by local governments is the exposure to market risk. The risk exposure results from a change in market prices, which includes changes in interest rates, currency and other prices. As hedging market risk is not available to councils, this risk is mitigated by fixed-rate instruments.
- Liquidity Risk – Liquidity risk usually arises if there is a lack of market depth, or the number of potential willing buyers and sellers that can influence the price of the investment. The mitigation of this risk is to only deal with standard investments in a well-traded market.
- Maturity Risk – Maturity risk identifies the impact of maturity on the valuation of the investment. The longer the term to maturity of an investment, the greater the length of exposure to market risks for the investment. This risk is mitigated by consideration of the term to maturity on the risk exposure to an investment.
- Leveraging Risk – Leverage, or borrowings, increases the potential returns of an investment, but also increases the potential loss. Leverage risk usually arises through investment in structured products or derivatives, which can potentially be used to create leveraged positions where the exposures obtained are greater than the value of the assets required to support them. Councils are prohibited from investing in structured products or derivatives, other than those grandfathered by Order of the Minister.
- Credit Risk – Credit risk is the risk of loss to an investor due to the failure of the institution/entity to pay the interest and/or repay the principal of an investment. This risk is mitigated by Council complying with the Order of the Minister on investments, Circulars, regulatory and statutory requirements.
- Interest Rate Risk – Interest rate risk is a sub-set of Market Risk and is the risk that the fair value or future cash flows of an investment will fluctuate because of changes in market interest rates. This risk is mitigated by investing in fixed rate instruments.

7.6 Credit and Maturity Guidelines

Investments are to comply with three key criteria relating to:

1. Overall Portfolio Credit Framework: limit overall credit exposure of the portfolio.
2. Institutional Credit Framework: limit exposure to individual institutions based on their credit ratings.
3. Term-to-Maturity Framework: limits based upon maturity of securities.

7.7 Overall Portfolio Credit Framework

To control the credit quality on the entire portfolio, the following credit framework limits the percentage of the portfolio exposed to any particular credit rating category.

S&P Long Term Credit Ratings	Moody's Equivalent	Maximum
AAA Category	Aaa	100%
AA Category	Aa1 to Aa3	100%
A Category	A1 to A3	60%
BBB Category	Baa1 to Baa3	30%

7.8 Institutional Credit Framework

Exposure to an individual institution will be restricted by their credit rating so that single entity exposure is limited, as detailed in the table below:

S&P Long Term Credit Ratings	Moody's Equivalent	Maximum
AAA Category	Aaa	65%
AA Category	Aa1 to Aa3	60%
A Category	A1 to A3	15%
BBB Category	Baa1 to Baa3	10%

Where the investment is with a 100 per cent Commonwealth government or government guarantee deposit then no upper limit shall apply to the counterparty.

In the event that a financial institution is a 100 per cent subsidiary of another, their combined investments will be totalled to confirm that the individual institution limit of the parent is not exceeded.

7.9 Term to Maturity Framework

The investment portfolio is to be invested within the following maturity constraints:

Overall Portfolio Term to Maturity Limits		
Portfolio % ≤ 1 Year	40% Min	100% Max
Portfolio % >1 Year ≤ 3 Year	0% Min	60% Max
Portfolio % >3 Year ≤ 5 Year	0% Min	25% Max

In this event, or in the event of changes in policy, or any other event that impacts policy limits such as ownership changes, grandfathering of investments is allowable subject to assessment and decision. (Grandfathering refers to existing investments being retained till maturity.)

7.10 Credit Ratings

Standard & Poors (S&P) and Moody's are professional organisations that provide analytical services. The following is as identified by S&P on their own website. An S&P rating is an opinion of the general credit worthiness of an obligor with respect to particular debt security or other financial obligation – based on relevant risk factors.

Credit ratings are based, in varying degrees, on the following considerations:

- likelihood of payment
- nature and provision of the obligation
- protection afforded by, and relative position of, the obligation in the event of bankruptcy, reorganisation or other laws affecting creditors' rights.

The ratings below consider the risk of default.

Long-Term Obligation ratings are:

AAA: An obligation/obligor rated AAA has the highest rating assigned by S&P. The obligor's capacity to meet its financial commitment on the obligation is extremely strong.

