

Reserves and Treasury Policies

Background

At the last Board meeting held on 19 August a draft reserves and treasury policy was discussed. The Board agreed that the draft policy on reserves should be revised from 70% to 60% of net annual expenses, and that it should reference the short-term fixed interest security credit rating of our banker.

Our banker has advised that specific ratings are applied to debt instruments such as perpetual bonds, etc but for general liabilities (demand deposits, term deposits, on-call investments) the appropriate guide is the long term rating of the institution. The BNZ, our banker, has a long term credit rating AA (Stable) with Standard & Poor's and Aa2 (Stable outlook) with Moodys, which is described as "very strong ability to pay".

Draft

Reserves and Treasury Policy 15 October 2009

Water New Zealand policy is to:

- accumulate 60% of annual expenses as reserves; and
- invest surplus funds in secure short term fixed interest securities only.

For the purposes of this policy:

- 'secure' shall be defined as term deposits held with its banker; and
- 'short term' shall mean a period of not more than six months.

At least two months' expenses shall be held in an 'on call' account, available for immediate need.

The banker shall be determined by the Board. The banker shall hold a high credit rating with a reputable rating agency.

A high credit rating is defined as the equivalent of, or better than:

- A1+ (short term) and A (long term) with Standards and Poores; and/or
- Prime-1(short term) and A1 (long term) with Moody's.

Water New Zealand's banker is currently the Bank of New Zealand.

The Chief Executive has delegated authority to manage surplus funds in accordance with this policy.

Explanation

The purpose of this policy is to:

- Mitigate business risk;

- Provide guidance for Water New Zealand directors and management investing surplus funds in ways that minimize risk;
- Balance appropriate levels of liquidity against the opportunity to profit from investing surplus funds;
- Provide for contingencies; and
- Help protect directors and management.

As with other membership organizations Water New Zealand's is funded by a mixture of subscription income, profits from events, publishing, the provision of administrative services, and investments. Proportionately, its income from running events and publishing is significantly higher than that of similar organizations.

There is significant financial risk associated with this funding model, particularly associated with the underwriting of events. The financial failure of one major event would put the Association's funding at risk. This risk can be mitigated by the accumulation of adequate reserves.

Maintaining relatively liquid reserves mitigates against losses that might be incurred on realization of longer term investments, such as shares or long term debt instruments.

Investment decisions are determined by the timeframes required for income along with appetite for risk. Investments in cash are recognized as being appropriate for short and intermediate term requirements. For intermediate and long timeframes bonds may be more appropriate. Shares and property provide greater returns as long term investments. The short term volatility in values for bonds, shares and property limit their usefulness as reliable short term investments.

While there are no guidelines for desired levels, the general rule of thumb for not for profit corporates is to accumulate between 50% and 100% of annual expenses as reserves.

Directors and management of corporates have fiduciary responsibilities under statutory and common law. Subject to the caveats of proper management execution, appropriate Board monitoring and accurate and timely financial Board reporting, this policy will assist Water New Zealand directors and management in meeting their fiduciary responsibilities.