

# Investment of Available Funds Policy

## City Policy

### Responsible Directorate: Corporate Services

**Objective:** To invest the City's surplus funds, with consideration of risk at the most favourable rate of interest available to it at the time, for that investment type, while ensuring that its liquidity requirements are met.

#### 1. Definitions:

**“Authorised Institution”** means the same as that defined in Regulation 19C (1) of the Local Government (Financial Management) Regulations 1996 as amended.

**“Counterparty”** means the other party that participates in a financial transaction.

**“Credit Rating”** means an estimate of overall ability and willingness of an entity or person to fulfil financial obligations in full and on time, based on previous financial dealings. Ratings are opinions issued by credit rating agencies.

**“Short-term”** in relation to investments means it matures in 12 months or less.

**“Long term”** in relation to investments means it matures in excess of 12 months.

#### 2. Statement:

While exercising the power to invest, consideration needs to be given to preservation of capital, liquidity, and the return on investment.

- a. Preservation of capital is the principal objective of the investment portfolio. Investing activities are to be performed in a manner that seeks to ensure the security and safeguarding of the investment portfolio. This includes managing credit and interest rate risk within specified limits and parameters.
- b. The investment portfolio will ensure there is sufficient liquidity to meet all reasonably anticipated cash flow requirements, as and when they fall due, without incurring significant costs due to the unanticipated realisation of an investment.
- c. The investment portfolio is expected to achieve a predetermined market average rate of return that takes into account legislative investment limitations. Any additional return target set by Council must also consider risk limitations, liquidity requirements and prudent investment principles.

### **3. Details:**

#### **3.1. Legislative Requirements:**

All investments are to comply with the following:

- Local Government Act 1995 – Section 6.14;
- The Trustees Act 1962 – Part III Investments;
- Local Government (Financial Management) Regulations 1996 – Regulations 19, 19C, Regulation 28 and Regulation 49;
- Australian Accounting Standards.

#### **3.2. Delegation of Authority to Invest:**

Authority is delegated to the Chief Executive Officer to implement this policy. The Chief Executive Officer may in turn delegate the day-to-day management of the City's investments in accordance with the provisions of the *Local Government Act 1995*.

#### **3.3. Prudent Person Standard:**

Investments will be managed with the care, diligence and skill that a prudent person would exercise. Officers delegated with authority to manage investments are to safeguard the portfolios in accordance with the substance of this policy, and not for speculative or any other purposes.

#### **3.4. Approved Investments:**

Unless otherwise approved by Council, investments are limited to:

- State/Commonwealth Government Bonds maturing within three years;
- Interest bearing deposits up to 3 years with Authorised Deposit-taking Institutions (ADI);
- Bank accepted/endorsed commercial bills payable within 12 months;
- Negotiable Certificates of Deposit issued or guaranteed by an Authorised Institution.

#### **3.5. Prohibited Investments:**

This investment of available funds policy prohibits any investment carried out for speculative purposes including but not limited to:

- Derivative or derivative based instruments and/or Structured Products;
- Principal-only investments or securities that provide potentially nil or negative cash flow;
- Stand-alone securities issued that have underlying futures, options, forwards contracts and swaps of any kind; and
- Any form of investment that risks the loss of the initial capital outlay in anticipation of significant gain that may arise from expected changes in future economic conditions.

This policy also prohibits the use of leveraging (borrowing to invest) of an investment.

**3.6. Risk Management Guidelines:**

Officers delegated with the authority to invest must diversify the investment portfolio and avoid excessive risk concentration with any single counterparty.

The approach to diversification must be balanced with the need to seek an adequate rate of return for the City, given that higher rates of return are usually associated with higher credit risk.

Investments obtained are to be guided by:

- a. Portfolio Credit Framework: limit overall credit exposure of the portfolio;
- b. Counterparty Credit Framework: limit exposure to individual counterparties / institutions; and
- c. Term to Maturity Framework: limits based upon maturity of securities.

The portfolio credit guidelines applied to the City’s investments will be based on the Standard and Poor’s (S&P) ratings system criteria, or the equivalent from Moody’s or Fitch as necessary. A description of each S&P rating category is included in Appendix 1 including the meaning of the signs that may be linked to the rating.

Where conflicting ratings levels exist for any counterparty and/or product, the rating level applied by two out of the three ratings agencies will be used, represented by the S&P rating, if valid. Where all three agencies have issued different ratings, the S&P rating will prevail.

**3.6.1. Overall Portfolio Limits:**

To control the credit quality over the entire portfolio, the following credit framework limits the percentage of the portfolio exposed to any particular combination of long term and short-term credit ratings, as detailed in the matrix below:

Portfolio Limits				
Standard & Poor’s Rating		Long Term		
		AAA+ to AAA-	AA+ to AA-	A+ to A-
Short Term	A-1+	100%	100%	Not Applicable
	A-1	Not applicable	75%	50%
	A-2	Not applicable	Not applicable	40%

**3.6.2. Counterparty Credit Framework:**

Exposure to an individual counterparty/institution will be restricted by a combination of their long term and short-term credit rating so that single entity exposure is limited, as detailed in the table below:

Counterparty Limits				
Standard & Poor's Rating		Long Term		
		AAA+ to AAA-	AA+ to AA-	A+ to A-
Short Term	A-1+	30%	25%	Not Applicable
	A-1	Not applicable	20%	15%
	A-2	Not applicable	Not applicable	10%

In the absence of any evidence to the contrary unrated wholly owned subsidiaries of a rated financial institution will be taken to have the same credit rating as their parent entity.

