

ITEM 3. POLICY AND STRATEGY FOR THE INVESTMENT OF SURPLUS FUNDS**FILE NO: SO4 7745****SUMMARY**

This report proposes a revised Policy and Strategy for The Investment of Surplus Funds for Council.

The purpose of this policy and strategy is to optimise investment income from the short and long term investment of funds that are surplus to Council's present operational needs, while ensuring the investments are secure, satisfy our risk/return criteria, and comply with the relevant legislation (Local Government Act 1993).

The proposed revision to Council's existing Investment Policy is designed to broaden Council's options for investing in direct and indirect investment securities to improve the yields on Council's managed funds portfolio while continuing to maintain a high level of security over the entire investment portfolio.

RECOMMENDATION

It is resolved that Council adopt the revised Policy and Strategy for the Investment of Surplus Funds as shown at Attachment A to the subject report.

ATTACHMENTS

Attachment A: Policy and Strategy for the Investment of Surplus Funds.

Attachment B: Section 625 Minister's Order

BACKGROUND

1. The Local Government Code of Accounting Practice and Financial Reporting (Code) states that:

“Councils must maintain an investment policy that complies with the Act and ensures it or its representatives exercise care, diligence and prudence when investing council funds. Managers have a fiduciary obligation to ensure that the resources under their control are efficiently utilised and effectively protected.

In exercising its powers of investment council should be guided by the latest Ministerial Order and consider a range of factors. These include the purpose of the investment; the desirability of investment diversification; the nature and risks associated with those investments; the likely income return and timing of income return; the length of the proposed investment; the costs involved in making the investment and other matters as appropriate.

Councils should establish an investment strategy as part of its overall financial plan and have a process of performance review which should be undertaken regularly and in any case at least annually”.

2. In accordance with the principles of financial management, Council's Investment Policy and Strategy is designed to optimise investment income from the short and long term investment of funds that are surplus to Council's present operational needs, while ensuring the investments are secure, satisfy our risk/return criteria, and comply with the relevant legislation.
3. The current Investment Policy and Strategy was adopted by Council in August 2004, with the intention that it would be subsequently revised to ensure the document remained relevant and suitable for legislative changes and prevailing market conditions.
4. The revised Investment Policy and Strategy proposes the following key changes:
 - (a) the maximum percentage allowed for direct investments (eg. term deposits, FRN's, etc.) and indirect investments (eg. managed funds) in A-rated funds to increase from 30% to 50% and 40% to 70% respectively. (refer to section 7 of the policy).
 - (b) investments with a single institution to be increased as follows: (refer to section 7 of the policy):

AA-Rated	From 20% to 25%
A-Rated	From 10% to 20%

- (c) A new clause provides that where a change in the size of the overall portfolio would result in existing investments exceeding maximum investment thresholds, then no immediate forced sale will be required. Instead, a freeze will be imposed on the acquisition of new investments in the relevant category until such time as the portfolio can be effectively managed back within the maximum thresholds allowed under the Policy. (eg "A" rated fund managers hold 69% of total funds management portfolio, funds are recalled from a "AAA" rated fund manager which results in a reduction of the total portfolio size thereby increasing the "A" rated fund managers holding to 71% of the total portfolio, slightly exceeding the maximum threshold).
 - (d) This tolerance must be corrected within a period of 3 months, or immediately if the maximum threshold is exceeded by more than 5% points. (e.g. in the above scenario, if the recall from a "AAA" rated fund manager resulted in the "A" rated fund holding increasing from 69% to 77% an immediate correction would be required to bring the "A" rated fund threshold back within the 70% maximum allowed)
 - (e) A new section has been included enabling delegation of the management of complex investment securities within the portfolio, where the expertise for doing so is beyond the City staff, to professional fund managers or investment advisers in order to earn higher yields. The delegation is limited to a maximum of 10% of the City's total portfolio, or \$20M, whichever is the lesser. All investments will still be required to comply with all aspects of Council's Investment Policy and Strategy and investments must be held in either the City's name or held in safe custody with Council as beneficial owners. A number of other councils are already utilising this expertise to improve their investment returns.
5. Council's risk profile in relation to the investment of surplus funds can generally be described as prudent, conservative and risk averse as required by the Local Government Code of Accounting Practice and Financial Reporting.
 6. The benchmark performance goal of Council's Investment Policy and Strategy is to surpass the UBSA Bank Bill Index.
 7. The policy conforms with the principles outlined in the NSW Local Government Investments Best Practice Guide as published by the Local Government Finance Professionals and Local Government Managers' Association.
 8. In developing the revised Investment Policy and Strategy, a number of industry investment advisers were consulted. The general consensus is that the proposed Investment Policy and Strategy is well balanced, and if anything, could be less conservative.

KEY IMPLICATIONS

9. Council's Investment Policy directs its investments to ensure compliance with the requirements of the Local Government Act 1993 and Minister's Order within acceptable risk/return parameters.

FINANCIAL IMPLICATIONS

10. Council's budgeted income for the 2006/07 financial year is \$18.1M based on achieving benchmark returns against surplus cash for the budgeted operational and capital works program. The revised Policy and Strategy will increase the potential investment opportunities in securities that aim to outperform the benchmark returns while still maintaining a balanced portfolio to ensure security of the funds.

RELEVANT LEGISLATION

11. Council is authorised to invest its surplus cash under Section 625 of the Local Government Act 1993.
12. The Local Government (Financial Management) Regulation 2005 (clause 212) requires Council to provide a written monthly report of all monies invested, under Section 625 of the Act.
13. The Local Government Code of Accounting Practice and Financial Reporting at 11.3.5 states that Council must maintain an investment policy that complies with the Act and ensures it or its representatives exercise care, diligence and skill that a prudent person would exercise in investing council funds.

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