Notice is given that an ordinary meeting of the Corporate Services Committee will be held on:

Date:	**Thursday 13 March 2014**
Time:	**11.30 am**
Meeting Room:	**Tasman Council Chamber**
Venue:	**189 Queen Street Richmond**

Corporate Services Committee

AGENDA

MEMBERSHIP

Chairperson	Cr T B King	
Deputy Chairperson	Cr M J Higgins	
Members	Mayor R G Kempthorne	Cr M L Bouillir
	Cr J L Edgar	Cr B W Ensor
	Cr Z S Mirfin	Cr T E Norriss
	Cr B F Dowler	Cr M J Greening
	Cr P L Canton	Cr J L Inglis
	Cr P F Sangster	Cr S G Bryant

(Quorum 7 members)

Contact Telephone: 03 543 8453
Email: valerie.gribble@tasman.govt.nz
Website: www.tasman.govt.nz

Note: The reports contained within this agenda are for consideration and should not be construed as Council policy unless and until adopted.

AGENDA

1 OPENING, WELCOME

2 APOLOGIES AND LEAVE OF ABSENCE

An apology has been received from Mayor R G Kempthorne.

Recommendation

That an apology be accepted from Mayor R G Kempthorne.

3 PUBLIC FORUM

4 DECLARATIONS OF INTEREST

5 LATE ITEMS

6 CONFIRMATION OF MINUTES

That the minutes of the Corporate Services Committee meeting held on Thursday, 30 January 2014, be confirmed as a true and correct record of the meeting.

7 REPORTS OF COMMITTEE

Nil

8 PRESENTATIONS

Nil

9 REPORTS

9 REPORTS

9.1 ACTION SHEET - 13 MARCH 2014

Information Only - No Decision Required

Report To:	Corporate Services Committee
Meeting Date:	13 March 2014
Report Author:	Valerie Gribble, Executive Assistant
Report Number:	RFN14-03-08

1 Summary

1.1 The outstanding action items from previous Corporate Services Committee meetings are attached.

1.2 Progress on items is shown in the status column.

2 Draft Resolution

That the Corporate Services Committee receives the Action Sheet - 13 March 2014 RFN14-03-08.

3 Attachments

Action Sheet – Corporate Services Committee

Item	Action Required	Responsibility	Completion Date/Status
Meeting Date: 8 November 2012			
Growth projection monitoring	A regular report back is required to measure actual growth against budget	R Holden, Finance Manager M Tregurtha, Strategic Projects Adviser A Humphries, Regulatory Manager	A cross-functional project is being set up to determine the most effective way to capture the required information. No further progress has been made.
Meeting Date: 7 November 2013			
9.3	Staff to prepare draft policy on Remissions for Sporting etc.	R Holden, Finance Manager	In progress for including Special Consultative Process in conjunction with the Annual Plan
9.5	Staff to find out Forestry Overhead costs and communicate them to Councillors	J Frater, Manager Property Services	Completed
9.5	Manager Property Services to investigate practicalities of different ownerships of wharves in Golden Bay and report back to Council	J Frater, Manager Property Services	CEO report went to 6 March Full Council meeting

9.2 CHAIRPERSON'S REPORT - MARCH 2014

Decision Required

Report To:	Corporate Services Committee
Meeting Date:	13 March 2014
Report Author:	Tim King, Chairman, Corporate Services
Report Number:	RFN14-03-07
File Reference:	

1 Summary

Chair's report for Corporate Services Committee meeting 13 March, 2014.

2 Draft Resolution

That the Corporate Services Committee receives the Chairperson's Report - March 2014 RFN14-03-07.

3 Draft Annual Plan 2014/15

3.1 The decisions taken recently over the key items for inclusion or exclusion from the draft Annual Plan highlights the challenges that Council is going to face in preparation of the ten year plan in moving to a position less reliant on debt for financing both renewals and in the case of community infrastructure, new facilities.

3.2 While reducing debt is one of the key issues, other ways of financing the costs of renewals, upgrades and new infrastructure will not necessarily be less challenging. Looking at some of the newspaper reports of other councils rate rises, it is clear that even those with little debt or significant other assets are still facing rate rises in order to meet community expectations across the wide-range of activities that they are involved with.

3.3 As part of today's agenda, the item relating to the elements of a revised financial strategy are the first steps in setting the broader parameters in which the decisions about what to do, and when, and what the highest priorities are will be made.

3.4 As you can see, a number of the elements will require some difficult discussions with communities who may have an expectation of particular works in their areas over the next ten years. In part, this expectation has been built up by the significant amount of work that has been undertaken over the previous ten years. I firmly believe that while this has resulted in debt levels that need to be managed carefully, the community is considerably better off than had these works not been undertaken. It is often easy to look at the accounts and see the results that have been done, it is however much harder when looking at the same accounts to see what hasn't been done and may be a liability in the future.

3.5 I am confident that with the advice that we are receiving from staff in relation to the transition heading into the ten year plan, that these issues will be resolved.

4 Attachments

Nil

Item 9.3

9.3 CORPORATE SERVICES MANAGER'S REPORT

Information Only - No Decision Required

Report To:	Corporate Services Committee
Meeting Date:	13 March 2014
Report Author:	Mike Drummond, Corporate Services Manager
Report Number:	RFN14-03-01
File Reference:	

1 Summary

1.1 **LAPP -** Council has received the LAPP Annual Report for 2013. A copy is available on request from the Corporate Services Manager.

1.2 **Civic Assurance –** There has been a further extension to the Civic Assurance 2012 Share Offer. The offer has been extended to December 2014. Council previously declined to purchase an increased shareholding in the company. No further action is being taken on the offer.

1.3 **Half Yearly reports** – The half yearly reports have been received from the following identities and referred to the Joint Shareholders Committee. Copies of the reports are available to councillors on request.

- Port Nelson Ltd
- Tasman Bays Heritage Trust
- Nelson Airport Ltd

1.4 **NRSBU** – The NRSBU annual business plan has been delayed but this will not impact on the Councils 2014/15 draft Annual Plan.

1.5 **Local Government Funding Agency (LGFA) quarterly and half yearly report** – The half yearly report has been received. The LGFA is operating well and Council can expect to receive a 7% dividend on its investment. Total borrowings through the LGFA now total $3.05 billion. In 2013, 76% of new local government debt was placed through the LGFA.

1.6 **Local Government Funding Agency (LGFA) SOI -** The draft 2014/15 SOI has been received comments from shareholders are due to the LGFA board by 30 April 2014. The Corporate Services Committee will be requested to formally accept the SOI at its April Meeting.

1.7 **Risk Pool Annual report** – the 2013 annual report has been received. Risk pool announced in November that there was presently no need for a call during the 2014-2015 financial year. This has been factored into the 2014/15 draft Annual Plan.

1.8 **Nelson Airport -** There is a proposed amendment to the Company's constitution to bring it into line with the Council's director appointment process. The Airport's Statement of Corporate Intent for 2014/15 has been received. This will be referred to the Joint Shareholders Committee for review and a recommendation to each council shareholder.

1.9 **Insurance –** Public liability and professional indemnity cover for councillors. Our brokers have confirmed that some cover is available in some circumstances. Staff are contacting all organisations that Councillors are appointed to, or serve on, to determine if they have appropriate cover in place for trustees etc. The initial response was poor and follow up is taking place.

1.10 **IS Department update -** Progress has been made on the GIS shared services project with a combined tender document having been produced. The installation of a rates modelling system has been completed. The electronic building consent project is on track and will go live in April 2014. The Council's Disaster Recovery Plan is being updated and the fit-out of the Regional Emergency Operations Centre is on track for the April 2014 exercise.

1.11 **Local Government Funding Agency Draft SOI 2014-15** - The draft 2014/15 SOI has been received (Attachment 1). Comments from shareholders are due to the LGFA Board by 30 April 2014.

2 Draft Resolution

That the Corporate Services Committee receives the Corporate Services Manager's Report RFN14-03-01.

3 Purpose of the Report

3.1 This report is to update the Committee on Corporate Services activities not covered in separate reports.

4 Local Authority Protection Programme (LAPP)

4.1 Council has received the LAPP Annual Report for 2013. Highlights of the Chairman's report include:

- Settlement of the below-ground claims for the Waimakariri District Council and Christchurch City Council ($217m).
- Continued growth of the fund projected to be $20m by 1 July 2014.
- Successful outcomes in the two court cases that LAPP instigated.

4.2 LAPP covers 40% of Council's under-ground infrastructure assets. The remaining 60% is covered by central government. LAPP is unable to obtain 100% reinsurance at an acceptable cost. As a result LAPP members cover the difference through "mutual self insurance". As a result of more affordable reinsurance rates the members' mutual self insurance component of the 40% dropped from $45m in 2012/13 to $34m in 2013/14.

4.3 The full annual report is available on request from the Corporate Services Manager.

5 Civic Assurance

5.1 Civic Assurance has advised a further extension to their share offer to all councils. In addition the offer has been extended again, this time to 5 December 2014. The share offer is at 90c/share. The current net asset value per share is approximately $1.05.

5.2 The purpose of the share offer was to allow non-shareholding councils to become shareholders and for existing shareholders to increase their shareholding. The capital raised is to be used to strengthen Civic's balance sheet and provide Civic with more options for re-entering the local government insurance market.

5.3 Council has previously considered the share offer and declined to participate. There has been no material change in the circumstances that led to Council's previous decision. In the absence of further direction from the Committee no further action is being taken and the offer will lapse in due course.

6 Half Yearly Reports – Council Controlled Organisations (CCOs)

6.1 The half yearly reports from the following organisations have been received and referred to the Joint Shareholders Committee. Copies are available to Councillors on request. The reports are likely to be made public after they have been reviewed by the Joint Shareholders committee. Under the Local Government Act 2002 only annual reports are required to be made public.

- Port Nelson Ltd
- Tasman Bays Heritage Trust
- Nelson Airport Ltd

7 Nelson Regional Sewerage Business Unit (NRSBU)

7.1 Due to delays in constituting the NRSBU Board post the local authority elections there was a delay in receiving the NRSBU 2014/15 Business Plan. This will have a minor impact on the finalisation of the 2014/15 Annual Plan.

8 Local Government Funding Agency (LGFA) Quarterly and Half Yearly reports

8.1 The LGFA quarterly report to 31 December 2013 has been received. The December 2013 bond tender raised $150m, bringing the total LGFA bonds outstanding to $3.05 billion. The LGFA bond programme in 2013 was $1.515b just under the $1.535b issued in 2012. These bond issues continue to attract good support. The margins being paid for these borrowings are lower and this translates into reduced borrowing costs for councils.

8.2 Based on the expected cost of funds of 5% during 2013/14 the LGFA anticipates paying a return to shareholders of 7%. This dividend will be used to cover interest costs on Council's borrowing to purchase its shares in the LGFA and a small reduction in the loan principal.

8.3 76% of new local government debt in 2013 was placed through the LGFA. The other two largest lenders were the ANZ bank 17% and BNZ 6.3%.

8.4 On 7 November 2013 Standard and Poors and Fitch affirmed the LGFA's local currency credit rating as AA+ and foreign currency rating as AA. The outlook for both ratings is stable. This rating is the same as the New Zealand government rating.

8.5 All Council's borrowing through the LGFA complied with the required financial covenants measured at 30 June 2013. Tasman District Council has the fifth highest ratio of debt to revenue of the 38 council members of the LGFA. Councils with a higher ratio of debt to revenue were Tauranga City, Hamilton City, Western Bay of Plenty and Kapiti Coast .

8.6 The Half Yearly Report (December 2013) has been received. A copy is available to Councillors, on request. Key matters covered in the directors' commentary include:

- The continuing reduction of base margins to Councils. These have reduced from an initial 30bps on launch to 15bps (0.15%) in September 2013.
- Bond issuing has exceeded $3 billion. This is a significant milestone.
- Pre-establishment expenses have now been fully recovered.
- During the half year, three further councils joined the LGFA. Members of the LGFA now represent 90% of the local government debt.
- The net operating profit for the half year was $3.27m, slightly ahead of forecast.

9 Local Government Funding Agency Draft Statement of Intent (SOI)

9.1 The draft 2014/15 SOI has been received (Attachment 1). Comments from shareholders are due to the LGFA Board by 30 April 2014.

9.2 Councillors are requested to advise any concerns or issues with the draft SOI to the Corporate Services Manager. The Corporate Services Committee will be requested to formally accept the SOI at its April 2014 meeting. Key changes on the previous year's SOI include:

- Revising the financial forecasts primarily to reflect a significant increase in forecast total expenses. This is mainly as a result of increased liquidity facility fees, the cost of the new treasury system, and the requirement for additional LGFA staff as a number of operational functions are migrated from the NZ Debt Management Office (NZDMO) to the LGFA. Despite these significant cost increases, LGFA's forecast profitability remains strong.
- Updating performance targets, with a further reduction in the base margin target over the next three years relative to SOI 2013/14.
- Adding two more quarterly reporting requirements in relation to the new treasury system and the weighted average maturity of LGFA bonds.

10 Riskpool Annual Report

10.1 The Riskpool annual report for 2013 has been received. A copy is available to Councillors on request.

10.2 Key points from the report include:

- The past year has seen further developments in New Zealand case law and legislation, in particular with regard to commercial exposures. Riskpool announced in November 2013 that there was presently no need for a call during the 2014-2015 financial year.
- Riskpool continues to enjoy ground-up reinsurance. This was secured on 1 July 2012 and is in place for three years. Riskpool intends seeking the continuation of ground-up reinsurance as this factor has been communicated to the Riskpool Board by councils, as being of significant importance.
- Riskpool is continuing to monitor developments due to changes in New Zealand case law. The extension of liability for commercial claims has the potential to affect prior fund years. There have also been interesting developments on matters such as contributory negligence which are now influencing the way Riskpool, their Claims Manager and Scheme Solicitor handle mediations and trials.
- Riskpool, in concert with Local Government New Zealand and the Society of Local Government Managers made a number of submissions to the New Zealand Law Commission as to the impact joint and several liability has had on the sector.

11 Nelson Airport Ltd

11.1 The directors of Nelson Airport Ltd (NAL) are promoting an amendment to the constitution. This amendment covers the appointment and rotation of directors. The change is necessary to align the constitution with both councils approach to the appointment of directors to NAL.

11.2 Two key changes are that the appointments by TDC and NCC will no longer be restricted to a council member or an employee, and a suggested change to remove from the constitution the provision for directors to retire by rotation, as this is included in the Council Appointment Policy. I have advised that this is not acceptable and suggested a simplified provision covering retirement by rotation. This is currently with the solicitors for drafting. A revised set of amendments will be received in due course for consideration.

11.3 The draft Nelson Airport Ltd Statement of Corporate Intent (SOI) for 2014/15 has been received. The SOI includes new targets and objectives along with a modernising of the language to improve readability. The SOI is being reviewed by staff and will be the subject of a separate report to the Joint Shareholders Committee. The SOI forecasts a $508,544 for the 2014/15 year. This is lower than the dividends for the 2013/14 year. This year dividends were boosted by a special one-off dividend of $150,000 in recognition of the 75th anniversary of the Airport.

12 Insurance – Public Liability and Professional Indemnity etc

12.1 Our brokers have advised that some cover is available for Councillors and staff acting within their role responsibilities, ie acting for and on behalf of Council as part of their role as TDC appointed members.

12.2 However the position changes where individuals are appointed to external legal entities such as companies, trusts and associations, including incorporated societies where such entities have an increased accountability in respect of the provision of their advice or services. These companies, trusts and associations need to consider **Professional Indemnity and Public Liability Insurance** protection for businesses (including all of their employees/ directors etc) in respect of legal liability arising from the activities and conduct of their practice or business.

12.3 Employees will generally be indemnified (personally), for work-related acts, errors or omissions made by the organisation that they work for, by way of their employment contract. Such acts, errors or omissions are covered by a Professional Indemnity or Public Liability Insurance policy held in the name of the company or trust or association.

12.4 Entities such as the Nelson Airport Ltd will fall outside of Council's cover provided by Riskpool, and should have their own liability insurance programme including Public Liability, Professional Indemnity and Directors and Officers Liability Insurance.

12.5 We are continuing to follow through with a number of organisations the need for them to have Professional Indemnity and Public Liability Insurance in place to protect their elected/ appointed officials including Council nominees. Councillors should note that where they hold their position in a personal capacity, rather than being appointed by Council, as a Council representative they will fall outside the Council Riskpool cover.

13 IS Department Update

12.1 Shared Services GIS

TDC has developed a combined tender document for the GIS imagery and data purchasing programme to allow joint purchasing by Top of the South councils. This will increase our buying power and share administration costs of the flying programme. The combined tender will be finalised in time for any purchasing as part of the 2014/15 financial year.

12.2 Rates Modelling System

This was installed in early February 2014. Napier Computer Systems staff will be onsite in March 2014 working with finance staff to configure the system. Rates Modelling will allow staff to analyse rating changes and gain a clearer picture of revenue and ratepayer cost implications.

12.3 Project work

- Building staff are being trained on the new electronic building consent process. The process is due to go live in April 2014.
- The Information Services (IS) Disaster Recovery Plan is in the final stages of updating. IS are investigating recovery solutions with the Plan due to be completed at the end of March 2014.
- IS staff are installing computer equipment into the Emergency Operations Centre Operations Room ready for an emergency management exercise in early April 2014.

13 Attachments

LGFA New Zealand Local Government Funding Agency

Statement of Intent 2014/15

1. Introduction

This Statement of Intent (SOI) sets out the intentions and expectations of New Zealand Local Government Funding Agency Limited (LGFA).

The LGFA is enabled under the Local Government Borrowing Act 2011 and is a council-controlled organisation (CCO) for the purposes of the Local Government Act 2002.

The SOI is prepared in accordance with section 64(1) of the Local Government Act 2002.

2. Nature and scope of activities

LGFA will raise debt funding either domestically and/or offshore in either NZ dollars or foreign currency and provide debt funding to New Zealand local authorities, and may undertake any other activities considered by the Board of LGFA to be reasonably related or incidentally to, or in connection with, that business.

The LGFA will only lend to local authorities that enter into all the relevant arrangements with it (Participating Local Authorities) and comply with the LGFA's lending policies.

In lending to Participating Local Authorities, LGFA will:

- Operate in a manner to ensure LGFA is successful and sustainable in the long-term
- Educate and inform Participating Local Authorities on matters within the scope of LGFA's operations
- Provide excellent service to Participating Local Authorities
- Ensure excellent communication exists and be professional in its dealings with all its stakeholders
- Ensure its products and services are delivered in a cost effective manner

3. Objectives

Principal Objectives

In accordance with the Local Government Act 2002, in carrying on its business, the principal objectives of LGFA will be to:

- achieve the objectives and performance targets of the shareholders (Shareholders) in LGFA (both commercial and non-commercial) as specified in this SOI;

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- be a good employer;
- exhibit a sense of social and environmental responsibility by having regard to the interests of the community in which it operates and by endeavouring to accommodate or encourage these when able to do so; and
- conduct its affairs in accordance with sound business practice.