AA: An obligation/obligor rated AA differs from the highest rated obligations only in a small degree. The obligor's capacity to meet its financial commitment on the obligations is very strong.

A: An obligation/obligor rated A is somewhat more susceptible to the adverse effects of changes in circumstances and economic conditions than obligations/obligor in higher rated categories. However, the obligor's capacity to meet its financial commitment on the obligation is still strong.

BBB: An obligation/obligor rated BBB exhibits adequate protection parameters. However, adverse economic conditions or changing circumstances are more likely to lead to a weakened capacity to the obligor to meet its financial commitment on the obligation.

Unrated: Most Credit Unions and Building Societies fall into this category and do not necessarily require a credit rating from agencies such as S&P. They must still adhere to capital maintenance requirements of the Australian Prudential Regulatory Authority (APRA) in line with all Authorised Deposit Taking Institutions (Banks, Building Societies and Credit Unions).

Plus (+) or Minus (-): The ratings from 'AA' to 'BBB' may be modified by the addition of a plus or minus sign to show relative standing within the major rating categories.

Ratings will be reviewed at least annually. Where Council becomes aware of changes outside this annual review these changes will also be included.

In the event of a rating agency regrade event, which results in investments outside policy limits, an assessment will be made by Council staff, with a recommendation made to Council as soon as practicable.

7.11 Benchmarking

As Council traditionally invests in short-term deposits, the performance benchmark to be used is the annualised Bloomberg AusBond Bank Bill Index.

7.12 Legal Title

All investments made by Council must clearly demonstrate that the investment has been made in the name of Norfolk Island Regional Council. Where tradeable securities such as floating rate notes or fixed-rate bonds are purchased, these should be held directly in the name of the Council via the Austraclear system or via a single reputable custodian.

7.13 Investment Advisor

Should the Council deem it necessary to consult an investment advisor, the investment advisor must be approved by Council and licensed by the Australian Securities and Investment Commission. The advisor must be an independent person who has no actual or potential conflict of interest in relation to the investment products being recommended and is free to choose the most appropriate product within the terms and conditions of the investment policy.

7.14 Reporting and Reviewing of Investments

Documentary evidence must be held for each investment and details thereof maintained in the Investment register.

Details to be included in the Investment Register:

- the amount of money invested;
- particulars of the security or form of investment in which the money is invested;
- the term of the investment; and
- the rate of interest to be paid, and the amount of money that Council has earned, in respect of the investment.

The documentary evidence must provide Council legal title to the investment. Custody service providers must have an approved safe custody agreement.

Certificates must be obtained from the financial institutions confirming the amounts of investments held on the Council's behalf as at 30 June each year and reconciled to the Investment Register.

All investments are to be appropriately recorded in Council's financial records and reconciled at least monthly. Where marketable securities are purchased the Council should obtain monthly valuations.

Council will be provided with a written report each month setting out details of the entire investment portfolio and its performance. The report will confirm compliance of Council's investments with legislative and policy requirements. The contents of these reports will be used as the basis for preparing Note 3-c of the annual financial statements.

7.15 Responsibilities and Authorities

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

The General Manager has delegated the day-to-day management of Council's investment to the Responsible Accounting Officer (RAO) and senior staff.

The Responsible Accounting Officer is responsible for:

- the keeping of Council's accounting records and keeping them up to date
- providing a report to Council each month detailing the money that Council has invested along with a certificate stating whether the investments have been made in accordance with the Act, the Regulations and Council's Investment policy.

The Chief Financial Officer is responsible and accountable for:

- monitoring compliance of this policy
- ensuring this policy is reviewed and updated to meet external compliance
- implementing and communicating this policy.

The placing of investments must be authorised by a minimum of two Council officers, with at least one authorising officer from Group 1:

Group 1	**Group 2**
General Manager	Financial / Management Accountant
Chief Financial Officer	Finance Team Leader
Group Manager Services	Finance Officer

8 REVIEW AND VERSION CONTROL

Policy Number	3.04		Responsible Officer	Group Manager Corporate / CFO
Effective Date			Next Review Date	2020
Version Number	**Version**	**Resolution No.**	**Effective Date**	**Version description**
	V1	2016/133	21 December 2016	Developed and Adopted
	V2	2018/17	21 February 2018	Reviewed and Adopted
	V3	2019/19	20 February 2019	Reviewed and Adopted