If the credit rating of any counterparty is downgraded such that any investments held with such party no longer comply with this policy, the City will take steps to divest such investments as soon as practicable, subject to due consideration of penalties and lost interest.

### 3.6.3 Term to Maturity Framework:

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

Overall Portfolio Return to Maturity	Minimum	Maximum
Up to 12 months	70%	100%
13 to 24 months	0%	30%
25 to 36 months	0%	20%

Officers delegated to invest must take into account ongoing liquidity requirements when placing investments to ensure availability of funds to meet the City's payment obligations as and when they fall due.

### 3.7. Investment Advisor:

The City may appoint an investment advisor to provide independent advice regarding the management of the City's investments.

Any investment advisor appointed by the City must be appropriately licensed by the Australian Securities and Investment Commission. The investment advisor must be an independent person who has no actual or potential conflict of interest in relation to investment products being recommended and is free to recommend the most appropriate product within the terms and conditions of the investment of available funds policy.

The investment advisor's appointment is to be subject to a letter of engagement setting out the terms of appointment which may include:

- Monthly reporting;
- Monthly market review of returns and market value of the portfolio; and
- Meetings with the responsible City officers no less than six monthly, to review the City's investment portfolio.

### 3.8. Benchmarking:

The performance benchmark for the City's investment portfolio is set at fifty basis points above the average Reserve Bank Cash Rate for the reporting period.

### 3.9. Reporting and Review:

A monthly report will be provided to Council in support of the monthly Financial Activity Statement. The report will detail the investment portfolio in terms of performance, percentage exposure of total portfolio, maturity date and changes in market value.

Documentary evidence must be held for each investment and details thereof maintained in an Investment Register.

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.

This Investment of Available Funds Policy will be reviewed at least once a year or as required in the event of legislative changes.

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**Creation Date:** April 2008

Formally: *Sustainable Statement Policy, Investment Policy*

**Amendments:** INT10/29125, CJ213-06/99, CJ121-06/02, CJ232-09/02, CJ213-09/03, CJ206-10/05, CJ207-10/07, CJ052-04/08, CJ187-09/13, CJ048-03/16, CJ170-10/17, CJ160-10/20

**Related Documentation:**

- *Local Government Act 1995*
- *Register of Delegation of Authority*
- *The Trustee Act 1962*
- *Local Government (Financial Management) Regulation 1996*
- *Australian Accounting Standards*

## Appendix 1 – Investment of Available Funds Policy

### Standard & Poor’s Ratings Definitions

Standard and Poor’s (S&P) is a professional ratings agency that provides analysis of corporate and institutional creditworthiness. An S&P rating is an opinion of the general creditworthiness of an entity, either as a whole or with respect to a particular financial obligation, based on relevant risk factors.

According to S&P, credit ratings are based, in varying degrees, on the following considerations:

- Likelihood of payment;
- Nature and provisions of the obligation; and
- Protection afforded by, and relative position of, the obligation in the event of bankruptcy, reorganisation or other legal arrangement that affects creditors’ rights.

<b>Ratings – Long Term Financial Obligations (Maturity greater than 365 days)</b>	
<b>AAA</b>	Extremely strong capacity to meet financial commitments on the long-term obligation
<b>AA</b>	Very strong capacity to meet financial commitments
<b>A</b>	Strong capacity to meet financial commitments, but somewhat susceptible to adverse circumstances and economic conditions
<b>BBB</b>	Adequate capacity to meet financial commitments, but susceptible to adverse circumstances and economic conditions
<b>BB</b>	Currently has capacity to meet financial commitments, but clearly vulnerable to adverse circumstances and economic conditions
<b>B</b>	Currently has capacity to meet financial commitments, but highly vulnerable to adverse circumstances and economic conditions
<b>CCC</b>	Currently vulnerable to non-payment, and dependent on favourable economic conditions to meet financial commitments
<b>CC</b>	Currently highly vulnerable to non-payment
<b>R</b>	Under regulatory supervision. Highly likely not to meet financial commitments

<b>Ratings – Short Term Financial Obligations (Maturity not more than 365 days)</b>	
<b>A-1</b>	Strong capacity to meet financial commitments on the short-term obligation
<b>A-2</b>	Satisfactory capacity to meet financial commitments, but somewhat susceptible to adverse circumstances and economic conditions
<b>A-3</b>	Adequate capacity to meet financial commitments but susceptible to adverse circumstances and economic conditions
<b>B</b>	Current capacity to meet financial commitments but vulnerable to adverse circumstances and economic conditions and faces major ongoing uncertainty which could lead to inadequate capacity
<b>C</b>	Currently vulnerable to non-payment and is dependent on favourable economic conditions to meet financial commitments
<b>R</b>	Under regulatory supervision and highly likely not to meet financial commitments

Ratings may be modified by the addition of a plus (+) or minus (-) sign to show relative standing within the major rating categories.

(Source: Standard & Poor’s Ratings Definitions, [https://www.standardandpoors.com/en\\_AU/web/guest/article/-/view/sourceId/504352](https://www.standardandpoors.com/en_AU/web/guest/article/-/view/sourceId/504352), accessed 2 February 2016).