Primary objective

LGFA will operate with the primary objective of optimising the debt funding terms and conditions for Participating Local Authorities. Among other things this includes:

- Providing estimated savings in annual interest costs for all Participating Local Authorities of at least 30 basis points, based on the methodology set out in LGFA's Annual Report 2012-2013
- Making longer-term borrowings available to Participating Local Authorities
- Enhancing the certainty of access to debt markets for Participating Local Authorities, subject always to operating in accordance with sound business practice

Additional objectives

LGFA has a number of additional objectives which complement the primary objective. These objectives will be measurable and achievable and the performance of the company in achieving its objectives will be reported annually. These additional objectives are to:

- Operate with a view to making a profit sufficient to pay a dividend in accordance with its stated Dividend Policy set out in section 6
- Provide at least 50% of aggregate long-term debt funding for Participating Local Authorities
- Ensure its products and services are delivered at a cost that does not exceed the forecast for issuance and operating expenses set out in section 4
- Maintain LGFA's credit rating equal to the New Zealand Government sovereign rating where both entities are rated by the same Rating Agency
- Achieve the Financial Forecasts set out in section 4
- Meet or exceed the Performance Targets outlined in section 5
- Comply with its Treasury Policy, as approved by the Board

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4. Financial forecasts

LGFA's financial forecasts for the four years to 30 June 2017 are:

Financial Year ($m)	2013/14	2014/15	2015/16	2016/17
Comprehensive income				
Net interest revenue	9.84	11.97	12.4	13.38
Issuance and operating expenses	3.20	4.00	5.00	5.20
P & L	6.64	7.97	7.40	8.18
Financial position				
Dividend	(1.75)	(1.75)	(1.75)	(1.75)
Retained earnings	3.59	9.80	15.45	21.88
Total assets	3,544.00	4,550.97	5,556.61	6,563.05
Total LG loans	3,484.00	4,484.00	5,484.00	6,484.00
Total bonds	3,480.00	4,435.00	5,435.00	6,435.00
Total borrower notes	55.74	71.74	87.74	103.74
Total equity	28.59	34.80	40.45	46.88
Shareholder Funds/Total Assets	0.8%	0.8%	0.7%	0.7%

Issuance and operating expenses are forecast to be significantly higher in SOI 2014/15 relative to SOI 2013/14. This is due to:

1. Implementing and maintaining a new treasury system. This includes the cost of consultants to advise and assist with the project, depreciation on the capital cost of the new treasury system, and ongoing system maintenance costs.

2. Increasing LGFA staff as key operational services (bond tendering, settlements, risk reporting and accounting) are migrated from NZDMO to LGFA. The cost of additional LGFA staff is forecast to significantly exceed the outsourced services fee currently paid to NZDMO.

3. Undertaking more marketing activity to increase offshore holdings of LGFA bonds.

4. Increasing Approved Issuer Levy (AIL) payments. This cost increase is directly associated with the rise in offshore holdings of LGFA bonds.

5. Potentially incurring significantly higher fees associated with the NZDMO liquidity facility. We had previously assumed that the facility size chosen by LGFA would be reduced in February 2015 to offset a contractual doubling of the facility fee. For SOI 2014/15, we have adopted a more conservative assumption that the maximum facility size ($1 billion) will be chosen.

Specifically, forecast total expenses for the 2015/16 financial year ($5 million in SOI 2014/15) are $1.6 million higher than previously reported ($3.4 million in SOI 2013/14). The difference is reconciled in the following table:

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Forecast 2015/16 expenses	SOI 2014/15 (000's)	SOI 2013/14 (000's)	Difference (000's)
Facility fee	1,000	200	800
New treasury system (incl. consultants)	650	20	630
New LGFA staff	350	100	250
Marketing	90	30	60
AIL	300	240	60
Net cost savings (other expense categories)	(200)	-	(200)
Total	**2,190**	**590**	**1,600**

It may be possible to substantially reduce the cost of the NZDMO liquidity facility. In this regard, LGFA intends to consult with shareholders on ways to reduce the cost of this facility, including possible amendments to the Foundation Policies.

5. Performance targets

LGFA has the following performance targets:

- LGFA's average cost of funds relative to the average cost of funds for New Zealand Government Securities for the period to:
  - 30 June 2015 will be less than 0.50% higher
  - 30 June 2016 will be less than 0.50% higher
  - 30 June 2017 will be less than 0.50% higher
- The average margin above LGFA's cost of funds charged to the highest rated Participating Local Authorities for the period to:
  - 30 June 2015 will be no more than 0.15%
  - 30 June 2016 will be no more than 0.10%
  - 30 June 2017 will be no more than 0.10%
- LGFA's annual issuance and operating expenses for the period to:
  - 30 June 2015 will be less than $4.0 million
  - 30 June 2016 will be less than $5.0 million
  - 30 June 2017 will be less than $5.2 million
- Total lending to Participating Local Authorities at:
  - 30 June 2015 will be at least $4,400 million
  - 30 June 2016 will be at least $5,400 million
  - 30 June 2017 will be at least $6,400 million

6. Dividend policy

LGFA will seek to maximise benefits to Participating Local Authorities as Borrowers rather than Shareholders. Consequently it is intended to pay a limited dividend to Shareholders.

The Board's policy is to pay a dividend that provides an annual rate of return to Shareholders equal to LGFA cost of funds plus 2.00% over the medium term.

Retained earnings are forecast to increase to $21.9 million by June 2017. As a result, LGFA will review its capital structure and report to shareholders by 30 June 2015.

At all times payment of any dividend will be discretionary and subject to the Board's legal obligations and views on appropriate capital structure.

7. Governance

Board

The Board is responsible for the strategic direction and control of LGFA's activities. The Board guides and monitors the business and affairs of LGFA, in accordance with the Companies Act 1993, the Local Government Act 2002, the Local Government Borrowing Act 2011, the Company's Constitution, the Shareholders' Agreement for LGFA and this SOI.

The Board will comprise between four and seven directors with a majority of independent directors.

The Board's approach to governance is to adopt "best practice" with respect to:

- The operation of the Board
- The performance of the Board
- Managing the relationship with the Company's Chief Executive
- Being accountable to all Shareholders

All directors are required to comply with a formal Charter, to be reviewed from time to time in consultation with Shareholders.

The Board will meet on a regular basis and no less than 6 times each year.

Shareholders' Council

The Shareholders' Council is made up of between five and ten appointees of the Shareholders (including an appointee from the Crown). The role of the Shareholders' Council is to:

- Review the performance of LGFA and the Board, and report to Shareholders on that performance on a periodic basis (no less frequently than quarterly)
- Make recommendations to Shareholders as to the appointment, removal, replacement and remuneration of directors
- Make recommendations to Shareholders as to any changes to policies, or the SOI, requiring their approval

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- Ensure all Shareholders are fully informed on LGFA matters and to coordinate Shareholders on governance decisions

8. Information to be provided to Shareholders

The Board aims to ensure that the Shareholders are informed of all major developments affecting LGFA's state of affairs, while at the same time recognising that commercial sensitivity may preclude certain information from being made public. The LGFA will adhere to a 'no surprises' approach in its dealings with its Shareholders.

Annual Report

The LGFA's balance date is 30 June.

By 30 September each year, the Company will provide to the Shareholders an Annual Report complying with Sections 67, 68 and 69 of the Local Government Act 2002, the Companies Act and Financial Reporting Act. The Annual Report will contain the information necessary to enable an informed assessment of the operations of the company, and will include the following information:

- Directors' Report
- Financial Statements incorporating a Statement of Financial Performance, Statement of Movements in Equity, Statement of Financial Position, Statement of Cashflows, Statement of Accounting Policies and Notes to the Accounts
- Comparison of the LGFA's performance with regard to the objectives and performance targets set out in the SOI, with an explanation of any material variances
- Auditor's Report on the financial statements and the performance targets
- Any other information that the directors consider appropriate

Half Yearly Report

By 28 February each year, the Company will provide to the Shareholders a Half Yearly Report complying with Section 66 of the Local Government Act 2002. The Half Yearly Report will include the following information:

- Directors' commentary on operations for the relevant six month period
- Comparison of LGFA's performance with regard to the objectives and performance targets set out in the SOI, with an explanation of any material variances
- Un-audited half-yearly Financial Statements incorporating a Statement of Financial Performance, Statement of Movements in Equity, Statement of Financial Position and Statement of Cashflows

Quarterly Report

By 30 April, 31 July, 31 October and 31 January each year, the Company will provide to the Shareholders' Council a Quarterly Report. The Quarterly Report will include the following information:

- Directors' commentary on operations for the relevant quarter, including a summary of borrowing margins charged to Participating Local Authorities (in credit rating bands)
- Comparison of LGFA's performance with regard to the objectives and performance targets set out in the SOI, with an explanation of any material variances
- Commentary in relation to implementation of the new treasury system and the migration of operational services from NZDMO to LGFA
- Analysis of the weighted average maturity of LGFA bonds outstanding
- In the December Quarterly Report only, commentary on the Net Debt/Total Revenue percentage for each Participating Local Authority that has borrowed from LGFA (as at the end of the preceding financial year)
- To the extent known by LGFA, details of all events of review in respect of any Participating Local Authority that occurred during the relevant quarter (including steps taken, or proposed to be taken, by LGFA in relation thereto)

Statement of Intent

By 1 March in each year the Company will deliver to the Shareholders its draft SOI for the following year in the form required by Clause 9(1) of Schedule 8 and Section 64(1) of the Local Government Act 2002.

Having considered any comments from the Shareholders received by 30 April, the Board will deliver the completed SOI to the Shareholders on or before 30 June each year.

Shareholder Meetings

The Board will hold an Annual General Meeting between 30 September and 30 November each year to present the Annual Report to all Shareholders.

The Company will hold a meeting with the Shareholders' Council approximately every six months – prior to the Annual General Meeting and after the Half Yearly Report has been submitted. Other meetings may be held by agreement between the Board and the Shareholders' Council.

9. Acquisition/divestment policy

LGFA will invest in securities in the ordinary course of business. It is expected that these securities will be debt securities. These investments will be governed by LGFA's lending and/or investment policies as approved by the Board and/or Shareholders.

Any subscription, purchase or acquisition by LGFA of shares in a company or organisation will, if not within those investment policies, require Shareholder approval other than as concerns the formation of wholly-owned subsidiaries and the subscription of shares in such wholly-owned subsidiaries.

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10. Activities for which compensation is sought from Shareholders

At the request of Shareholders, LGFA may (at its discretion) undertake activities that are not consistent with its normal commercial objectives. Specific financial arrangements will be entered into to meet the full cost of providing such as activities.

Currently there are no activities for which compensation will be sought from Shareholders.

11. Commercial value of Shareholder's investment

LGFA will seek to maximise benefits to Participating Local Authorities as Borrowers rather than Shareholders.

Subject to the Board's views on the appropriate capital structure for LGFA, the Board's intention will be to pay a dividend that provides an annual rate of return to Principal Shareholders equal to LGFA cost of funds plus 2.00% over the medium term.

As the Shareholders will have invested in the LGFA on the basis of this limited dividend, the Board considers that at establishment the commercial value of LGFA is equal to the face value of the Shareholders' paid up Principal Shares - $25 million.

Based on observed share transfers on 30 November 2012, the Board considers the current commercial value of LGFA continues to equal the face value of the Shareholders' paid up Principal Shares - $25 million.

The commercial value of LGFA will be assessed annually.

12. Accounting policies

LGFA has adopted accounting policies that are in accordance with the New Zealand International Financial Reporting Standards and generally accepted accounting practice. A Statement of accounting policies is attached to this SOI.

This statement is taken from the Financial Statements presented as part of LGFA's Annual Report 2012-2013.

DRAFT – For discussion purposes

ATTACHMENT: Statement of accounting policies

a Reporting Entity

The New Zealand Local Government Funding Agency Limited (LGFA) is a company registered under the Companies Act 1993 and is subject to the requirements of the Local Government Act 2002.

LGFA is controlled by participating local authorities and is a council-controlled organisation as defined under section 6 of the Local Government Act 2002. LGFA is a limited liability company incorporated and domiciled in New Zealand.

The primary objective of LGFA is to optimise the debt funding terms and conditions for participating local authorities.

The registered address of LGFA is Level 13, 342 Lambton Quay, Wellington Central, Wellington 6011.

The financial statements are as at and for the year ended 30 June 2013. The comparatives are for the seven month period to 30 June 2012 as LGFA was first registered as a company on 1 December 2011.

These financial statements were authorised for issue by the Directors on 27 September 2013.

b Statement of compliance

LGFA is registered under the Companies Act 1993 and is a reporting entity as defined by the Financial Reporting Act 1993. LGFA is a profit orientated entity as defined under the New Zealand Equivalents to International Financial Reporting Standards (NZ IFRS).

The financial statements and accounting policies comply with the specific recognition, measurement and disclosure requirements of NZ IFRS and New Zealand Generally Accepted Accounting Practice (NZGAAP). The financial statements comply with International Financial Reporting Standards.

c Basis of Preparation

Measurement base

The financial statements have been prepared on a historical cost basis modified by the revaluation of certain assets and liabilities.

The financial statements are prepared on an accrual basis.

Functional and presentation currency

The financial statements are presented in New Zealand dollars rounded to the nearest thousand, unless separately identified. The functional currency of LGFA is New Zealand dollars.

Foreign currency conversions

Transactions denominated in foreign currency are translated into New Zealand dollars using exchange rates applied on the trade date of the transaction.

DRAFT – For discussion purposes

Changes in accounting policies

There have been no changes in accounting policies.

Early adoption standards and interpretations

The following accounting standard has been early adopted by LGFA.

NZ IFRS 9: *Financial Instruments*. The first two phases of this new standard (which is incomplete as at 30 June 2013) were approved by the Accounting Standards Review Board in November 2009 and November 2010. The standard addresses the issues of classification and measurement of financial assets and financial liabilities and becomes effective for annual reporting periods commencing on or after 1 January 2015.

Standards not yet adopted

LGFA does not consider any standards or interpretations in issue but not yet effective to have a significant impact on its financial statements. Those which may be relevant to LGFA are as follows:

- Amendments to NZ IAS 32: Financial Instruments: Disclosures. Effective for periods beginning on or after 1 January 2014. This amendment provides clarification on the ability to set-off financial instruments.
- NZ IFRS 13: Fair Value Measurement. Effective for periods beginning on or after 1 January 2013. This standard provides a single source of guidance on determining fair value.

d Financial instruments

Financial assets

Financial assets, other than derivatives, are recognised initially at fair value plus transaction costs and subsequently measured at amortised cost using the effective interest rate method.

Cash and cash equivalents include cash on hand; cash in transit, bank accounts and deposits with an original maturity of no more than three months.

Purchases and sales of all financial assets are accounted for at trade date.

At each balance date an assessment is made whether a financial asset or group of financial assets is impaired. A financial asset or a group of financial assets is impaired when objective evidence demonstrates that a loss event has occurred after the initial recognition of the asset(s), and that the loss event has an impact on the future cash flows of the asset(s) that can be estimated reliably.

Financial liabilities

Financial liabilities, other than derivatives, are recognised initially at fair value less transaction costs and subsequently measured at amortised cost using the effective interest rate method.

Derivatives

Derivative financial instruments are recognised both initially and subsequently at fair value. They are reported as either assets or liabilities depending on whether the derivative is in a net gain or net loss position respectively.

Fair value hedge

Where a derivative qualifies as a hedge of the exposure to changes in fair value of an asset or liability (fair value hedge) any gain or loss on the derivative is recognised in profit and loss together with any changes in the fair value of the hedged asset or liability.

The carrying amount of the hedged item is adjusted by the fair value gain or loss on the hedged item in respect of the risk being hedged. Effective parts of the hedge are recognised in the same area of profit and loss as the hedged item.

e Other assets

Property, plant and equipment (PPE)

Items of property, plant and equipment are initially recorded at cost.

Depreciation is charged on a straight-line basis at rates calculated to allocate the cost or valuation of an item of property, plant and equipment, less any estimated residual value, over its remaining useful life.

f Other liabilities

Employee entitlements

Employee entitlements to salaries and wages, annual leave and other similar benefits are recognised in the profit and loss when they accrue to employees.

g Revenue and expenses

Revenue

Interest income

Interest income is accrued using the effective interest rate method.

The effective interest rate exactly discounts estimated future cash receipts through the expected life of the financial asset to that asset's net carrying amount. The method applies this rate to the principal outstanding to determine interest income each period.

Expenses

Expenses are recognised in the period to which they relate.

Interest expense

Interest expense is accrued using the effective interest rate method.

The effective interest rate exactly discounts estimated future cash payments through the expected life of the financial liability to that liability's net carrying amount. The method applies this rate to the principal outstanding to determine interest expense each period.

Income tax

LGFA is exempt from income tax under Section 14 of the Local Government Borrowing Act 2011.

DRAFT – For discussion purposes

Goods and services tax

All items in the financial statements are presented exclusive of goods and service tax (GST), except for receivables and payables, which are presented on a GST-inclusive basis. Where GST is not recoverable as input tax, then it is recognised as part of the related asset or expense.

The net amount of GST recoverable from, or payable to, the IRD is included as part of receivables or payables in the statement of financial position.

The net GST paid to, or received from the IRD, including the GST relating to investing and financing activities, is classified as a net operating cash flow in the statement of cash flows.

Commitments and contingencies are disclosed exclusive of GST.

h Lease payments

Payments made under operating leases are recognised in profit or loss on a straight-line basis over the term of the lease. Lease incentives received are recognised as an integral part of the total lease expense, over the term of the lease.

i Segment reporting

LGFA operates in one segment being funding of participating local authorities in New Zealand.

j Judgements and estimations

The preparation of these financial statements requires judgements, estimates and assumptions that affect the application of policies and reported amounts of assets and liabilities, income and expenses. For example, the present value of large cash flows that are predicted to occur a long time into the future depends critically on judgements regarding future cash flows, including inflation assumptions and the risk free discount rate used to calculate present values. Refer note 2b for fair value determination for financial instruments.

The estimates and associated assumptions are based on historical experience and various other factors that are believed to be reasonable under the circumstances. Actual results may differ from these estimates.

The estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised, if the revision affects only that period, or in the period of the revision and future periods if the revision affects both current and future periods. Where these judgements significantly affect the amounts recognised in the financial statements they are described below and in the following notes.

