Liability Management Policy

Introduction

This policy has been established to ensure the prudent financial management for the issuance and management of Council debt.

The policy incorporates the requirements of the Local Government Act and should be read together with the Investment Policy. These policies form the Treasury Management Policy of the Council.

This policy includes the Christchurch City Council Sinking Fund Commissioners. For the purposes of limiting total debt levels of the Council and financial management ratios, the debt levels and liquid investments of Christchurch City Holdings Ltd, parent only, (a 100% owned holding company) are added to the Council figures.

To determine the scope of this policy, the definition of terms used shall be that of the Local Government Act and Accounting Standards in force.

Standard and Poor's has provided a joint credit rating for both the Council and Christchurch City Holdings Ltd. The rating is AA+ (Long Term) and A1+ (Short Term). It is an objective of this policy that the ratings at this level be maintained as a minimum.

Principles

The following principles underlie the policy:

2.1 Borrowed funds will be used to fund capital expenditure and investment. An allowed exception is for working capital overdraft under section 4.12. Debt will be used as a residual funds source after funds generated from depreciation are applied to renewal and new capital expenditure. The mix of debt and revenue funding for capital funding will be determined by the Financial Plan each year.

2.2 Debt raised will be repaid over the economic life of assets restricted to a maximum of 20 years to ensure inter-generational equity.

2.3 Interest costs are part of operating expenditure and will be funded from operating revenue.

2.4 The annual debt repayment provision will be funded from operating revenue.

2.5 Interest rate exposure will be managed consistent with the aim to:

- have interest costs where possible at or below interest rates projected in the Council's Long-Term Financial Strategy or the rates determined to be economically feasible for specific assets funded
- hedging is only allowed for debt in place (or part thereof) or where there is a commitment to borrow in the near future and not for speculative purposes
- remain risk averse
- maintain a mix of both fixed and floating rates, where appropriate, to maintain flexibility and advantage in case of interest change.

2.6 Debt financing is recognised as a component in the Council's Revenue & Financing Policy and Long-Term Financial Strategy to provide inter-generational equity which prevents costs being incurred by the current generation which are for the benefit of future generations.

Limits on Total Borrowing

3.1 The forecast interest rate payable on external debt intended to be raised by the Council in the ensuing year will be budgeted for and disclosed in the Financial Plan.

3.2 Total external debt as a percentage of total assets of the Council and Christchurch City Holdings Ltd, parent only, shall be no more than 12%.

3.3 The total external debt of the Council and Christchurch City Holdings Ltd combined as a percentage of realisable assets (all assets excluding infrastructural and restricted assets) shall be no more than 33%.

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3.4 Net interest paid on term debt by the Council and Christchurch City Holdings Ltd combined will not exceed 8% of the consolidated gross revenue provided interest rates do not rise above 8.5%. Should rates rise then the Council will approve a further limit to contain interest costs.

3.5 The ratio of net external debt of the Council and Christchurch City Holdings Ltd combined to funds flow from operations shall not exceed five times, ie an ability to repay debt over five years (medium term) before net capital additions.

Note: Funds flow from operations is the net cash surplus of gross revenue over operating cash expenses (excludes depreciation).

Borrowing

4.1 All external debt of the Council including financial leases must be authorised by resolution of the Council.

4.2 The aggregate amount the Council determines as not being so significant as to require specific authorisation under Section 112 (c) (ii) (A), is $500,000.

4.3 Loans raised by the Council are to be secured by a charge on Rates revenue.

4.4 Except as qualified in section 4.6 below, new loans raised in any particular year are to be no greater than the amount disclosed in the Financial Plan for that year and applied only to capital projects and investments listed in the Financial Plan.

4.5 Borrowing will be applied to project funding after utilisation of other capital funding identified in theFinancial Plan in accordance with the principle set out in section 2 above.

4.6 All new loans required to fund expenditure which has arisen subsequent to the Financial Plan being confirmed shall require Council approval by a specific resolution of the Council including the reasons why expenditure was not included in the Financial Plan.

4.7 Debt may be raised in either fixed or floating-rate terms, and for short (ie up to one year) or long maturity terms subject to limits.

4.8 The term of a loan must not be longer than the economic life of the capital assets it funds (as defined by Council resolution) and in any event no more than 20 years.

4.9 A loan may be raised in several tranches for terms less than 20 years. Repayments at maturity of a tranche within the term of a loan may be refinanced without further Council resolution. Refinancing loans shall not add to the term of the original loan.

4.10 For new loans, the Council must consider the risks of borrowing including a sensitivity analysis to changing interest rates.

4.11 The borrowing resolution shall define who has the authority to raise loans. Should it be silent then authority is granted to staff as defined in section 9.2 below.

4.12 Unless the Council resolves to the contrary and subject to any instruction issued by the Director of Finance, the Funds Accountant may raise loan funds by way of bank overdraft to cover short-term cash shortfalls limited to a maximum of $2M. Borrowing under this clause is not subject to the constraints of clauses elsewhere in this policy.

The Director of Finance may issue guidelines and instructions on the raising of overdraft funds up to the $2M limit.

Any overdraft so raised shall be reported to the Director of Finance within two working days.

For the purposes of this clause the term “short-term” means for terms of less than one year.

