# liability management policy

## 1. 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 current ratings are AA+ (Long Term) and A1+ (Short Term). It is an objective of this policy that minimum ratings of AA and A1+ be maintained.

## 2. 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 4.11. 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 Annual 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 consistently with the aim to:

- Recognise that the Council is a risk adverse entity and that it aims to have interest costs where possible at or below interest rates projected in the Annual Plan or the rates determined to be economically feasible for specific assets funded
- Maintain a mix of both fixed and floating rates, as appropriate, to ensure a degree of flexibility and also to take advantage of lower floating rates when appropriate.
- 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.

2.6 Debt financing is recognised as a component in the Council's Revenue and Financing Policy and Annual Plan to provide inter-generational equity recognising that some of the current costs incurred by the Council are for the benefit of future generations and should not be funded from current revenue streams.

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## 3. 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 Annual 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%.

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 that interest rates as reflected in the 90-day bank bill rate, do not rise above 8.5%. Should interest rates rise above this level then the Council may have to approve a further limit to contain interest costs after considering any such recommendation from the Director of Strategic Investments.

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, i.e. 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).

## 4. Borrowing

4.1 All external debt of the Council including financial leases must be authorised by resolution of the Council, subject to clauses 4.2 and 4.11.

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 Annual Plan for that year and applied only to capital projects and investments listed in the Annual Plan.

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

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

4.7 Debt may be raised in either fixed or floating-rate terms, subject to the limits within this policy.

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 the economic life of the capital asset it funds or the maximum loan term permissible, of 20 years. Repayments at maturity of a tranche within the term of a loan may be refinanced without further Council resolution. However these refinancing loans shall not add to the original agreed term or make the effective term of the loan more than 20 years.

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4.10 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 below.

4.11 Unless the Council resolves to the contrary and subject to any instruction issued by the Director of Strategic Investment, the Funds Accountant may raise loan funds by way of bank overdraft to cover short-term cash shortfalls limited to a maximum of $2,000,000. Borrowing under this clause is not subject to the constraints of clauses elsewhere in this policy.

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

For the purposes of this policy the term "short-term" means for terms of less than one year.

## 5. Repayment of debt

**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 annually 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 Strategic Investment and the Chief Executive Officer 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.

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## 6. Interest rate exposure

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

6.2 The Council may have an exposure to both fixed and floating interest rates. Fixed rate debt, defined as having an exposure to repricing greater than twelve months in the future, may vary between 35% and 80% of total debt maintained by either direct borrowing under these terms or by interest-rate hedging except if total debt is under $30,000,000 million in which case there is no minimum criteria and the maximum is 100%. No interest rate hedging can be entered into for periods longer than ten years without the approval of the Treasury Review Team.

6.3 The Director of Strategic Investment is responsible for the appointment of a Treasury Review Team to develop an interest rate view and borrowing management strategy. The Treasury Review Team shall approve and maintain operational guidelines developed for the proper management of the Council's debt under this policy. The Council's independent treasury advisor will be an ex officio member of the Treasury Review Team.

6.4 The Funds Accountant shall be authorised, after discussion with the Director of Strategic Investment and, in his absence, with the Funds and Financial Policy Manager, to enter into interest-rate-hedging contracts to avoid an exposure to adverse rate movements within the parameters of this policy and the operational guidelines developed by the Treasury Review Team. Hedging activities will be based on the strategic interest rate view developed by the Treasury Review Team, in conjunction with the Council's independent treasury advisor and the Funds Accountant.

6.5 The strategic interest rate view will be updated at least quarterly. The Funds Accountant will also hold regular meetings with the independent treasury advisor and update the Treasury Review Team at each meeting.

6.6 All hedging contracts must relate to actual or projected debt. Hedging contracts may be entered into to pre-hedge the market rate risk on future fixed rate drawdowns but any such hedging must commence within twelve months. Speculation is not permitted.

6.7 All hedging contracts longer than twelve months are to be discussed with the Director of Strategic Investment or the Funds and Financial Policy Manager before being transacted. All hedging transactions must be reported to the Director of Strategic Investment on the same day that the transaction is entered into and to the Strategy and Finance Committee quarterly.

## 7. Liquidity Policy

7.1 The debt-maturity profile shall be maintained so that no more than 35% of the relevant debt matures within twelve months 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. This ratio must be reviewed by the Director of Strategic Investment if the Council's long term credit rating from Standard and Poor's (or the Moody's equivalent) falls below 'AA-'.

## 8. Credit Exposure

8.1 Hedging can only take place with counterparties who are credit rated 'A' or better by Standard and Poor's (or Moody's equivalent).

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.

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## 9. Management by Staff of the Borrowing Policies

9.1 The day-to-day management of the Council's liabilities will be specified in a set of operational guidelines developed by the Treasury Review Team and approved by the Director of Strategic Investment.

9.2 All external debt must be authorised by the Council except that under sections 4.2 and 4.11 (working capital overdraft). Staff shall have evidence of such approvals before any debt is raised.

9.3 Authority is delegated (under this Policy Statement) to the Funds Accountant and in his absence, any one of the Director of Strategic Investment, 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 Strategic Investment.

9.4 If a specific debt raising resolution requires joint delegations for action. This more restrictive delegation shall be followed rather than the general parameters of this policy.

9.5 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.

9.6 The Funds Accountant shall maintain the register of charges and these shall be available for public inspection.

9.7 Actions taken under the Liability Management Policy are to be reported to the Director of Strategic Investment at least weekly, and to the Strategy and Finance Committee quarterly. Appropriate reporting requirements will be included in the operational guidelines.