9.4 NELSON REGIONAL SEWERAGE BUSINESS UNIT - TREASURY POLICY

Decision Required

Report To:	Corporate Services Committee
Meeting Date:	13 March 2014
Report Author:	Mike Drummond, Corporate Services Manager
Report Number:	RFN14-03-03
File Reference:	C756

1 Summary

1.1 It has been noted by the auditors that the Nelson Regional Sewerage Business Unit (NRSBU) does not have a formal treasury policy.

1.2 The purpose of the NRSBU Treasury Management Policy is to outline policy in respect of the Nelson Regional Sewerage Business Unit (NRSBU) treasury activity, to be undertaken by the Nelson City Council (NCC) and the Tasman District Council (TDC). The formalisation of such policies enables the treasury risks within the NRSBU to be prudently managed.

1.3 Under the original agreement with NCC, TDC was responsible for the NRSBU Treasury function. Under this policy this responsibility formally shifts to the NCC. In effect the day-to-day treasury management is currently being carried out by NCC and there is little merit in splitting the function between the two councils.

1.4 The opportunity has been taken to allow the consolidation of the TDC share of the NRSBU borrowings to be merged into the main TDC treasury activity. The basis for setting the interest rate on advances to the NRSBU has also changed to reflect that they will not have their "own" facilities and interest rate swap instruments post 1 July 2014.

1.5 The Corporate Services Manager at TDC, The Chief Financial Officer at NCC and Council's external treasury advisor, have reviewed a draft policy, made a number of changes and now recommend this revised policy to both councils.

1.6 A copy of the proposed policy and a draft of this paper have been made available to the NRSBU. At their January 2014 meeting the NRSBU joint committee formally adopted the proposed policy.

2 Draft Resolution

That the Corporate Services Committee:

1) **receives the Nelson Regional Sewerage Business Unit - Treasury Policy report RFN14-03-03; and**
2) **approves the draft Nelson Regional Sewerage Business Unit Treasury policy; subject to confirmation by Nelson City Council of its approval of this policy.**
3) **Approves the proposed mechanism to determine the interest rate to be charged to the Nelson Regional Sewerage Business Unit on its borrowings sourced through the Tasman District Council from 1 July 2014; subject to confirmation by Nelson City Council of its approval of this approach.**

3 Purpose of the Report

3.1 To obtain formal approval for a Treasury Policy covering the Nelson Regional Sewerage Business Unit (NRSBU).

4 Background and Discussion

4.1 It has been noted by the auditors that the NRSBU does not have a formal treasury policy. They have recommended that a formal policy be developed.

4.2 Under the original agreement for the NRSBU the TDC has responsibility for the Treasury function of the NRSBU. The day-to-day cash management for the NRSBU is carried out by the NCC. The accounting for the unit is also managed by NCC. It is considered to be more effective if the full treasury function was carried out by NCC. This has been discussed with NCC staff who are supportive of the change. NCC recovers its administration costs through a modest administration charge to the NRSBU.

4.3 The Corporate Services Manager at TDC, the Chief Financial Officer at NCC and Council's treasury advisor have reviewed a draft policy, made a number of changes and now recommend this revised policy (attachment 1) to both councils.

4.4 The purpose of the NRSBU Treasury Management Policy is to outline policy in respect of its treasury activity. This is undertaken by NCC and TDC. The formalisation of such policies enables the treasury risks within the NRSBU to be prudently managed.

4.5 The NRSBU is not a separate legal entity from the councils. As such it does not borrow or invest funds in its own name. Both councils borrow separately to support the NRSBU treasury requirements. These borrowings, while in each council's name, are managed through separate loan facilities with Westpac bank. The day-to-day cash management for the NRSBU is undertaken by NCC.

4.6 TDC currently has a separate borrowing arrangement ($12,500,000) with Westpac bank to cover the borrowing needs of the NRSBU. The covenants in the arrangement relate to TDC as a whole, as the facility is in TDC's name. The security for this arrangement is a charge over TDC rates.

4.7 TDC has also purchased interest rate swaps specifically to cover the risks associated with this borrowing facility. TDC currently has swaps with a nominal value of $8 million in place.

4.8 With the movement of debt to the Local Government Funding Agency (LGFA), Council is currently reviewing its borrowing arrangements with all banks. This provides an opportunity to merge these separate facilities and interest rate swaps into the main Council treasury activity. This is provided for in the proposed NRSBU Treasury Policy.

4.9 The NRSBU policy links to the related NCC and TDC treasury policies. This is appropriate as the underlying borrowing is being undertaken by each council separately.

4.10 With the proposal to move away from maintaining a separate bank facilities for the TDC share of the NRSBU core debt a new mechanism was necessary to determine an appropriate interest rate to charge the NRSBU on these borrowings. In considering available options staff at TDC and NCC were looking for a solution that was administratively straight forward, linked to external rates and transparent. This rate is important as the cost of borrowings is the basis for the weighted average costed capital calculation used to determine charges.

4.11 After reviewing a number of options staff determined that

- The rate should be the same for borrowing sourced through NCC and TDC.
- The rate should be based on the 3 year swap rate.
- The margin over the three year swap rate should be based on normal bank margins for a 3 year committed facility.
- That the rate should be reviewed on a quarterly basis.

4.12 This approach averages out short and long term interest rates, is based on the current market conditions and commercial bank margins.

5 Options

5.1 There are two options:

5.1.1 Option 1 – To adopt the proposed NRSBU Treasury Policy (subject to adoption by NCC). Under this option the management of the treasury operations, including risk management, will be formalised. The proposed policy also removes the need for maintaining separate facilities for the NRSBU.

5.1.2 Option 2 – Status Quo - under this option the current separate arrangements will remain in place and no formal treasury management policy will be in place. NCC will continue to manage the day-to-day activities. This approach is likely to result in a negative comment from the Council's auditors.

6 Strategic Challenges / Risks

6.1 Introducing this formal policy links to Strategic Challenge Two, Financial Stability. This relates to the funding strategy for the NRSBU and the related treasury risk management.

7 Policy / Legal Requirements / Plan

7.1 There is no legal requirement for the NRSBU to have a specific treasury policy. It would however be financially prudent to have this policy in place with appropriate links to the TDC and NCC treasury policies.

8 Consideration of Financial or Budgetary Implications

8.1 There are no direct budgetary implications. The cost of the policy development has been met from existing budgets. The underlying borrowing costs for funding the NRSBU may be reduced as under the proposed policy NCC and TDC will be able to access a mixture of funding sources and not be restricted to bank funding only. The cost of funds to the NRSBU will be market based on the proposed formula. There is the potential for a gap between the

Council cost of borrowing and the charge to the NRSBU to exist. The risk of this is considered to be low.

9 Significance and Consultation

9.1 The decision is considered to be of low significance. As it will not have an impact on residents or ratepayers, formal consultation with the public is not required. A copy of the proposed policy has been provided to the NRSBU Joint Committee. The Committee reviewed the draft policy and adopted it at their January 2014 meeting.

10 Conclusion

10.1 The Council should adopt the proposed Treasury Policy for the NRSBU, subject to its adoption by NCC.

11 Next Steps / Timeline

11.1 On approval, this decision will be communicated to the Chief Financial Officer at NCC and the NRSBU Joint Committee Chair.

12 Attachments

2013

NRSBU Draft Treasury Policy

Version: 1.0, 2 September 2013

Author: Mike Drummond, Group Manager Corporate Services Tasman District Council

Contents

1 Introduction

1.1 Purpose of Policy

The purpose of the Treasury Management Policy is to outline approved policy in respect of all Nelson Regional Sewerage Business Unit (NRSBU) treasury activity, to be undertaken by the Nelson City Council and the Tasman District Council. The formalisation of such policies enables the Treasury risks within the NRSBU to be prudently managed.

As circumstances change, the policies and practices outlined in this document will be modified to ensure the treasury risks associated with the NRSBU continue to be well managed. In addition regular reviews will be conducted to test the existing policy against the following criteria:

1) Industry "best practices".
2) The risk bearing ability and tolerance levels of the underlying revenue and cost drivers.
3) The effectiveness and efficiency of the Nelson City Council and the Tasman District Council Treasury Management Policies and function to recognise, measure, control, manage and report on the NRSBU financial exposure to market interest rate risks, funding risks, liquidity risks and associated risks.
4) The operation of a pro-active treasury management function by the Nelson City Council in an environment of control and compliance.
5) In relation to the NRSBU, the robustness of the Nelson City Council and the Tasman District Council Treasury Management Policies risk control limits and risk spreading mechanisms against normal and abnormal financial market movements and conditions.
6) Assist the NRSBU in achieving strategic objectives relating to its stakeholders.

It is intended that the policy be distributed to all personnel involved in any aspect of the NRSBU's financial management. In this respect, all staff at the NRSBU and at the respective councils must be completely familiar with their responsibilities under this policy at all times.

The governance review and monitoring oversight responsibility rests with the NRSBU Joint Committee.

Day to day treasury management for the NRSBU is carried out by the finance team of Nelson City Council on behalf of both councils.

1.2 Scope

This document identifies the policies of the Nelson City Council, the Tasman District Council and the NRSBU in respect of treasury management activities in relation to the NRSBU. This policy does not override the respective councils Treasury and related Liability Management and Investment policies. Where there is a conflict between these policies the most conservative or lowest limit will apply to the NRSBU.

This policy has not been prepared to cover other aspects of the NRSBU'S operations particularly transactional banking management, systems of internal control and financial management. Other policies and procedures of the NRSBU and council cover these matters. Planning tools and mechanisms are also outside the scope of this policy.

The policy is formally reviewed on a three year basis.

2 Objectives

2.1 Statutory Objectives

2.1.1 All borrowing, investments and incidental arrangements (for example the use of derivatives) will be approved by resolution of the respective councils in accordance with the Local Government Act 2002.

2.1.2 All legal documentation in respect to borrowing and financial instruments will be reviewed by the respective Councils solicitors, prior to tabling of the relevant resolutions.

2.1.3 A resolution of each Council is not required for hire purchase, credit or deferred purchase of goods if:

a) The period of debt is less than 91 days(including rollovers); or

b) 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 the respective councils.

2.2 General Objectives

2.2.1 Manage all of the NRSBU's investments within its strategic and commercial objectives and optimise returns within these NRSBU objectives.

2.2.2 In conjunction with the Tasman District Council and the Nelson City Council, arrange and structure appropriate funding in terms of both maturity and interest rates.

2.2.3 In conjunction with the Tasman District Council and the Nelson City Council, manage the NRSBU borrowing programme to ensure funds are readily available at acceptable margins and costs.

2.2.4 In conjunction with the Tasman District Council and the Nelson City Council, borrow funds and transact risk management instruments within an environment of control and compliance to protect the NRSBU's financial assets and costs.

2.2.5 In conjunction with the Tasman District Council and the Nelson City Council, maintain liquidity levels and manage the overall cash position of the NRSBU operations to meet known and reasonable unforeseen funding requirements.

2.2.6 In conjunction with the Nelson City Council, invest surplus cash in liquid and credit worthy investments.

2.2.7 Avoid adverse interest rate related increases on stakeholder charges and maintain overall interest costs within budget.

2.2.8 Develop and maintain professional relationships with council staff and financial market participants as required.

2.2.9 In conjunction with the Nelson City Council Treasury Team monitor and regularly report on financing/borrowing covenants and ratios applicable to the NRSBU.

2.2.10 In conjunction with the Tasman District Council and the Nelson City Council, ensure that all statutory requirements of a financial nature are adhered to.

In meeting the above objectives the NRSBU and the respective council Treasury management teams recognise that there are financial risks such as liquidity, funding, interest rate, credit and operational risks arising from treasury activities. The NRSBU, Tasman District Council and the Nelson City Council are risk averse entities and do not want to incur additional risk from the NRSBU related treasury activities. Accordingly the Tasman District Council and the Nelson City Council's finance functions, in relation to treasury activities, are a risk management function focused on protecting the NRSBU's budgeted interest costs, stabilising NRSBU cash flows and achieving its capital spend programme. The Councils will seek to prudently manage these risks. Accordingly, activity that is unrelated to its underlying cash flows or that may be construed as speculative in nature is expressly forbidden.

2.3 Borrowing

The NRSBU's borrowing activity is largely driven by its capital expenditure programme. The NRSBU does not borrow in its own name. The Tasman District Council and the Nelson City Council borrow in their name to fund the NRSBU. The funding requirement is generally split 50/50 between the two councils. This borrowing is carried out and subject to the individual councils borrowing policies. Borrowing limits are not expressly applied to the NRSBU and borrowing is funded at the council level like other council activities.

The NRSBU maintains a committed funding facility with Nelson City Council that ensures the achievement of the liquidity ratio and debt funding requirements of the business plan. The liquidity and funding mechanisms are as follows;

- The committed funding facility has a constant maturity term of no less than two years.
- The total committed funding facility must be maintained at an amount of 110% of at least the existing debt borrowing amount.

The interest rate is fixed annually at 1 July and charged quarterly in arrears. The fixed annual rate is set at a margin above the prevailing 3-year market swap rate. The interest rate can be adjusted quarterly if required.

2.4 Investments

The NRSBU does not participate in equity or other investments with the exception of treasury instruments. Nelson City Council manages these treasury investments in accordance with the Nelson City Council investment policy.

3 Management Responsibilities

Day to day treasury management for the NRSBU is carried out by the Nelson City Council on behalf of both councils. This includes regular financial reporting and ensuring compliance with Councils Treasury policies. This management is carried out in accordance with and under the Nelson City Council's policies and procedures.

The NRSBU debt is split evenly and funded by each council separately. This debt is reported and managed as part of each council's activities. This management including risk management is carried out under the respective councils own Treasury Policies.

Approval for the borrowing programme is separately reviewed by each council and approved as part of the Annual Plan or Ten Year Plan process.

9.5 LOCAL GOVERNMENT NEW ZEALAND INSURANCE MARKET REVIEW

Decision Required

Report To:	Corporate Services Committee
Meeting Date:	13 March 2014
Report Author:	Mike Drummond, Corporate Services Manager
Report Number:	RFN14-03-04
File Reference:	

1 Summary

1.1 Local Government New Zealand (LGNZ) has commissioned a local government insurance review. This review was presented to LGNZ prior to Christmas 2013. A copy of the review is included with this report.

1.2 This review made three recommendations:

- Councils should spend more resources on risk profiling, management and mitigation.
- Councils should create a new agency to replace the local authority owned insurers.
- That the current 60/40% natural disaster co-funding arrangement with the crown should be removed to be replaced with a tiered approach (self insurance, commercial insurance and taxpayer support).

1.3 LGNZ has decided to set up a working party to further progress this work. The terms of reference and project scope are currently being worked on.

1.4 It is considered appropriate that Council staff continue to support this work and participate wherever appropriate in the work of the LGNZ working party.

2 Draft Resolution

That the Corporate Services Committee receives the Local Government New Zealand Insurance Market Review Report RFN14-03-04;

3 Purpose of the Report

3.1 To advise the committee on the work being undertaken by Local Government New Zealand (LGNZ) on the insurance market in relation to local authority insurance needs.

4 Background and Discussion

4.1 The Christchurch earthquakes have had a significant effect on the insurance markets and the provision of insurance products and services to councils. All councils have seen major increases in insurance costs, increases in deductibles and reduction in cover levels.

4.2 In August 2013 LGNZ commissioned Craig Stobo to conduct a review of the local government insurance market. Mr Stobo’s report was delivered to LGNZ and considered prior to Christmas 2013.

4.3 Three key recommendations come from the review.

- Councils should spend more resources on risk profiling, management and mitigation.
- Councils should create a local authority owned agency to replace the current local authority owned insurers. This agency would not be an insurance provider.
- The current 60/40 percent natural disaster co-funding arrangement with central government for underground assets should be removed in return for set dollar insurance layers (self insurance, commercial insurance and taxpayer support).

4.4 The LGNZ has established a working party to further assess the case for a “Local Government Insurance Agency”.

4.5 Currently the management of LGNZ is developing a project scope and terms of reference for this working party.

4.6 A copy of the Insurance Market Review is attached to this report. This report is not being widely distributed outside of LGNZ members, Civic Assurance, LAPP, Riskpool and Treasury.

5 Options

5.1 Council may choose to participate or not, as requested by LGNZ. Council participated by providing information for Mr Stobo’s initial review and officers see benefits in responding to future requests.

6 Strategic Challenges / Risks

6.1 The work being carried out by LGNZ is in alignment with the work staff need to do as part of our review of risk management and appropriate insurance cover for Council’s assets. The related Strategic Challenge is Coping with Natural Hazards, although there is a strong link to financial sustainability. There is no risk involved in further involvement with LGNZ on this review.

7 Consideration of Financial or Budgetary Implications

7.1 Any costs of participation or responding to LGNZ requests around this review will be met from existing budgets.

8 Significance and Consultation

8.1 A decision to participate, if requested, in the LGNZ work is of very low significance as it will have no impact on the general ratepayers. For this reason no formal consultation is proposed.

9 Conclusion

9.1 The work programme being developed by LGNZ to review risk management, in particular insurance cover by councils, is timely. Council should continue to participate where requested and officers will report back progress. Depending on the outcome from the working party, new strategies for risk management and mitigation (financial) may be implemented.

10 Attachments

New Zealand Local Government Insurance Market Review

Prepared for Local Government New Zealand

Craig Stobo

We are.
LGNZ.

December 2013

"We can't solve problems by using the same kind of thinking we used when we created them."

Einstein

CONTENTS

Biography
Craig Stobo

Craig Stobo was educated at Waitaki Boys High School (Milner Prize), Otago University (BA Hons First Class in Economics) and Wharton Business School, University of Pennsylvannia (Advanced Management Programme).

He has worked as a diplomat, economist, investment banker and also as CEO and Executive Vice President for BT Funds Management. He Chaired the Government review of the taxation of investment income which led to the PIE managed fund tax regime which underpins Kiwisaver; Chaired the Government review of financial services exports which led to tax changes necessary for New Zealand to become a funds domicile and Chaired the Establishment Board of the Local Government Funding Agency (LGFA) prior to its incorporation on 1 December 2011.

He is currently an independent director and Chair of the LGFA, AIG Insurance New Zealand Ltd, Precinct Properties New Zealand Ltd, and OCG Consulting Ltd.

Craig also has directorship and private equity interests in financial services and other businesses, and provides consultancy services to businesses and the New Zealand Government.

Summary

The Christchurch earthquakes have shaken the provision of insurance products and services to New Zealand local authorities. The business models of the three sector-owned entities Civic, LAPP and Riskpool have been severely tested as a result of this and the leaky homes liabilities. In some cases the latter entities may not survive the current reinsurance arbitration process.

The price and extent of insurance provision for local authorities have changed, created extra costs, and has forced a deeper examination of risk profiles, risk assessment practices and risk mitigation techniques including alternatives to existing risk transfer solutions. Finally, the consequences of weaknesses in co-funding arrangements with the Crown for natural disaster recovery requires a rethink on ratepayer/taxpayer risk sharing.