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Repayment of Debt

5.1 Debt may be repaid by one or a combination of:

- Annual Sinking Fund instalments where the Sinking Fund Commissioners hold the funds as a separate trust, for the Council, for the sole purpose of debt repayment of specific loans.
- Annual Contributions to a Loan Repayment Reserve to be held by the Council for the sole purpose of applying at appropriate opportunities to repayment or reduction of loans.
- Annual table repayment instalments providing for full repayment over the term of a loan being 20 years or less.
- Repayment from revenue or other sources.

5.2 With the exception of table loans, a minimum of 3% of the aggregate of the initial external debt raised by the Council and Christchurch City Holdings Ltd, combined, shall be repaid annually in accordance with one or a combination of the options set out in 5.1 above. Initial Debt is defined as the original sum of any loan borrowed which has not been fully repaid.

5.3 The rate of 3% shall be reviewed periodically to ensure that with accumulated interest earnings on invested funds, sufficient funds are available to repay each initial loan tranche at the end of 20 years. At all times 3% shall be a minimum.

5.4 Sinking Funds and Loan Repayment reserves may be applied to earlier repayment of loans in conjunction with refinancing of tranches. In such cases the annual contributions to sinking funds or loan repayment reserves shall be recalculated to ensure that sufficient funds will be on hand to ensure repayment of the balance within the 20-year time frame.

5.5 When the repayment provision for any specific loan has been fully funded, no further contributions will be required for that loan.

5.6 The Funds Accountant, after consultation with the Director of Finance and the Company Secretary of Christchurch City Holdings Ltd, may select the specific debt to be repaid in any one year to optimise the mix of debt types retained within the group.

Interest Rate Exposure

6.1 The interest rate policy of the Council is to manage the exposure to adverse interest rates consistent with the need to have interest costs, where possible, at or below interest rates projected in the Council's Financial Plan or Long Term Financial Strategy or the rates determined to be economically feasible for specific assets funded.

6.2 The Funds Accountant may implement an interest rate strategy with interest rates higher than that budgeted, where this is supported by an interest-rate view and strategy formed under the procedures of 6, 7, 8, and 9 below.

6.3 The Council may have an exposure to both fixed and floating interest rates. Fixed Rate Debt may vary between 35% and 100% of total debt maintained by either direct borrowing under these terms or by interest-rate hedging. There is a preference for fixed rate borrowing to fund long term asset acquisition.

6.4 The Funds Accountant shall be authorised to enter into interest-rate-hedging contracts to avoid an exposure to adverse rates based on the interest rate view.

6.5 All hedging contracts are only to protect the actual debt and debt to be raised. Speculation is not permitted.

6.6 All hedging contracts are to be discussed with the Director of Finance and, in his absence, with the Funds and Financial Policy Manager prior to being entered into, and reported to the Director of Finance on the same day that the transaction is entered into and to the Strategy and Finance Committee quarterly.

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6.7 Hedging can only take place with counter-parties who have a long-term credit rating of 'A-' or better.

Liquidity Policy

7.1 The debt-maturity profile shall be maintained so that no more than 35% of the relevant debt matures in either of the current or following fiscal year unless the total relevant debt outstanding is lower than $30,000,000. The relevant debt is the total external debt for the Council but excludes any leases, table loans, and floating-rate short-term loan issues.

7.2 Where possible, maturity dates should be spread throughout the year.

Credit Exposure

8.1 Hedging can only take place with counterparties who are credit rated 'A-' or better.

8.2 Settlement for new loans shall be by cleared funds.

8.3 Loan raising should be managed so that the impact of settlement default will not adversely affect the Council.

Management by Staff of the Borrowing Policies

9.1 All external debt must be authorised by the Council except that under section 4.12 (working capital overdraft). Staff shall have evidence of such approvals before any debt is raised.

9.2 Authority is delegated (under this Policy Statement) to the Funds Accountant and in his absence, any one of the Director of Finance, Funds and Financial Policy Manager, Financial Analyst, and the Financial Services Manager to raise external debt funds and to enter into hedging contracts on terms he may determine within the limits and guidelines of this Policy Statement.

The day-to-day management and actions may be undertaken by the Funds Accountant, but the responsibility for overview lies with the Director of Finance.

9.3 The Funds Accountant shall form a view on future interest rates based on independent professional advice. The view shall be revised at least quarterly. Action to change the Council's fixed, floating interest rate profile shall be based on that view.

9.4 The Director of Finance shall appoint a Treasury Review Team to assist on the formation of interest rate views and borrowing management strategy. The Treasury Review Team shall approve and maintain guidance notes and instructions developed for the proper management of the Council's debt under this policy.

9.5 A specific debt raising resolution may require joint delegations for action. If so, the more restrictive delegation shall be followed.

9.6 There shall be appropriate segregation of duties among staff involved in borrowing and investing of Council funds and this shall be subject to audit review.

9.7 The Funds Accountant shall maintain the register of charges and shall file with the Registrar of Companies a copy of the debt instrument periodically.

9.8 Actions taken under the Liability Management Policy are to be reported to the Director of Finance at least weekly, and to the Strategy and Finance Committee quarterly. Actions requiring reporting are:

- Debt servicing costs, both budgeted and actual
- Comment on interest rate exposure
- Debt-maturity profiles and expected timing of debt raising
- Total debt raised (including financial leases)
- Hedging contracts taken up since the last report
- Hedging and derivative contracts in place at the time of the report