Despite this turmoil New Zealand local authorities are in a strong position to move forward if they can work together. The underlying principles for options and my recommendation are as follows:

1. In my discussions on insurance it is very clear that the bigger issue for local authorities is their access to skills and expertise to think about and manage risk, not just the purchase of insurance which tends to be the last risk mitigation option.
2. Local authorities face similar sets of asset and liability risks and therefore have enormous opportunities to benefit from economies of scale if they can work together. They should use their asset and liability risk homogeneity and size to their advantage including identifying, owning and leveraging their intellectual property, including seeking innovative products and services for their benefit. Pooling risks doesn't have to mean pooling scarce local authority capital in a local authority-owned insurance company/mutual to fund risk mitigation. Councils have limited capital to insure other councils' misfortunes. Insurance markets are also changing. The key is to think smarter about self-reliant sustainable resilient solutions including the most efficient pathway from local authority needs to stable global reinsurer support.
3. The 60/40 per cent co-funding arrangement with the Crown for underground infrastructure damage caused by a natural disaster has no basis for its formula, incentivises councils to avoid self-reliant risk management outcomes and creates funding uncertainties for both parties. This needs to change.

Options

I have detailed options for change from the status quo in my Review. Three of these options are recommended for their economic sustainability.

The three recommendations

1. Encourage councils to spend more resources on risk profiling, risk management and risk mitigation to improve self-reliance and resilience. Identify, own, share and leverage this information to reduce the costs of poor information.
2. Create a local authority-owned Agency to replace the current local authority owned insurers. It is **not** an insurance provider which competes with insurance companies. It should provide expertise on risk profiling, risk management and risk mitigation. Local authority data is its intellectual property which it must own and control. It uses its exclusive negotiating role and collective buying power to negotiate insurances on behalf of all local authorities but settles via individual contracts. The Agency's balance sheet is therefore "capital light." It actively seeks product, service and insurance contract innovation. It works with Crown agencies such as EQC and GNS. It builds strong global relationships with local and global insurers/reinsurers. It is funded by annual premium-related service fees from councils and the Crown. It is owned by councils and the Crown.
3. The 60/40 per cent natural disaster co-funding arrangement with the Crown for material damage to underground infrastructure is removed in return for set dollar insurance layers comprising self-insurance, commercial insurance and taxpayer support in return for Crown funding assistance for the Agency. This will encourage greater council self-reliance and use of the Agency.

Recommended next steps

Convene a working group meeting of like-minded councils to assess the Agency initiative. Specifically, representatives of all the Local Authority Shared Service (LASS) type entities, plus Auckland, Wellington, Christchurch and Dunedin City Councils. National Council has to be a funding sponsor and champion. If required I would be interested in assisting LGNZ to take the next step.

Terms of reference for the review

1. To analyse and assess the insurance market in New Zealand insofar as it affects the provision of insurance products and services to the local authorities.
2. Provide advice on the state of the market, its conditions and the consequent risks and threats facing local authorities.
3. Analyse and assess local authorities risk profiles and advise on their insurance needs.
4. Advise on the insurance arrangement options available to local authorities.
5. Make recommendations to the National Council of Local Government New Zealand (LGNZ) on actions LGNZ should take or promote to ensure that appropriate and economically sustainable risk protection is in place to protect the interests of local authorities.

Methodology

My methodology involved the following research:

- Meetings with the Crown and Crown agencies to determine the Crown's perspective on local authority insurance. This included The Treasury, Office of the Auditor General (OAG), Department of Internal Affairs and the Earthquake Commission. In particular, the OAG reports "Insuring Public Assets" and "Managing Public Assets" should be read in conjunction with this Review.
- Meetings with selected councils to determine insurance issues from their different perspectives. This included Auckland, Wellington City, Christchurch City, Dunedin City, Queenstown Lakes District, and Waitaki District Councils.
- Meetings with entities that offered insights into different collective insurance business models. This included Health Benefits Ltd (for New Zealand DHBs), and the Australian local authority insurance businesses Statewide Mutual in NSW and Local Government Risk Services in South Australia.
- Meetings with the Chairs of Civic, LAPP and Riskpool. Meetings with the Board of Riskpool and CEO of Civic.
- Meetings in New Zealand and Sydney with all major global insurance brokers and insurers/reinsurers who have had an interest in local authority insurance in New Zealand.
- Meetings with subject matter experts in Australia and New Zealand.

The meetings are listed in Appendix 1.

A survey on insurance was sent to all local authorities for their comments. Thirty eight replied and are listed in Appendix 2. This did not extend to CCOs and is out of scope of this Review. The results are only summarised in this Review due to commercial sensitivities. The survey questionnaire is attached to this Review as Appendix 5.

Research into insurance issues and markets was conducted. The publication "Assuring and Enduring, Fifty Years of Civic Assurance-Tested by Time and Disaster" was excellent background reading.

I am indebted to all participants in this Review for their time, cooperation given freely and frank views. This Review attempts to capture those views. I apologies for any errors or omissions.

My potential conflict of interest as Chair of AIG Insurance in New Zealand was disclosed at these meetings.

Findings

1. To analyse and assess the insurance market in New Zealand insofar as it affects the provision of insurance products and services to the local authorities

The insurance market has changed considerably on several levels over the last few years. This is already well documented in the OAG Report "Insuring Public Assets." I won't repeat their findings here. The following captures issues that lead to this Review's options and recommendations.

a) Undercapitalised insurers have struggled with major event risks such as the Christchurch earthquakes and weathertight homes. ANSVAR has exited the market. AMI has been broken up and sold. LAPP has paid out and is seeking capital contributions. Riskpool only provides insurance now where reinsurance is available. Civic has limited freedom to operate as an insurer with a provisional licence only from the RBNZ due its arbitration with its reinsurers, and a sub-prime credit rating. Note 24 of Civic's 2012 annual accounts discloses the potential solvency issues.

b) Civic's product offering restrictions from 2011 resulted in its clients becoming distressed buyers in a more expensive market. Local authorities have moved to use brokers directly or through regional collective structures to gain access to expert advice and stable commercial insurance.

c) Commercial insurers/reinsurers are demanding more information about insurance risks and being more selective in their offerings.

d) Premiums and deductibles have increased but some stabilisation is occurring now. The global catastrophe environment in 2013 has been benign to date. It is therefore unlikely that there will be premium increases or restrictions in capacity in the reinsurance sector in the near future. Appendix 3 details premiums written by the insurance industry. The OAG report provides more detail on public asset insurance conditions. My survey also indicates the extent of premium increases for local authorities were variable by region and insurance type, with earthquake risk in the Canterbury and Wellington regions being the most problematic drivers of premium change. Finally, there was some deterioration in cover obtained (ie policy exclusions).

e) As a result of premium increases new entrants have come into the market such as Berkshire Hathaway. Despite earlier doubts some councils have been able to get underground infrastructure insurance from global insurers/reinsurers.

f) The Crown has expressed its concerns over the open ended nature of its contingent liability to its 60/40 per cent co-funding of natural disasters under Clause 26 of the Civil Defence Emergency Plan. All councils have expressed a desire for the Crown to continue to use taxpayers' funds to support a natural disaster in their locality. Some councils may unduly rely on their participation in LAPP to access the Crown's funding under this formula rather than pursue sustainable alternatives.

2. Provide advice on the state of the market, its conditions and the consequent risks and threats facing local authorities

State of commercial providers

No major broker or commercial insurer/reinsurer met who is a provider to the sector wishes to pull out. Rather they are or want to be highly engaged and wish to see the sector evolve. Some, such as Berkshire, have entered the market as premiums have risen. Many have insurance capacity and have offered innovative ideas for the sector. As the OAG insurance report outlines, historical patterns show that while insurance costs rise sharply after the event, they also show that, relatively soon after, insurance costs plateau and fall. However, insurance for material damage risks from earthquakes is clearly being repriced. This represents a change from perceived to revealed risk, and can be expected to be a structural feature of insurer risk selection going forward. My view is that commercial capacity and changes to the cost of insurance by themselves do not represent a threat to local authorities' ability to manage risk.

Appendix 4 lists the current RBNZ licensed insurers in New Zealand relevant to the sector.

State of local authority owned insurance providers

a) Civic Assurance

Civic Assurance's financial challenges are clearly laid out on page 42 of the OAG insurance report. The matters referred to by OAG that need to be resolved are detailed in Civic's 2012 Annual Report. It currently has a provisional licence from the regulator RBNZ, has been assigned a sub-prime credit rating and therefore cannot provide the services needed by local authorities. It has attempted to provide insurance via another non-regulated structure but the council survey indicates it has not met with support from members. Its offer of shares to members to recapitalise remains open. Its future is tied to winning the arbitration with reinsurers, regaining a full insurance licence, getting an acceptable rating and recapitalising.

The company's core business is as an insurer. After retained earnings and calls on capital it turns to the global market for reinsurance. In that sense it is like any other local insurer. However, it does have differences. It has paid rebates to premium contributors. Its major asset is Civic Assurance House on Lambton Quay. (The asset does not provide diversification from the risks Civic is attempting to manage in my view). Civic relies heavily on its CEO who is accountable across the three sector owned entities – Civic/LAPP/Riskpool.

Importantly, the insurance market Civic operates in is changing. Commercial insurers are able to provide competitive products and services to local authorities without the need for capital calls. The needs of local authorities are shifting to advice on risk management solutions. Civic is at risk of becoming an undifferentiated insurance provider.

b) The Local Authority Protection Programme Disaster Fund (LAPP)

LAPP's genesis, development and its future prospects are also clearly laid out on page 42 of the OAG insurance report. It is a not for profit non-taxable discretionary mutual charitable trust with Civic Assurance as manager. It commenced operations in response to the Government's shift in 1991 to fund only 60 per cent of affected underground local infrastructure above a threshold laid out in section 26 of the Guide to the National Civil Defence Emergency Management Plan. Eligibility for the 60 per cent is subject to the following:

- "the local authority has adequately protected itself through asset and risk management including mitigation, where appropriate, and the proper maintenance of infrastructure assets; or
- the local authority has made sound financial provisions (such as the provision of reserve funds, effective insurance or participation in a mutual assistance scheme with other local authorities) to a level sufficient to ensure the local authority could reasonably be expected to meet its obligation to provide for its own recovery."

Clearly LAPP has "done its job" (funding the Christchurch rebuild-subject to its insurance payout from Civic), but no local authority expected the scale of the disaster and the size of the LAPP payout. The survey captures concerns over the size of contributions required for the LAPP rebuild, and its discretionary status. Consequently, many members have exercised their rights to withdraw from LAPP next year (while still retaining the option to cancel that right). Members are seeking and getting alternative solutions to LAPP. LAPP's future is therefore not clear.

Currently, if local authorities did nothing else but gain LAPP (or another mutual) membership then the Crown is obliged to fund 60 per cent as per the Guide. In my view, this reduces councils' incentives to consider other risk mitigation solutions. LAPP's current problematic rebuild also means that it is not clear that a member local authority can 'reasonably be expected to meet its obligation to provide for its own recovery." Requests for clarity from the Crown on this by one local authority have met with a response that does not provide any certainty.

It is timely to reconsider why both the Crown and local authorities believe that the 60/40 formula is appropriate following lessons learnt after Christchurch. There is a policy hazard here. If LAPP does provides co-funding security for a council, then both the Crown and LAPP have theoretically unlimited liabilities (ie tied to the unknown size of the next disasters). However, LAPP does not necessarily have the same resources to recapitalise post event as the Crown since it relies on scarce local authority capital before a reinsurance layer. Some councils are just now unwilling to fund someone else's disaster.

c) Riskpool

Riskpool is a mutual liability fund started in 1997. Its genesis lies in councils individually being unable to get liability cover at the right price. Civic owns the shares of the Trustee for Riskpool. Following the court rulings on leaky buildings liability, Riskpool can no longer offer this insurance and its members are on notice for capital calls if required. Riskpool has recently put in place a three year reinsurance programme and does not offer insurance outside of this reinsurance (ie no future council-funded capital layer).

Many councils surveyed do not want to be the "last man standing," have withdrawn from Riskpool and obtained satisfactory insurance from the commercial sector. What was a virtue for some councils with Riskpool (collective risk sharing) has become a collective liability (long tail calls on capital).

While the commercial sector may be meeting liability insurance needs (and without capital calls) they may not be able to advocate for the sector, and ensure that case law does not develop with precedents that adversely affect all councils. Riskpool has played an important role in this regard.

Local authority response

The changes to insurance market conditions have resulted in a number of different responses by local authorities:

- Agreed to accept higher premiums/deductibles/exclusions because the council policy requires full insurance, ie a passive transaction approach;
- Decided to the alter the extent of insurance cover (from full replacement to fire only loss or indemnity or demolition costs); and increased deductibles to keep costs down;
- Expressed unwillingness/uncertainty to support Civic/LAPP/Riskpool. Various reasons have been given including cost, service, a conflicted business model, and the presence of alternative suitable products and services;
- Asked the Crown if LAPP in its current state would meet the eligibility criteria for 60/40 co-funding assistance;
- Moved/moving to source advice/insurance from brokers/commercial insurers directly or through regional collective structures eg Waikato Local Authority Shared Services (LASS), Bay of Plenty LASS, Wairarapa collective, Wellington cooperative, Canterbury CFOs and Top of the South;
- Have commenced reviews of risk management;
- Christchurch City Council announced it was undertaking a formal review of a number of issues related to the Council's insurance led by an independent barrister; and
- LGNZ has commissioned a Review of the Insurance Market for Local Authorities.

Local authority risks and threats

a) Local authority risk management

Local authorities are required to maintain essential services to their communities including the continuous provision of the three waters and roading. The risks that have to be managed are disorderly disruption to essential services and the funding of repair and/or replacement in a timely manner. Councils also have to protect themselves from potential liabilities incurred in performing council services.

Councils do have asset management plans which record the condition of infrastructure and buildings which informs repairs, renewals and therefore future capital expenditure. However my survey indicates that these are recorded in different types of software and in some cases do not link to risk mitigation strategies or depreciation schedules.

Councils do not have uniformly complete policies on their risk appetite, risk management and risk mitigation. They lack resources to consider these issues and may view insurance as the panacea to risk mitigation which is managed in the annual budget negotiation round by confirming that cover is in place at the same or less premium than the previous year. I am very concerned about what councils don't know.

So in some senses this Review has a Terms of Reference which focuses at the last step in the risk mitigation process, ie risk transfer (insurance) when the bigger issue is councils' capacity to consider risk appetite/profiles, risk management opportunities and risk mitigation techniques.

For example, no council surveyed could confirm that they had had a clear mandate with their communities on their appetite for risk. Conversations are needed on what infrastructure is essential to be reinstated first in a disaster setting and therefore should attract priority management and funding today. That might be three waters infrastructure, but not community halls and sports facilities for example.

Secondly, there is a lack of uniform consideration of risk management techniques to reduce risks of asset or service non-performance. Fire alarms, security patrols, refusing to permit unsuitable development, sale and leaseback structures, and asset leasing; or pushing back on legislation which might lead to onerous liabilities for councils are examples of the use of management skills that can reduce risk for ratepayers without paying insurance premiums while still delivering services to communities.

Thirdly, there needs to be consideration of risk mitigation through pre event and post event funding structures which links appetite for risk with asset management plans and councils' balance sheets. This really does build council self-reliance and community resilience to withstand unforeseen shocks. Put simply, once risk management solutions are in place, what resources are required to fund unforeseen damage to assets the community views as essential?

These resources could come from:

- Specific cash reserves for this purpose;
- The sale of assets. The Christchurch City Council public response to the prospect of asset sales has so far been politically difficult. In hindsight that may have been an easier decision if leadership had been able to have a public conversation on broader choices to fund disasters. Councils also need to consider the benefits of asset diversification. Owning assets that are tagged for sale in the event of a disaster that could themselves be subject to the same disaster affecting essential services seems reckless portfolio concentration in hindsight;
- Building spare debt funding capacity (ie councils could fund well within their debt covenants, and/or use LGFA to gain access to the LGFA's AA+ credit rating which builds a contingency for funding disasters); and finally
- Risk transfer ie insurance. But councils could consider smarter consideration of tradeoffs between premiums, deductibles and exclusions, types (ie full replacement, indemnity, fire loss only, demolition costs only),and purchasing recovery cost insurance before asset insurance can be paid out. New ideas for the sector should be considered.

b) Local authority threats

My study of insurance for the sector indicates that threats can be broken down into two types – external and internal.

The external threats could come in the form of more insurance market disruption due to more natural disasters including earthquakes, floods and tsunamis. This disruption could occur due to these events happening in New Zealand or overseas since local premiums are affected at the margin by the global costs of reinsurance. Councils' response should be to put in place risk profiling, risk management and pre event and post event funding mechanisms described above to increase their self-reliance and sustainability. In addition, they need to ensure that they arrange their insurances with strong stable global insurers/reinsurers.

The internal threats relate to the way the sector has organised its sector-owned insurance structures and their own internal processes.

Councils can't currently use Civic when councils' investment policies require a minimum credit rating of A or better from their insurer. The ability of Civic to resume its normal business activities is, according to Civic's directors "uncertain." Fundamentally, as the Notes to the 2012 Financial Statements of Civic state "the resolution of the reinsurance issue is necessary to enable the Company to restore its claims payable rating of A- or better." Furthermore, the Notes state that "the validity of the going concern assumption on which the financial statements are prepared depends, inter alia on limiting the Company's net outstanding claims liability to $6.6m."

It is clear from the survey responses that continued council support for LAPP is uncertain. I am not able to determine what minimum level of membership, and therefore contributions, is required to ensure LAPP is viable. If it is not viable, then councils who have relied on LAPP to meet the eligibility criteria for 60 per cent taxpayer funding of infrastructure disasters will have to seek alternatives. The level of council preparedness for this latter outcome is of some concern."

The Crown is wary about its contingent liability under the 60/40 per cent arrangement, which enables ratepayers to access taxpayer funds when councils could be more self-reliant. The National Council of LGNZ should take this opportunity to renegotiate the sector's relationship with the Crown in the event of natural disasters.

Councils have not put in place processes to consider the full suite of risk management and mitigation options available to them. Possibly councils are therefore over-insured.

The counterpoint to this is that council asset valuations for insurance purposes are estimated on an Optimised Replacement Cost (ORC) under normal operating conditions. However, reinstatement costs are more than ORC following a major disaster. These reinstatement costs include access costs in remote areas, higher labour and material costs, professional fees and claims administration. Possibly then councils are underinsured.

"What concerns me is not the way things are, but rather the way people think things are."

Epictetus

3. Analyse and assess local authorities risk profiles and advise on their insurance needs

As discussed above, my research indicates that council risk profiles/risk appetites are absent or not well documented across the sector. This makes it hard to analyse and assess actual profiles. The important conclusion is that this work needs to be done.

In discussions with large private businesses the identification of risk and elimination or reduction in risk through good management has resulted in much lower insurance costs. However, the following list of insurance types and desire for low deductibles purchased by councils indicates an astonishing breadth of insurable activities and probably a risk averse industry/organisational culture:

- material damage to property (above and below ground);
- crime;
- fine arts;
- forestry;
- forest and rural fire costs;
- standing timber;
- marine;
- motor vehicles;
- employee liability;
- statutory liability;
- public liability;
- general liability;
- trustee liability;
- professional indemnity;
- fidelity guarantee;
- personal accident;
- airport owners and operators;
- hanger keepers;
- harbour masters;
- wreck removal;
- punitive damages;
- contract works;
- hall hirers;
- life insurance;
- business interruption;
- civil defence costs;
- election costs; and
- machinery breakdown.

The list of insurances indicates to me that councils may not be thinking about risk appetite, risk management, and risk mitigation alternatives before seeking insurance. In addition, there needs to be more consideration given to funding the coverage of emergency or reinstatement costs following a disaster. As detailed earlier council officers have expressed concerns to me that their biggest issue is the availability of resources to consider risk and implement cost effective remedies – not just an insurance solution. Third party risk advisors are provided with valuable Intellectual Property (IP) data and are paid for the consequent advice while global insurance brokers are beginning to move from insurance placement to more holistic advice. There is a risk of divide and rule here, where councils are not driving contractual negotiations from a position of IP strength. A local authority supported vehicle with these specialist skills who understands the sector's needs could fulfil this role very effectively.

When choosing insurance, councils need a strong stable insurer or insurers who will honour the insurance contract sum when required for a premium at a reasonable price. Insurers should offer innovations such as rolling reinstatement insurance to provide budget certainty or parametric insurance alternatives. Catastrophe bonds are another potential avenue for risk transfer. Councils do not necessarily want to be in a mutual fund which requires unforeseen capital calls particularly when it funds someone else's disaster. And they do not necessarily want to own an insurance company to deliver stable insurance products.

Councils want great service from specialist claims support management that balances legal support with member input on claims.

Councils need to engage with the Crown and solve the uncertainty over the 60/40 per cent co-funding arrangements for infrastructure damage due to natural disasters. It would be my preference to move away from the 60/40 per cent obligation to an agreed sum insurance tower structure whereby councils self-insure up to a dollar threshold; councils have access to funds/purchase insurance for the next layer based on (for example) maximum probable loss and the Crown agrees to fund the excess top layer. Membership of a mutual such as LAPP should no longer automatically mean eligibility for taxpayer funding. This would assist in incentivising councils to manage their risks.

In return for negotiating this, the Crown would assist in funding local authority risk management.

"Information gaps are filled by premiums."

Chief of Risk, Fonterra

4. Advise on the insurance arrangement options available to local authorities

Local authorities have the following (non-exclusive) options available to them:

a) Self insurance

Councils need to more actively embrace risk profiling, risk management and risk mitigation, including the selection of funding techniques and insurance condition tradeoffs (premiums, deductibles, exclusions). A more detailed review is needed on the current state of the commonality of methodologies of determining asset criticality, asset valuations and its link to risk mitigation including insurance, followed by consistent continuous improvement programmes. This builds self-reliance and resilience.

b) Councils can continue to individually go directly to commercial insurers via local brokers

Councils get tailored solutions, executive accountability and imposes a degree of budgetary discipline. But there is no leverage to drive down premiums, deductibles and exclusions. There is a strong asymmetry of insurance expertise.

c) Regional initiatives to go direct to commercial insurers via brokers

Councils get similar insurance solutions based on their proximate geographic location. There is more leverage from a larger grouping. The asymmetry of expertise is better since councils can invest in skills.

d) Let the current shareholders of Civic, LAPP and Riskpool determine the future of these entities

I have already expressed my views on the challenges that Civic and LAPP now face. Riskpool is now effectively a broker intermediary to global reinsurers.

e) Actively evolve the mutual model

Galvanise the sector to recapitalise Civic, LAPP and support Riskpool but under a single, independently governed and appropriately skilled Board; and reconsider internal vs external management structures. Sell Civic Assurance House.

Statewide Mutual in NSW and the South Australian local government mutual structures have got strong local and/or state government support with elected local government directors to the schemes, and managed by externally managed insurance specialists (Jardine Lloyd Thompson in both cases). These schemes have a strong focus on workers' compensation which is mitigated in New Zealand by ACC. Without the workers' compensation liability schemes the balance of insurance provision for local authorities in Australia is considerably smaller. Like my view on equivalent structures in New Zealand, I believe their members could benefit from skilled independent professional directors who should focus on the value delivered by the manager (eg through monitoring service level agreements in the case of an external solution).

(An iteration of this option is to consider the move of the entity to become a captive insurer in an overseas jurisdiction such as Singapore, where there are attractive incentives to relocate this type of business. This has been discounted as politically unsuitable for LGNZ).

The success of this option then is entirely dependent on New Zealand local authorities willingness to make capital contributions. However, it is difficult for them to assess the future net benefits of membership ie paying potentially lower net premiums than commercial insurers vs potential capital calls. At this stage, I don't believe that enough support will be forthcoming.

f) Change the business model. The Local Government Insurance Agency (LGIA)

Councils should shift their focus from controlling insurance provision through ownership and then competing with insurers, to controlling the ownership of their Intellectual Property (IP) and working with domestic and global insurers. In this case, their IP is their risk profiles, risk management plans and risk mitigation solutions. With control of their data they should use their economies of scale to reduce the costs of risk mitigation solutions as they have successfully done with debt funding through LGFA. If all councils were to delegate risk advisory and insurance contract negotiations to a council-owned LGIA then LGIA could commence using common sector expertise and size to benefit individual councils. LGIA could evolve from the current sector entities Civic/LAPP/Riskpool. Or LGIA could be independent of, or a part of LGFA.

Key risk advisory functions provided by LGIA could include:

- risk assessment/analytics/modelling;
- asset and liability risk register compilation (eg in RMS format for reinsurers understanding);
- placement negotiation (local insurer and overseas reinsurer);
- placement (by type and tenor);
- claims operations; and
- claims advocacy.

According to reinsurance advisory specialist, Guy Carpenter, there are four fundamental components in the pricing of an insurance contract:

- expected loss;
- volatility loading (primarily to allow for the cost of capital);
- expenses; and
- investment returns.

Two of the components – volatility load and expenses – are reduced by increasing the amount of business within a programme. By purchasing insurance for all councils on a combined basis ie a single insurance contract protecting each council, councils receive a technical pricing advantage. In addition, the LGIA would have greater negotiating power, not just on price, but deductibles, reinstatement, and exclusions. Clearly the Agency would have to develop generic standard contracts specific for the sector but endorsed by each council (but that is what occurs now with standard borrowing tenors for councils using the LGFA). And then there is the opportunity to market "NZ Local Authority Inc" risk to strong global insurers and seek innovation.

The LGIA should also look after claims support including legal advice.

LGIA funding should be sourced from an annual pro rata service fee charged to councils for LGIA services and to the Crown. The latter is negotiated as part of the revised 60/40 per cent funding of natural disaster damage of council infrastructure.

The establishment costs of the LGIA company's operations would need to be funded by councils and the Crown, but on-going capital should not be required. Councils should expect a reduction in broking costs as the Agency passes lower negotiated insurance premiums directly from the insurers to councils. Councils should experience a reduction in their staff costs as some risk management/insurance functions shift to the Agency. It is not a profit maximising entity but will need to pay a suitable return to shareholders. Service fee revenues should support on-going operations including staffing and capex for data management.

The LGIA should be owned by councils and the Crown. Councils could operate a Shareholder Council to provide coordinated accountability of the Board of LGIA. The Board's directors should be a majority of skilled independent directors. Management could commence with a transparently priced external management model initially with a view to bringing it eventually in-house. Management skills need to be world class and globally credible. The risk data must be owned and controlled by the LGIA.

"There are no shortcuts to any place worth going."

Beverley Sills

g) Natural disaster funding

Make membership of LAPP/council mutuals no longer a condition for Government infrastructure disaster funding. Change funding from 60/40 per cent of loss funding formula to towered dollar limits. The first layer of the tower is council self-insurance, the second layer is commercial insurance (LAPP is classed as a commercial provider) and the top layer is Government funding uncapped. However, the layer thresholds are dollar limits, tied to (for example) advice on maximum probable loss. This incentivises councils to manage their risks and the caps may generate more capacity/lower prices from commercial insurers for councils.

5. Recommendations to LGNZ

In making recommendations to the National Council of LGNZ, on actions LGNZ should take or promote to ensure that appropriate and economically sustainable risk protection is in place to protect the interests of local authorities, I recommend that National Council canvas support from its members for options a), f) and g) above. This must be run in conjunction with option d). National Council must have a contingency plan in place if option d) fails.

Specifically convene a working group meeting of like-minded councils to assess the Agency initiative. Specifically representatives of all the LASS-type entities, plus Auckland, Wellington, Christchurch and Dunedin City Councils. National Council has to be a funding sponsor and champion. If required, I would be interested in assisting LGNZ to take the next step.

Appendix 1:
Insurance industry meetings

- The Treasury, Wellington
- Office of the Auditor-General, Wellington
- Department of Internal Affairs, Wellington
- EQC, Wellington
- Jardine Lloyd Thompson, Auckland
- Jardine Lloyd Thompson, Sydney
- Berkshire Hathaway, Sydney
- Guy Carpenter, Sydney
- PWC, Auckland
- Fonterra, Auckland
- Risk Management Partners, Sydney
- Willis, Auckland
- Highfield Group, Auckland
- Aon, Auckland
- Marsh, Auckland
- Crombie Lockwood, Auckland
- Munich Re, Auckland
- Munich Re, Sydney
- Insurance Council of NZ
- IAG NZ
- Vero Liability Insurance
- Lumley Insurance, Auckland
- AIG NZ, Auckland
- General Re, Auckland
- QBE, Auckland
- Chair of Civic Assurance
- Chair of Riskpool
- Chair of LAPP
- Board of Riskpool
- CEO of Civic Assurance
- Auckland Council
- Wellington City Council
- Christchurch City Council
- Waitaki District Council
- Dunedin City Council
- Queenstown Lakes District Council
- Lloyd and Partners, London
- Health Benefits Ltd, Auckland
- Statewide, Sydney
- Local Government Risk Services, Adelaide

Appendix 2: **Local authority insurance survey**

Responses to the survey were received from the following councils:

- Ashburton District Council
- Auckland Council
- Bay of Plenty Regional Council
- Central Hawke's Bay District Council
- Clutha District Council
- Environment Canterbury
- Greater Wellington Regional Council
- Hamilton City Council
- Hastings District Council
- Hawke's Bay Regional Council
- Kawerau District Council
- Marlborough District Council
- Masterton District Council
- Napier City Council
- Nelson City Council
- New Plymouth District Council
- Opotiki District Council
- Otorohanga District Council
- Palmerston North City Council
- Selwyn District Council
- Stratford District Council
- South Taranaki District Council
- South Waikato District Council
- South Wairarapa District Council
- Tasman District Council
- Tauranga District Council
- Thames-Coromandel District Council
- Timaru District Council
- Upper Hutt City Council
- Waikato Regional Council
- Waimakariri District Council
- Waimate District Council
- Waipa District Council
- Wanganui District Council
- Wellington City Council
- West Coast Regional Council
- Whakatane District Council
- Whangarei District Council

Appendix 3: **Insurance Council of New Zealand insurance premium statistics**

Gross written premiums by business class, $m, years to September.

	2008	2009	2010	2011	2012
Commercial	441	464	469	502	590
Domestic	766	840	933	1052	1170
Motor	1159	1210	1266	1340	1355
Marine	108	114	126	120	144
Liability	267	280	298	314	340
Earthquake	207	213	220	350	549
Other	306	283	297	296	303
Total	3260	3417	3604	3980	4449

Appendix 4: **Relevant RBNZ licensed general insurers** (rated A or better)

- AA Insurance Ltd
- ACE Insurance Ltd
- AIG Insurance New Zealand Ltd
- Allianz Australia insurance Ltd
- AMI Insurance Ltd
- Berkshire Hathaway International Insurance Ltd
- Farmers' Mutual Group
- IAG New Zealand Ltd
- Lloyd's of London
- Lumley General Insurance (N.Z.) Ltd
- Mitsui Sumitomo Insurance Company, Ltd
- QBE Insurance (International) Ltd
- The New India Assurance Company Ltd
- Tokio Marine & Nichido Fire Insurance Company Ltd
- Vero Liability Insurance Ltd
- Vero Insurance New Zealand Ltd
- Zurich Australia Insurance Ltd

Appendix 5: **Survey**

A view from councillors/your community

1. The Office of the Auditor General New Zealand recently published a paper on "Insuring Public Assets." They stated that there were several questions on councils' risk assessment capabilities that were of interest to them.

With this background in mind, does your council have an asset and liability risk management policy which inter alia sets out the council's risk "appetite" and whether and how the council's risks might be mitigated by solutions such as insurance?

Yes / No

If **yes**, please attach the policy.

If **no**, is there any other council guidance?

A view from Government

2. The Crown has a contingent liability tied to the 60/40 per cent formula for funding the replacement of local authority underground and certain flood protection assets should they be materially damaged.

What do you believe is your council's obligation in order to be eligible for the Crown's 60 per cent share of any potential damage to these assets?

Should the Crown continue to maintain their 60 per cent commitment?

Asset Insurance

3. **Do you have an up-to-date inventory of council assets, including where appropriate their age and maintenance schedule, and renewal programme?**

Yes / No

If **yes**, what is the management information system that holds these records?

If **yes**, does the inventory record whether assets should not be insured, self insured through available working capital/dedicated reserves, debt funded at the time of damage, insured or require the use of other risk mitigation solutions?

4. **Does this asset inventory information link to a depreciation schedule which is summarised in your council's annual accounts?**

Yes / No

5. **Do you insure below ground and flood protection infrastructure?**

Yes / No

If yes, with whom do you insure below ground infrastructure?

If no, are you satisfied that your council is eligible for the Government's 60 per cent contribution to make good in the event of damage to your below ground infrastucture?

6. **What is the ratio of your above ground assets/total assets?**

7. What is the ratio of your insured/not insured above ground assets?

8. What are your reasons for not insuring assets?

9. What was the largest fire and general insurance claim paid out to you in the last ten years, and what risk did it insure?

10. How does your council implement asset insurance cover?

☐ Directly with a private insurer

☐ Using a broker

☐ CIVIC

☐ LAPP

☐ Other

11. Please state why you implement this way.

12. Please describe your views on recent insurance market conditions as they have affected council insurance needs. This might include a description of changes in premiums, deductibles, renewals, or contract terms; or how it has affected whether the council has changed its insurance cover.

Local government insurance sector entities – Civic

13. **Please state which of the following applies to you**

- Your council is a shareholder of Civic

Yes / No

- Your council currently uses Civic for its fire and general insurance needs

Yes / No

If not, why not?

- You have recommended/will recommend to council to commit to recapitalise Civic

Yes / No

Local government insurance sector entities – LAPP

14. **Please state which of the following applies to you**

- Your council will commit to rebuilding LAPP

Yes / No

If not, why not?

Liability insurance

15. What types of liability risks have you insured in the past year?

16. What types of liability risks do you not insure?

17. What is the largest liability insurance claim paid to you in the last ten years and what risk did it insure?

18. How does council implement public liability insurance?

- ☐ Direct with a private insurer
- ☐ Using a broker
- ☐ Riskpool

19. If you do not use Riskpool for liability insurance, please describe why not?

Other insurance

20. Please describe other insurances taken out and why?

Collective procurement

21. Do you confer/work with other councils on insurance procurement practices?

Yes / No

If so, with whom or in what forums?

Resourcing

22. What full time equivalent council staff work on:

- Risk assessment analysis and risk mitigation?

- Insurance needs identification, procurement and monitoring?

The Future

23. If you could make changes to Civic, LAPP and Riskpool what would they be?

24. Is there a role for local government collective insurance vehicles?

Yes / No

Why?

25. Other thoughts on insuring local government's needs?

Item 9.5

Attachment 1

We are.
LGNZ.

Civic Assurance House
114-118 Lambton Quay
Wellington 6011

PO Box 1214
Wellington 6140
New Zealand

P: 64 4 924 1200
www.lgnz.co.nz

Item 9.6

9.6 ELEMENTS OF A REVISED FINANCIAL STRATEGY

Information Only - No Decision Required

Report To:	Corporate Services Committee
Meeting Date:	13 March 2014
Report Author:	Mike Drummond, Corporate Services Manager
Report Number:	RFN14-03-05
File Reference:	

1 Summary

1.1 The current financial strategy was developed as part of the 2012-22 Long Term Plan. That strategy was subject to adverse comment by the Auditor General due to Council's high reliance on debt funding. Concern at the Councillor, community and central government level has also been expressed over the current and projected Council debt levels.

1.2 As part of addressing the Financial Stability Strategic Challenge, staff are proposing a different approach to setting the financial strategy for the 2015-22 Long Term Plan. That approach involves setting a fiscal envelope prior to engaging in the review of the Council's asset/activity management plans. This approach will involve the level of service and investment decisions being made earlier in the process, alongside community affordability.

1.3 The proposed focus will be to limit investment (debt) to those areas that provide core infrastructure. This core infrastructure must demonstrate the ability to support growth, the local economy, environmental stewardship and a lifestyle/sense of place. All this primarily within the Tasman District.

1.4 In the preliminary work we have identified 13 elements for possible inclusion in the revised financial strategy:

- Assigning a whole-of-Council fiscal envelope at the start of the LTP process
- Minimising the level of capital works while focusing investment in core infrastructure
- Ensuring the cash funding of all the operational aspects of capital projects
- An initial focus on debt repayment
- Channelling all operational savings into debt reduction
- Strategic cost reduction
- Modest, but continuing, rates increases above the CPI inflation rate
- Reduction in the number of loans with 40 year terms
- A move to fully funding depreciation
- Asset sales to fund future strategic capital investments
- Reducing the reliance on debt by combining high levels of prefunding, and community fundraising for community infrastructure assets
- A review of Council's ability to fund cross-boundary (TDC/NCC) activities
- Improving financial literacy across the organisation and with Councillors

1.5 This paper is intended to socialise these approaches and for Councillors to indicate support or otherwise for each potential element of a revised financial strategy.

Item 9.6

2 Draft Resolution

That the Corporate Services Committee receives the Elements of a Revised Financial Strategy Report RFN14-03-05.

3 Purpose of the Report

3.1 To update the Committee on the likely direction and the elements to be considered for the 2015-25 Long Term Plan Financial Strategy.

4 Background and Discussion

4.1 The current financial strategy was developed as part of the 2012-22 Long Term Plan. This strategy was subject to adverse comment by the Auditor General, but the Audit report on the Long Term Plan was not qualified.

4.2 The Auditor General commented that the strategy, which relied on extensive borrowing and not funding depreciation, was a high risk approach. She also noted that as a result Tasman was incurring interest on renewals funding which other councils were not. The high projected debt levels were also of concern as they reduced Council's ability to deal with the unexpected, such as increased interest rates, lower growth, a disaster, or unexpected asset failure.

4.3 Councillors and the public have indicated that they are not comfortable with the current or proposed levels of debt. The challenge is that while addressing the debt issue we also need to ensure that rates overall remain affordable for the community as a whole.

4.4 This discussion paper does not address the overall funding of capital and renewals; this is a work in progress that will inform the final financial strategy. It is important however that Council is aware of the elements of a revised strategy being considered as they will form the basis of the fiscal envelope which is the forerunner to the development of revised asset and activity management plans (AMPs).

4.5 It is assumed that the focus will be to limit investment (debt) to those areas that provide core infrastructure and support core services. This core infrastructure must demonstrate the ability to support growth, the local economy, environmental stewardship and a lifestyle/sense of place. All this within the Tasman District (with perhaps one or two exceptions).

4.6 The elements being proposed for the revised financial strategy are based on business as usual, that is Tasman District Council continuing as an independent entity. This means that the focus is on the medium and long term.

4.7 A financial strategy based on placing Tasman District ratepayers in the most advantageous position under an amalgamation scenario with Nelson City Council would be dramatically different. That strategy would have a very short term focus. This is because in amalgamation proposals pre-amalgamation debt is usually funded from TDC ratepayers, not the combined ratepayers of a new local authority. Such a proposal could include approaches like deferring debt funded capital expenditure, major asset and investment sales, sale and lease back of municipal buildings and the rundown of all reserves with the cash released used to reduce current debt levels.

4.8 The importance of indicating the fiscal envelope prior to commencing work on the AMPs for the 2015-25 Long Term Plan cannot be understated. It is difficult to retrofit a financial strategy after the AMPs have been completed as key decisions and trade-offs have already been made.

4.9 Taking the proposed approach will mean Council will need to address the hard decisions on levels of service and investments in infrastructure during the AMP development and not at the end of the process when the draft financials are prepared.

4.10 Attachment one is the Financial Stability Road Map. This diagram illustrates the financial framework under which it is proposed that the LTP be developed. From this diagram you can see where the financial strategy fits into the overall approach to the long term and annual plans. In this diagram the Financial Strategy is referred to as the “Financial Sustainability Strategy”. The key focus under the strategy is financial sustainability.

4.11 The financial strategy is key to two main streams of work:

- The Funding Strategy
- The Investment Strategy

4.12 **The Funding Strategy** – this revolves around the Revenue and Financing Policy that determines the incidence of rates and, indirectly, income risks and levels of service. The Revenue and Finance Policy, in conjunction with the Investment Strategy will determine both the level and incidence of rates and Council’s debt levels.

4.13 **The Investment Strategy** – this Strategy deals with asset management plans, growth and levels of service. A key output of the Investment Strategy is Council’s capital expenditure programme.

4.14 The Commercial Subcommittee has requested a changed approach for the commercial and semi-commercial activities financial strategy within their portfolio. This involves them being treated as a group and allowing the profits from one activity to be used to fund the other activities (including capital programmes). The group as a whole, rather than individual activities, would then pay an internal dividend to Council. This would address the deferred investment in, and cash stripping of, these activities.

4.15 The 13 key elements being proposed for a revised Financial Strategy are:

- Assigning a whole of Council fiscal envelope at the start of the LTP process
- Minimising the level of capital works while focusing investment in core infrastructure
- Ensure the cash funding of all the operational aspects of capital projects
- An initial focus on debt repayment
- Channelling all operational savings into debt reduction
- Strategic cost reduction
- Modest, but continuing, rates increases above the CPI inflation rate
- Reduction in the number of loans with 40 year terms
- A move to fully funding depreciation
- Asset sales to fund future strategic capital investments
- Reducing the reliance on debt by combining high levels of prefunding, and community fundraising for community infrastructure assets
- A review of our ability to fund cross-boundary (TDC/NCC) activities
- Improving financial literacy across the organisation and with Councillors.

4.16 **Assigning a whole-of-Council fiscal envelope** – This approach assists in ensuring that the discussions around asset and activity plans and levels of service are better focused on what the community can afford. The overall Council fiscal envelope will need to then be allocated across all activities. That allocation will not be even as some activities are likely to be prioritised higher than others.

4.17 A key element of the fiscal envelope will be a limit on the capital expenditure programme. The proposal is to set an initial level of capital expenditure at a maximum of 1.5 times the year's depreciation. All other things being equal, a level of 1:1 should cover renewals. The additional .5 is for growth and level of service (LOS) increases. This approach will allow the cap to increase as Council's asset base increases. At current asset levels that would cap the capital programme at $29 million per annum. On its own, this measure is insufficient to address the steep increase in debt that is occurring. It needs to be combined with other measures that reduce the debt-funded portion of the capital programme.

4.18 The other key component of the fiscal envelope is acceptable rates increases. Given current debt levels and Council's exposure to interest rate movements, rates increases above the level of CPI are inevitable. The current practice of allowing a growth component (1.3%) on top of the underlying movement is supported. Setting an initial limit on acceptable rates increases will discipline both the capital and operational programmes.

4.19 The Reserve Bank NZ (RBNZ) current target range for inflation is 1%-3%pa. Historical evidence supports the view that CPI runs at 0.7% pa above the mid-point of the RBNZ's target range. That would support a 2.7% pa basis for CPI movements. Combining a modest increase in rates with this basis would suggest an initial limit on rates increases of 3.7% plus growth of 1.3%. Setting a limit at this level will place considerable pressure on activity and asset managers to contain and reduce operational costs through a range of measures.

4.20 **Minimising the level of capital works** – in order to meet the financial expectations set by the fiscal envelope there will be little new capital work. The public have seen large investments in community and infrastructure assets in the last 15 years. A campaign will be required to communicate Council's financial position and the reason for the minimal level of capital works. A key aim of this campaign will be to lower public expectations.

4.21 **Ensure cash funding of the operational aspects of capital projects** - Council has, in the past, loan funded feasibility and investigation costs. This practice of treating operational costs as capital and therefore loan funding them has been subject to negative auditor comment over several years.

4.22 The budgeting approach for the capital programme needs to change with each major capital programme having a related operation project to cover investigation and feasibility costs. This approach will increase operational costs. These increases will put additional pressure on the fiscal envelope. The result should be earlier prioritisation of projects (as they compete for a limited operational budget) and earlier decision to continue, modify the scope, defer or abandon a capital project.

4.23 **Initial focus on debt repayment** – a strong focus on debt repayment in the first half of the next LTP will be necessary to create enough head room within the borrowing programme to accommodate the reduced capital programme.

4.24 **Channelling all operational savings into debt reduction** – rather than channelling operational savings into reduced rates/charges increases, the savings will need to be channelled into reducing existing debt. At the same time a renewed focus on Council's non-rates income streams with a view to maximising income from these will occur. These two approaches will need to be managed while keeping rates increases within the agreed fiscal envelope. Given that operational savings/income increases will not be made evenly over the Council's diverse operations, there is likely to be changes within the incidence of rates even where the overall rates income increase is kept within the level set by the fiscal envelope.

4.25 **Strategic Cost reduction** - this involves cutting costs without killing the business. The focus here for management is to build in medium- and long-term permanent cost reductions, rather than short-term cost deferrals. This should be one of the outcomes from addressing Strategic Challenge One – Service to Customers and Citizens, theme one "Delivering Business Process Improvements". It should also flow out of decisions as to what levels of service are affordable to the community.

4.26 **Modest but continuing rates increases** - as noted above, limiting rates increases to the movement in the CPI is not likely to allow Council to meet its commitments to the community. Therefore a level of rates increases above the CPI movement is expected. The approach will be to step-in changes over time and so avoid, as far as possible, large increases in rates in any one year. That is not to say that the current incidence of rates will not move significantly for some groups of ratepayers in a particular year as a result of spending priorities and where savings have been made.

4.27 **Reduction in the number of loans with 40 year terms** – much of the debt incurred in funding community facilities has been funded over 40 years. The financial impacts of such a long term are a reduction in immediate costs, but a significant increase in overall costs. The total costs of a loan-funded asset as a multiple of the cash price are:

- 10 year loan – 1.44 times the cash price
- 20 year loan – 1.84 times the cash price
- 30 year loan – 2.24 times the cash price
- 40 Year loan – 2.64 times the cash price

4.28 The cost of reducing all 40-year loans to 20 years would be in the order of $1.3m per annum in additional income required to meet higher principal payments. There would however be increasing savings in interest costs over time. This is not possible in one step so the financial strategy would see progressive reductions in loan terms funded through a steady increase in the district and shared facilities rates.

4.29 Paying back borrowings earlier also has the advantage of creating additional headroom in the borrowing programme. Over time this would allow new projects to be loan funded. At this time the financial strategy should concentrate on reducing debt.

4.30 **A move to fully funding depreciation** - depreciation is a measure of the loss of service potential of an asset, ie a measure of the wearing out of the asset. In the 1990s the approach was not to fund depreciation on infrastructure assets as they were being maintained in perpetuity. These maintenance costs were treated as operational and met from operational income. In 1999 the Auditor General released a discussion on funding for depreciation. In that paper the Auditor General noted that the primary driver of funding depreciation was to ensure that the users pay the cost of the service. The impact of fully funding depreciation was significant rates increases for councils in the early 2000s. Tasman chose not to take this path. This, combined with the current financial strategy that has capital and renewals loan funded, has been a key driver of the steeply increasing debt levels.

4.31 Depreciation is currently $20 million per annum. A move to fund depreciation will not increase Council costs by this amount. This is because of two factors. Not all depreciation is funded and the income from funding depreciation can be used to make principal repayments on loans, along with funding renewals.

4.32 The impact of fully funding depreciation will not fall evenly across Council. Activities with significant assets will bear the majority of the cost increase. That being said, the ability to use income from depreciation to fund principal repayments on the activities capital loans will lessen the stepped increase in costs. This is because we are already treating interest and principal repayments on loans as operational costs.

4.33 **Asset sales to fund future strategic capital investments** – Council has investments in significant assets. The sale of non-core assets to fund strategic capital projects needs serious consideration. The preparation for, and timeframe to achieve asset sales makes them part of a medium term strategy. Forestry interests, the Airport and Port Nelson are major assets that Council has an interest in. A reduction in Council's involvement, say through the introduction of third party equity, would release cash to reduce debt or fund the capital programme. It should be noted that Council receives good income streams from these investments. This income would be affected by any sale and that in turn would have an impact on general rates.

4.34 **Improving financial literacy** across the organisation and with Councillors – this ongoing project is designed to improve the quality of decision-making. It will also lead to a better understanding of both the cost drivers for activities and revenue opportunities.

4.35 **Reducing the reliance on debt by combining high levels of pre-funding, and community fundraising for community assets** – The current strategy of having communities fund 20% of the cost of new community facilities, with the balance being loan funded came out of better economic times when Council was not facing the fiscal challenges it is now. We need to reduce this high level of reliance on debt to fund community facilities.

4.36 The opportunity here is to prioritise grants to where they substantially leverage other party investments in Tasman District into core infrastructure that demonstrates the ability to support growth, the local economy, environmental stewardship and a lifestyle/sense of place.

4.37 One way to do this is to change the approach. The revised financial strategy is likely to recommend a 1/3rd, 1/3rd, 1/3rd approach. Under this approach the community will need to fundraise for at least 1/3rd of the capital costs of a facility. Capital rating will commence prior to the building of the facility and be set to prefund 1/3rd of the capital cost. The final 1/3rd of the costs will be loan funded. Pre-funding will also contribute to reducing or removing the increased rates that occur once a facility is built. These increased rates are to meet operating costs and loan repayments. The aim of this approach is to better leverage community investment, not to replace it.

4.38 **A review of our ability to fund cross-boundary (TDC/NCC) activities** – We currently have substantial investments and obligations for cross boundary activities with NCC. We need to refocus our spending to meet the current financial constraints. That focus should be for activities delivered in the Tasman District. With its lower debt levels and primarily urban population base, NCC is better positioned to support activities, including regional facilities, delivered within its geographical boundary.

4.39 It should be noted that Council undertakes a number of regional council activities for NCC. These are charged on a full cost recovery basis to Nelson City Council. Regular reviews of these activities and charging to NCC needs to be undertaken. It may be that consideration needs to be given to providing these services on a commercial basis rather than just on a cost recovery basis.

5 Options

5.1 Council will be asked to adopt and consult on a revised financial strategy as part of the 2015-25 Long Term Plan. Council will have the option of including one or more of the above elements into that policy.

6 Strategic Challenges / Risks

6.1 Developing a new financial strategy is essential to meeting Strategic Challenge Two – Financial Stability. There is a clear risk that a failure to meet this challenge may create the opportunity for central government intervention in the running of the District, along with increased pressure for amalgamation with NCC.

7 Policy / Legal Requirements / Plan

7.1 The Local Government Act 2002 requires Council to develop, consult on, and follow a formal financial strategy. This paper is for information and discussion purposes. As part of the formal processes for the development of the 2015-25 Long Term Plan, Council will consider and adopt a revised financial strategy.

8 Conclusion

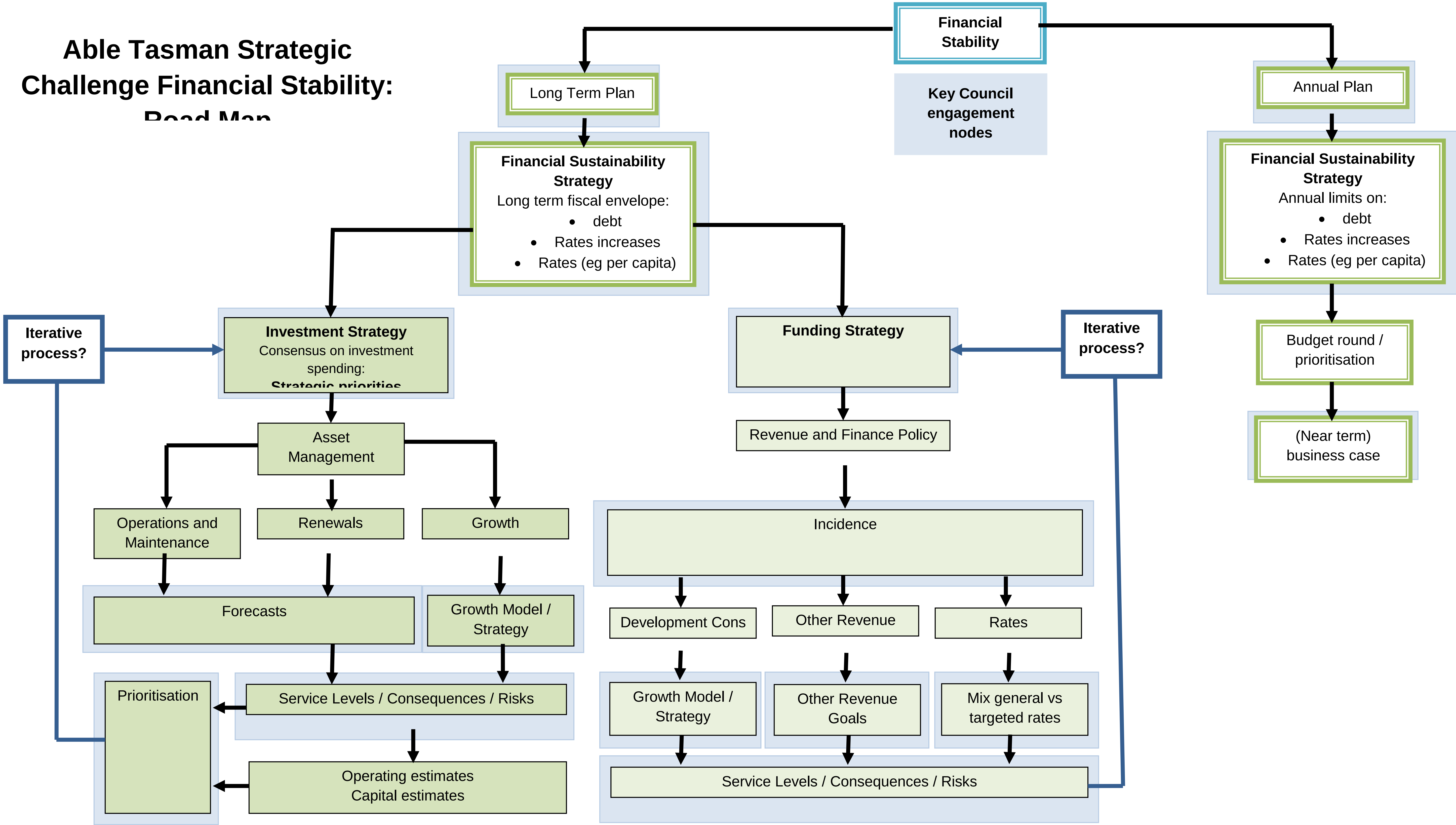
8.1 To address the concerns raised over the current Financial Strategy, Council needs to revise that strategy. Agreeing to key elements of a revised strategy and therefore an initial fiscal envelope prior to engaging in the review of asset management plans is essential to achieving the change required.

9 Next Steps / Timeline

9.1 Following discussion with Councillors, these elements will be included in a draft financial strategy.

10 Attachments

Able Tasman Strategic Challenge Financial Stability: Road Map



Item 9.7

9.7 HUMAN RESOURCES UPDATE REPORT

Information Only - No Decision Required

Report To:	Corporate Services Committee
Meeting Date:	13 March 2014
Report Author:	Joanna Cranness, Human Resources Manager
Report Number:	RFN14-03-02
File Reference:	

1 Summary

1.1 The number of staff (head count) as at 31 December 2013 is included in this report. The full time equivalent (FTE) has increased from 227 (June 2013) to 228.5 and an explanation is provided.

1.2 We are continuing to attract experienced and qualified applicants, and recent staff appointments are included in the report.

1.3 The biennial review of our Human Resources Policies has been completed and the biennial review of the Pandemic Business Continuity Plan has commenced.

1.4 The year-to-date salary expenditure is slightly over budget and this is currently being analysed by the finance team. Some of the factors contributing to this are new positions that are being funded by savings from other budget lines, additional unbudgeted hours being worked by part-time staff, and the timing of provisions being released from the balance sheet to cover outstanding leave and retirement gratuity payments to staff leaving our employment. The finance team will continue to closely track salary costs and provide regular reports to the Chief Executive.

2 Draft Resolution

That the Corporate Services Committee receives the Human Resources Update Report RFN14-03-02.

3 Purpose of the Report

1. The purpose of the report is to update the Committee on Human Resources activities from 1 September 2013 to 28 February 2014.

4 Staff Numbers

4.1 Staff numbers as at 31 December 2013:

	Full Time	Part Time	Casual	Fixed Term
Community Development	45	34	2	2
Corporate Services	33	2		2
Engineering Services	38	2		
Environment & Planning	75	15	1	1
Office of the Chief Executive	3	1		1
Actual = 257 **FTE = 228.5**	**194**	**54**	**3**	**6**

4.2 Staff numbers for the year ending June 2013 were a head count of 254 staff which equated to an FTE of 227.

4.3 The increase is due to two additional part-time staff in Building Control and a part-time fixed term staff member in Biosecurity whose agreement subsequently ended in January 2014.

4.4 A full report of staff number statistics is prepared annually and reported at the August Corporate Services Committee meeting.

5 Recruitment

5.1 General commentary on the ongoing success of our recruitment was reported by the Chief Executive at last week's Full Council meeting.

5.2 During the past four months the following appointments have been made:

- Senior Management Accountant (Matt McGlinchey commenced 10 February 2014)
- Revenue Accountant (Kelly Kivimaa-Schouten commenced 17 February 2014)
- Water Resources Officer
- Management Accountant (Lisette Taylor)

6 Staff Policies Review

6.1 The biennial review of all Human Resources Policies has been completed and they are with Lindsay McKenzie, Chief Executive for his final approval.

6.2 There are currently 45 policies that cover a range of employment, health and safety, and well-being aspects associated with New Zealand legislation and the Council being a good employer.

7 Pandemic Business Continuity Plan Review

7.1 The biennial review of the Pandemic Business Continuity Plan has commenced and will be completed by April 2014.

7.2 The purpose of the Plan is to set out the Council's internal response to managing the health of our staff in the event of an influenza pandemic occurring and minimising it affecting the services we provide.

8 Year-to-Date Salary Expenditure

8.1 Total salary expenditure for the 7 months to January 2014 is slightly over budget. The finance team is currently carrying out a more detailed analysis of this variance.

8.2 Some factors already identified are new positions in the finance team which will be funded by savings from other budget lines, part-time staff working additional unbudgeted hours due to section workloads or to cover for extended leave taken by other staff, and outstanding leave and/or retirement gratuities (from grandfathered contract provisions) paid to staff leaving our employment. Leave and retirement payments are normally accrued. Finance staff are checking that appropriate provisions have been released from the balance sheet to cover these payments.

8.3 There is an expectation that some activity areas will reconcile this against increased revenue from fees and charges or against reduced consultancy costs.

8.4 The finance team will continue to closely track salary expenditure and provide regular reports on this to Lindsay McKenzie, Chief Executive.

8.5 Mike Drummond, Corporate Services Manager will provide a verbal update at the meeting of the analysis completed to date.

9 Attachments

Nil

9.8 FINANCE ACTIVITIES

Information Only - No Decision Required

Report To:	Corporate Services Committee
Meeting Date:	13 March 2014
Report Author:	Russell Holden, Finance Manager
Report Number:	RFN14-03-06
File Reference:	C753

1 Summary

1.1 This report contains financial information, at a Council-wide position, for the year to date period ended 31 January 2014.

1.2 We continue to progress producing monthly financial reports utilising electronic purchase orders, and drawing the data from Confirm and RAMM databases. Now that the first target of 15 working days is the norm, focus moves to further enhancing processes across Council to continually reduce this timeframe over the remainder of the year.

1.3 At 31 January 2014, year-to-date accounting income was $4.9 million ahead of budget, and expenditure was $1.6 million above budget. The net position is an accounting surplus of $6.3 million, against a year-to-date budget surplus of $3.1million. The underlying operational result was a surplus of $565,000 once the non-cash items of Vested Assets and the Fair Value gain have been removed. Staff are working towards completing a “balanced budget” report, which will exclude all non-cash items and capital funding items, and more clearly present the cash position of Council.

1.4 This is a significant positive variance to budget which is mainly the result of:

(a) Accounting adjustments

- The very sizeable ($3.1million) unrealised gain on Interest Rate Swaps;
- The gain on sale of property and vehicles $110,000;
- The loss on sale of $158,000 in relation to the Golden Bay Medical Centre grant;
- Vested assets at $2.2 million, is lower than the budgeted year to date $2.7 million, and

(b) Cash movements

1.4.1 A positive variance in Development and Financial Contributions of $850,000 mostly through activity in Richmond; and

1.4.2 The early arrival of some grant funds.

1.5 The following items are contributing to the expenditure position:

1.5.1 Within the maintenance costs there is $4.2 million of emergency works expenditure. As this is significantly over the NZ Transport Agency (NZTA) approved budget, a request to increase the budget has now been approved by NZTA; and

1.5.2 Legal costs are up primarily as a result of the resource consent activity, land acquisition, Jackett Island costs, and the unbudgeted purchase of the Kina Reserve; and

1.5.3 There is currently a saving on budgeted consultants fees of around $600,000; and

1.5.4 There is also reduction in expenditure for charges from the Nelson Regional Sewerage Business Unit.

1.5 Council's working capital position as at 31 January 2014 was ($1 million) compared to the year-end projection of ($4.4 million).

2 Draft Resolution

That the Corporate Services Committee receives the Finance Activities Report RFN14-03-06.

3 Financial Comment January 2014

3.1 The team remains focused on further improving the timeliness of Council's financial reporting to Council, the Senior Management Team, and budget holders. The use of commitments from; purchase orders, Confirm, job costing and RAMM to populate the data fields in NCS is now normal practice, which is currently under continued refinement.

3.2 To further gain the benefits of the systems and better processing, further training of budget holders to improve their financial literacy will be provided. There is a higher level of the detail provided within the reporting module, with details of the actual work being captured, rather than a simple contract number. This will assist in identifying variances and the related cost drivers.

3.3 As reported previously the phasing of budgets to more accurately match the timing of both income and expenditure items continues to be refined, as budget holders become more aware of the new system's capabilities. The goal is to provide more rigour around the actual-to-budget analysis, which will provide early indications of areas to monitor more closely. The focus then becomes more on the year-to-date actual position and how this compares to budget expectations, rather than only as a percentage of the annual budget.

3.4 Flowing from this information, forecasting the year-end position becomes more attainable, as does the projection of cash flows and loan requirements. Aligned with this will be the future ability for budget holders to add comments and notes directly to the reports.

3.5 At the highest level of the monthly report, total income is $4.9 million ahead of budget, and expenditure is $1.6 million above budget. The net position is an accounting surplus of $6.3 million, against a year-to-date budget of $3 million. This is a significant positive variance to budget which is mainly the result of:

- the very sizeable ($3.1million) unrealised gain on Interest Rate Swaps, (a non cash accounting adjustment);
- the gain on sale of property and vehicles of $110,000;
- the loss on sale of $158,000 in relation to the Golden Bay Medical Centre properties;
- a positive variance in Development and Financial Contributions of $850,000, mostly through activity in Richmond;
- the early arrival of some grant funds;
- vested assets are $568,000 behind budget expectations, however this can vary considerably throughout the year.

3.6 Items contributing to the over-expenditure position include:

3.6.1 Within the maintenance costs $4.2 million of emergency works expenditure, which will be funded by a mix of NZ Transport Agency (NZTA) subsidies, Department of Conservation grants, and a transfer from the Disaster Fund; and

3.6.2 Legal costs are up primarily as a result of activity in:

- Resource Consents being contested;
- Stormwater – land acquisition;
- Jackett Island costs;
- Legal advice on the acquisition and use of the Kina Reserve.

3.6.3 Consultants fees are currently behind budget by around $600,000; and

3.6.4 The level of charge from the Nelson Regional Sewerage Business Unit (NRSBU) is also lower than budgeted.

3.7 Council's working capital position as at 31 January 2014 was ($1 million) compared to the year-end projection of ($4.4 million).

3.8 The high value of Debtors as at 31 January is the result of the early posting of the February rates instalment totalling $12 million. The contra entry is that Payables are also $12 million higher than actual as at that date.

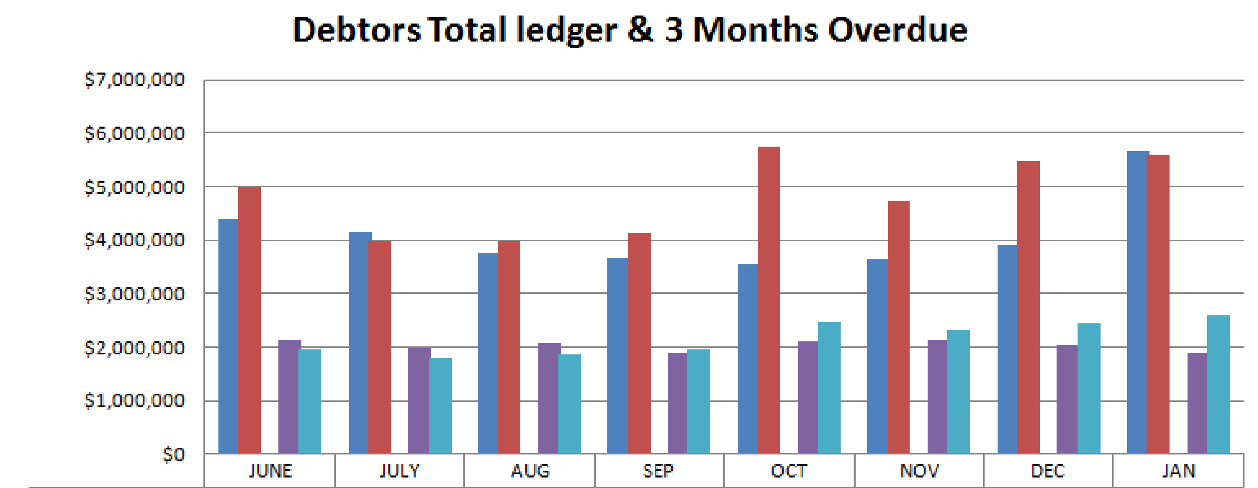
Tasman District Council
Statement of Comprehensive Financial Performance
For the year to January 2014

Actual 2013 $000		Actual Jan 2014 $000	Budget Jan 2014 $000	Budget 2014 $000
	INCOME			
	Revenue from Rates			
31,398	General rates	18,852	18,717	32,087
23,286	Targeted rates (other than for w ater supply)	13,909	14,142	24,244
5,543	Targeted rates for a w ater supply	3,563	3,154	5,407
	Operating Activities			
4,051	Development and financial contributions	2,598	1,748	3,152
10,330	Subsidies and grants	6,295	6,048	10,489
24,642	Other revenue	13,923	13,671	24,680
99,251	**Total Revenue**	**59,140**	**57,480**	**100,059**
6,070	Fair value movement on revaluation	3,645	583	1,669
59	Other gains	125	48	82
311	Finance income	221	129	237
105,690	**TOTAL INCOME**	**63,131**	**58,240**	**102,047**
	EXPENSE			
7,998	Finance expense	5,016	5,034	8,996
16,574	Employee related expense	10,831	10,645	18,264
34,574	Expenditure on operating activities	16,235	17,124	31,972
22,078	Maintenance	13,825	11,525	19,760
19,035	Depreciation and amortisation	10,858	10,858	18,614
100,258	**TOTAL EXPENSE**	**56,766**	**55,186**	**97,606**
5,432	**TOTAL OPERATING SURPLUS**	**6,365**	**3,053**	**4,442**
3,051	Income of joint ventures	0	0	4,200
4,268	Share of associates surplus/deficit	0	0	0
12,752	**NET SURPLUS BEFORE TAXATION**	**6,365**	**3,053**	**8,642**
0	Income tax expense	0	0	0
12,752	**NET SURPLUS for the year**	**6,365**	**3,053**	**8,642**
	OTHER COMPREHENSIVE INCOME			
42,957	Gain on asset revaluations	0	0	0
(501)	Asset impairment Loss	0	0	0
(601)	Restatements	0	0	0
565	Share of associate other comprehensive income	0	0	0
42,420	**TOTAL OTHER COMPREHENSIVE INCOME**	**0**	**0**	**0**
55,172	**TOTAL COMPREHENSIVE INCOME for the year**	**6,365**	**3,053**	**8,642**

Tasman District Council
Statement of Financial Position
As at January 2014

Actual 2013 $000		Actual Jan 2014 $000	Budget 2014 $000
	CURRENT ASSETS		
1,752	Cash and cash equivalents	1,207	2,557
15,612	Trade and other receivables	21,244	9,798
5,583	Other financial assets	5,672	7,188
1,866	Non current assets held for resale	0	1,000
24,813	**TOTAL CURRENT ASSETS**	**28,123**	**20,543**
	CURRENT LIABILITIES		
12,648	Trade and other payables	16,381	11,914
1,671	Employee benefit liabilities	1,645	1,853
8,203	Current portion of borrow ings	11,131	11,139
22,523	**TOTAL CURRENT LIABILITIES**	**29,157**	**24,905**
2,290	**WORKING CAPITAL**	**(1,034)**	**(4,363)**
	NON CURRENT ASSETS		
88,098	Investments in associates	88,098	82,929
3,790	Other financial assets	3,873	3,651
915	Intangible assets	0	0
31	Trade & other receivables	0	62
20,356	Forestry assets	20,356	20,166
3,460	Investment property	1,710	3,526
1,221,139	Property, plant and equipment	1,225,046	1,240,361
1,337,789	**TOTAL NON CURRENT ASSETS**	**1,339,083**	**1,350,695**
	NON CURRENT LIABILITIES		
149,812	Term borrow ings	145,292	171,656
3,197	Derivative Financial Instruments	(447)	4,000
545	Employee benefit liabilities	545	611
1,041	Provisions	1,041	974
154,595	**TOTAL NON CURRENT LIABILITIES**	**146,430**	**177,241**
1,185,484	**TOTAL NET ASSETS**	**1,191,619**	**1,169,091**
	EQUITY		
502,049	Accumulated equity	502,244	509,693
13,984	Reserve funds	19,679	11,010
669,451	Revaluation reserves	669,697	648,388
1,185,484	**TOTAL EQUITY**	**1,191,620**	**1,169,091**

4 Debtors



	JUNE	JULY	AUG	SEP	OCT	NOV	DEC	JAN
TOTALS 12/13	$4,411,900	$4,153,833	$3,761,135	$3,682,293	$3,555,008	$3,633,185	$3,906,146	$5,646,304
TOTALS 13/14	$4,989,411	$3,971,468	$3,979,739	$4,136,443	$5,737,670	$4,743,266	$5,477,038	$5,588,164
3 MONTH 12/13	$2,142,454	$1,987,556	$2,066,220	$1,883,790	$2,101,265	$2,138,829	$2,049,590	$1,896,272
3 MONTH 2013	$1,942,839	$1,813,954	$1,853,835	$1,953,195	$2,477,047	$2,324,516	$2,435,298	$2,601,304

4.1 Total debtors, are similar to the previous month, and also the same time last year. The data is again influenced by the timing of the NZTA monthly claim.

4.2 The three month and over position has increased as some older debts have remained unpaid. Accounts which have led to this position include; Development Contributions, some of which will incur an interest charge, outstanding berthage, a Civil Defence claim, and a grant from the Ministry of Economic Development towards the Great Taste Tasman Cycle Trail. A mixture of options are available to Council to recover debt; including time payment, putting a writ on assets, and using debt collection agent.

5 Rates Rebates

5.1 The Department of Internal Affairs Rates Rebate scheme continues to provide a strong level of financial assistance to Tasman ratepayers, with 1,454 applications already processed for the 2013/14 year, totalling just over $825,400 in rebates.

6 Staffing

6.1 We are pleased to advise that Matthew McGlinchey, Senior Management Accountant, has joined the team, and hit the ground running. The immediate focus for Matt is financial monthly reporting.

6.2 Also new to the team is Kelly Kivimaa-Schouten, Revenue Accountant. Kelly is quickly getting up to speed on all things Rates, will be attending the rates conference later this month, and implementing the rates modelling module.

6.3 An appointment for the Management Accountant has now been made, and Lisette Taylor will be joining the finance team on Monday 24 March 2014.

7 Attachments

Nil

9.9 TREASURY REPORT

Information Only - No Decision Required

Report To:	Corporate Services Committee
Meeting Date:	13 March 2014
Report Author:	Bryce Grammer, Financial Accountant
Report Number:	RFN14-01-03
File Reference:	B059

1 Summary

1.1 This report updates Committee members on compliance with Council's Treasury Management Policy as at the end of February 2014.

1.2 Council is complying with its Treasury Management Policy, as well as with Treasury limits, with the exception of the debt maturity profile. Council became non-compliant with its debt maturity profile from July 2013 as ASB's facility maturity date fell within the 0-3 years maturity bracket. Staff are currently working on a review of banking facilities. This review will cover both transactional banking and borrowing facilities. Bank facilities are being reduced as borrowing is transferred to the Local Government Funding Agency (LGFA).

1.3 Cash investments are at $6.2 million, with an average interest rate of 3.51%.

1.4 Council borrowings at 28 February 2014 total $157.2 million. The weighted average interest rate on borrowings is 5.091%. Council's cost of funds including interest rate swaps, bank margins and line fees being taken into account is 5.328% compared to a budget of 5.80%.

2 Draft Resolution

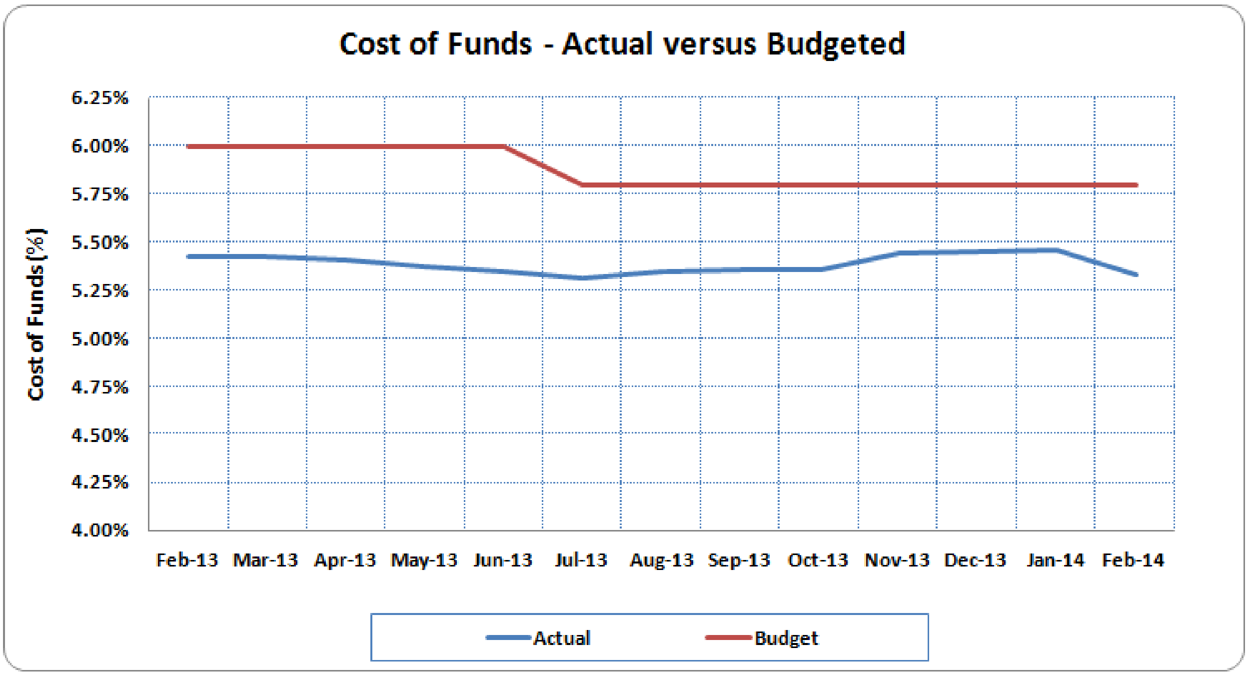
That the Corporate Services Committee receives the Treasury Report RFN14-01-03.

3 Treasury: November 2013

Debt Levels

3.1 Council's debt at 28 February 2014 stands at $157.2 million, with an average interest rate of 5.328% (June 2013 5.04%). Council's debt includes debt that relates to its share of the Nelson Regional Sewerage Business Unit.

Cost of Funds



3.2 This graph shows Council's actual weighted average costs of funds at 28 February 2014 including interest rate swaps, bank margins, and line fees at 5.328% against a budgeted rate of 5.8%.

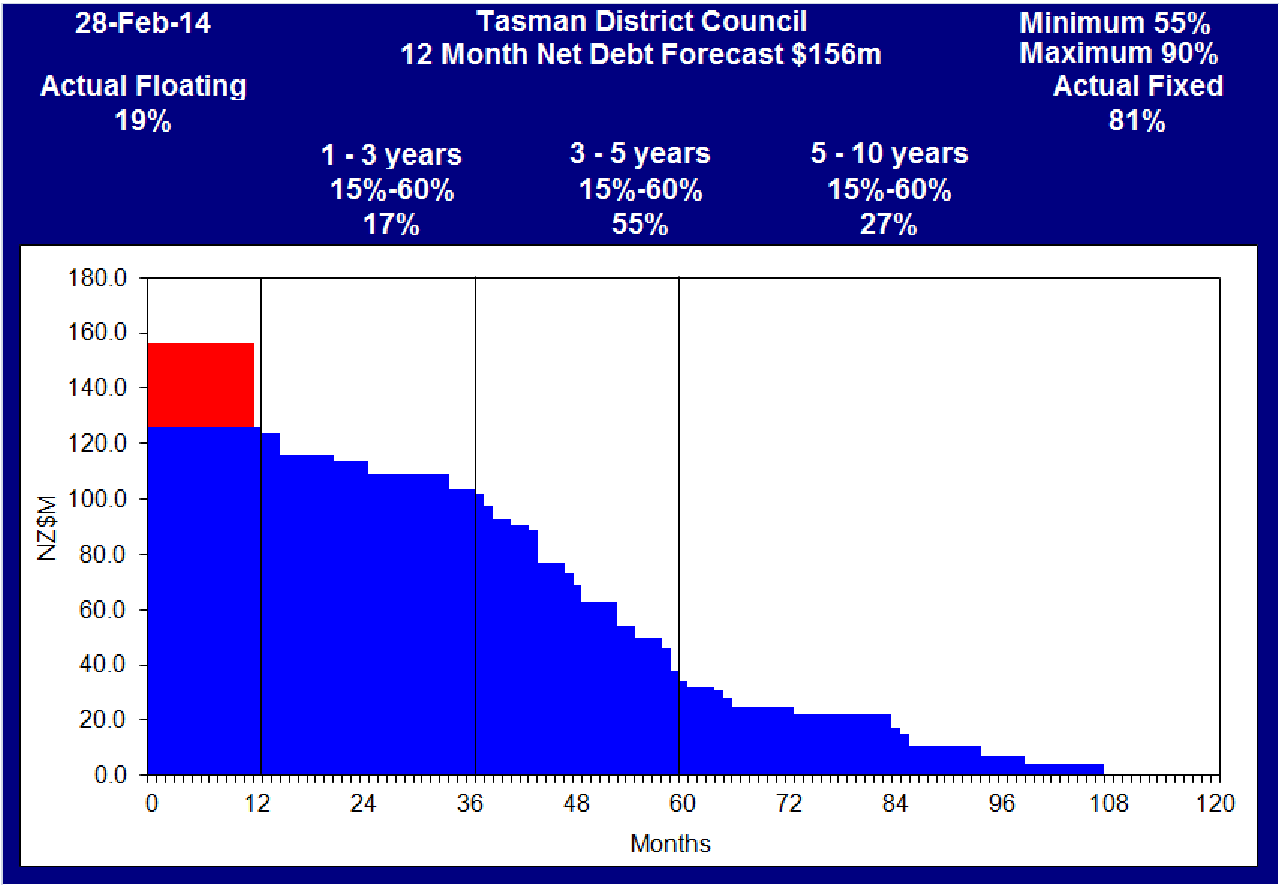
Interest Rate Swaps

3.3 The Corporate Services Manager has delegated authority to enter into interest rate swaps on behalf of Council on the proviso that it is reported back to this Committee. No new swaps have been entered into since the last report.

3.4 At February 2014 Council had $130.78 million of interest rate swaps in place, equal to 81% cover over existing debt and 84% over forecast 30 June 2014 net debt. Forecast 12 month net debt will be added for the next Treasury Report.

Treasury Limits

3.5 The following are details of Council's compliance with Treasury limits. The chart below displays the interest rate risk position of Council.



Interest Rate Risk Position Graph

The interest rate risk position visually represents the interest rate position within approved interest rate control limits as set out in the TDC Treasury Policy document. The chart takes a snapshot of the risk position as at the reporting date.

The blue part of the graph shows the amount of debt which is fixed – this includes fixed rate bonds, together with payer swaps, meaning debt which gets repriced in one year's time or later. The top of the red area represents the forecast debt in a year's time. The red area therefore illustrates the amount of debt deemed floating rate and will include any forecast debt that has not been pre-hedged. Any existing loans or financial instruments which will be repriced within the next 12 months are included in the red area.

The key areas of focus are:

Fixed Rate Percentage Limit: (wholesale interest rate certainty)

The fixed rate percentage calculation is the total amount of fixed rate debt/interest rate hedges over the 12 month forecast net debt amount. Fixed rate is defined as having an interest rate resetting maturity/expiry date of greater than 12 months.

Fixed Rate Maturity Limits: (spreading of wholesale interest rate maturity risks)

Fixed rate repricing maturity dates are spread based on defined maturity band limits, 1 - 3 years, 3 - 5 years and 5 - 10 years. Minimum and maximum percentage limits within each time band ensure a spread of maturities and reduces the risk of maturity concentrations.

3.6 Fixed Rate Maturity Profile Limit

This measures the spread of Council's risk of refinancing interest rates, achieved through the use of interest rate swaps.

	Minimum	Maximum	Actual: February 2014	Within Limits
1 – 3 years	15%	60%	17%	✓
3 – 5 years	15%	60%	55%	✓
5 – 10 years	15%	60%	27%	✓

3.7 Fixed/Floating Profile

This measure shows the balance between minimising exposures to negative fluctuations in floating rates against savings opportunities. Council's strategy is to limit negative exposures and provide certainty of future interest rate costs. This is achieved through its use of interest rate swaps.

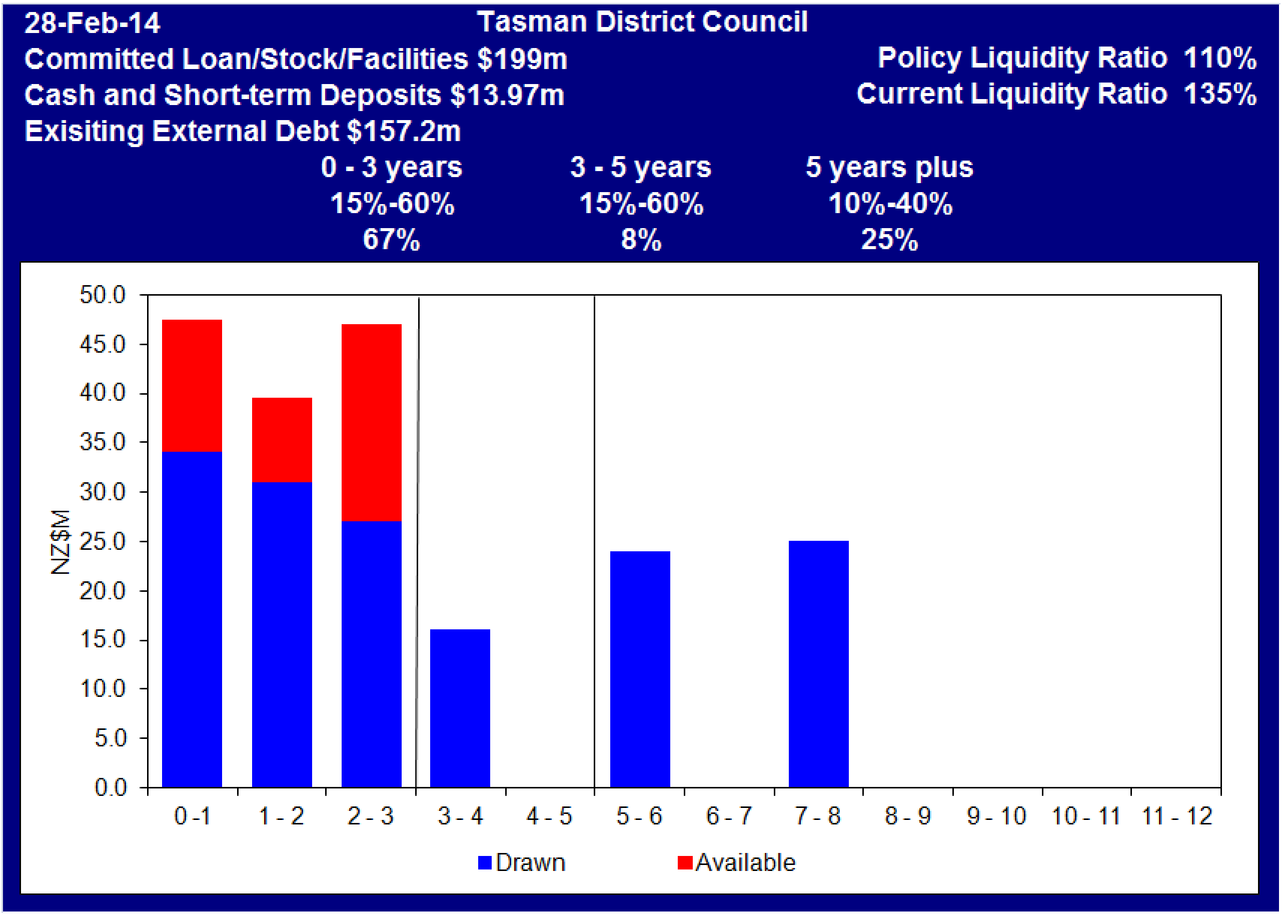
(A maturity greater than 1 year is defined as fixed)

Minimum	Maximum	Fixed Actual: February 2014	Within Limits
55%	90%	81%	✓

3.8 Facility Maturity Limit

Total committed funding in respect to all loans and committed bank facilities is controlled as follows:

The chart below represents Council's funding maturity profile. The measures indicate how effectively Council has spread the risk of refinancing its facilities and loans. The Liquidity Ratio represents the debt headroom available in Council's facilities along with cash available over and above its existing external debt.



Liquidity and Funding Maturity Risk Position Graph

The liquidity and funding risk position visually represents the approved funding maturity limits as set out in the TDC Treasury Policy document. The chart takes a snapshot of the risk position as at the reporting date.

The key areas of focus are:

Liquidity Ratio: (maintaining additional committed liquidity)

The liquidity ratio calculation represents the total committed bank facilities and term debt amounts, together with liquid investments, over the total debt amount.

Funding Maturity Risk Position: (spreading of debt maturity dates)

Existing committed bank facility expiry dates and term debt maturity dates are spread based on defined maturity band limits, 0-3 years, 3-5 years and 5 years plus. Minimum and maximum percentage limits within each time band ensure a spread of maturities and reduces the risk of maturity concentrations.

3.9 The debt maturity profile became non-compliant in July 2013 as the ASB $40m facility fell within the 0-3 year maturity bracket. Finance staff are currently working through a strategy to bring this back into compliance. Part of this includes refinancing existing debt sitting under bank facilities into longer maturities of LGFA debt. $25m of bank facilities were cancelled in December 2013 and a further $10m will be cancelled in March 2014. This is as a direct result of increased funding through the LGFA.

3.10

Treasury Limits	Actual November 2013	Within Limits
Net Debt not to exceed 20% of equity	12.0%	✓
Net external debt not to exceed 225% of total operating revenues	148.6%	✓
Net interest as a % of total revenues to be less than 20%	7.1%	✓
Net interest as a % of total annual rates to be less than 25%	12.4%	✓
Liquidity over existing external debt to be at least 110%	135%	✓

As the February 2014 financial reports had not been finalised at the time of completing this report, the January 2014 data has been provided**.**

Counterparty Credit Risk

3.11 Council's policy is that NZ Registered banks must have a minimum Standard & Poor's (or equivalent) short term rating of A-1+ or long term rating of AA-. All counterparty banks are Standard & Poor's AA-rated.

3.12 The policy credit limit (NZ$) for each NZ Registered bank is $30 million. This covers Council's interest rate risk management instruments and cash investments.

Bank	Cash/Cash Investments $m	Notional Swaps $m	Credit Exposure $m	Compliance
Westpac	6.2	60.1	14.0	Within Policy
ASB	7.756	61.7	14.7	Within Policy
ANZ	0.015	9.0	2.0	Within Policy

3.13 Counterpart credit risk will be reduced now that the proposed changes to the Treasury Policy are approved. This will occur through reduced investments with the banks.

4 Investments

4.1 Council cash investments which include the general disaster fund, wetlands fund and short-term investments total $6.2 million dollars with an average interest rate of 3.51% (June 2013 3.83%).

4.2 The individual cash balances are as follows:

	$ invested	Interest Rate
General Disaster Fund	1,200,000	3.98%
Wetlands Fund	15,325	3.80%
Short-term Deposit	5,000,000	3.40%
Total	**6,215,330**	**3.51%**

Item 9.9

4.3 Council has confirmed that specific reserves will no longer be held in separate bank accounts. These investments have been transferred into Council's main bank account and will be used to repay debt. $1.2m has been retained in the Cash Investments.

4.4 In February 2014, $10m was borrowed from the NZLGFA. These funds were to be used to repay existing debt. From these proceeds we had repaid $5m of ASB debt by 28 February 2014. The remaining $5m has been placed on short-term deposit and will be used, in addition to cash reserve balances, to repay debt in March (when it matures). This will leave $5m in debt remaining with ASB, and at that time the current facility limit will be reduced.

4.5 The existing 'NRSBU' facility of 12.5m will expire in late June 2014. This facility will not be renewed and existing debt will be transferred to the main Council facility.

5 Emissions Trading Scheme

ETS hedging Limits

5.1 There have been no new transactions entered into since the last report.

5.2 ETS credits are managed in defined time buckets incorporating minimum or maximum hedging.

	Minimum Cover	**Maximum Cover**	**Actual September 2013**	**Within Limits**
***Committed**	80%	100%	100%	✓
Forecast period				
0 – 1 years	0%	80%	80%	✓
1 - 2 years	0%	50%	20%	✓
2 – 3 years	0%	30%	0%	✓

**exposure becomes committed in Jan-Mar (quarter following emission period as Council must report emission from the previous year).*

6 Appendices

Nil

9.10 DECEMBER 2013 FINANCIAL REPORTS

Information Only - No Decision Required

Report To:	Corporate Services Committee
Meeting Date:	13 March 2014
Report Author:	Bryce Grammer, Financial Accountant
Report Number:	RFN13-03-11
File Reference:	A501

1 Summary

The financial statements and Selected Closed Accounts Report for the six months to December 2013 are attached for your information.

2 Draft Resolution

That the Corporate Services Committee receives the December 2013 Financial Reports RFN13-03-11.

3 Financial Statements

3.1 The financial statements and selected closed accounts report for the six months to 31December 2013 are attached for your information. This report is similar in format and detail to the Council's Annual Report.

3.2 The financial statements contain a summary of each significant activity in the Funding Impact Statement (FIS) format. They also contain narrative regarding any significant variances and details of major activity within the sections.

3.3 At the highest level, income is at 53% of budget, expenditure at 52%, leaving the overall position a surplus of just under $6 million, against a full year budget of $9 million surplus, or 66% of the full year budget. The underlying operational result was a $102,000 surplus after non-cash items of the fair value movement of interest rate swaps, and vested assets have been removed from income.

3.4 The Annual Report would include some transactions that are only completed at year end, and therefore are not reflected here. This would include such items as Joint Venture transactions, share of associates surplus/deficit, adjustments for fair value in forestry and the revaluation of assets.

3.5 We are working towards including the Balanced Budget Statement of Financial Performance and Reserve reporting in the next quarter's Council financial reports.

3.6 Council's set of Selected Closed Accounts is also included with the financial reports. These accounts are separated out within Council's equity, and carry their own balances. The accounts are monitored on an individual basis, and reported as such.

3.7 Some key items from the reports include:

- At the highest level, income is at 53% of budget, expenditure at 52%, leaving the overall position a surplus of just under $6 million, against a full year budget of $9 million surplus, or 66% of the full year budget.

- Fair value movement of interest rate swaps – other gains include a fair value gain for the year of $3.6m on Council's interest rate swaps due to the forecasted increase in long term interest rates.

- Subsidies and grants – this item includes a contribution of $430,000 towards the purchase of the LEH Baigent Reserve in Kina.

- Closed account – surplus balances in the Wastewater and Dog closed accounts will be used to repay debt.

3.8 If you have any questions regarding these reports, please feel free to contact the Finance Team to discuss before the meeting.

4 Appendices

1. Financials for the six months ended 31 December 2013 *(Under Separate Cover)*
2. Closed Account Report 31 December 2013 *(Under Separate Cover)*