Liability management policy

This policy should be read in conjunction with the Investment Policy.

1 Purpose

To enable the Council's debt funding and associated interest rate exposures to be managed in a prudent manner.

To establish a framework and a set of guidelines within which the treasury function of the Christchurch City Council (the Council) can operate.

2 Objectives

a) To minimise the Council's cost of borrowing through the effective control and management of its debt portfolio within the limits established by this policy;

b) To ensure the Council's continued ability to meet its debts in an orderly manner as and when they fall due in both the short and long term;

c) To maintain a prudent level of liquidity to meet both planned and unforeseen cash requirements;

d) To safeguard the Council's financial resources by establishing and regularly monitoring treasury credit limits and managing exposures within these limits.

e) To seek continued improvement in financial risk management strategies through ongoing evaluation and review of appropriate risk management techniques and strategies;

f) To maintain appropriate internal controls and staffing to minimise operational risk;

g) To ensure the Council's debt management is in accordance with the Council's requirements under the Local Government Act 2002;

h) To maintain the Standard and Poor's credit rating of the Council/Christchurch City Holdings Limited (CCHL) at AA (Long-Term) and A1+ (Short-Term) or better.

3 Management Structure, Responsibilities and Delegations

	Responsibilities
Council	• Approve the Liability Management Policy, and review, at least three yearly, as part of the LTCCP process. • Approve all new borrowing. • Amend liquidity profiles as required. • Monitor compliance with the Liability Management Policy through the receipt of periodic reports. • Appoint Sinking Fund Commissioners. • Grant delegated authority to act on liability management issues.
Chief Executive	• Ensure compliance with this policy through the appointment and accountability of appropriate staff. • Appoint a Treasury Review Team. • Execute deeds of charge for security.

4 Risk Control Limits

4.1 Liquidity

4.1.1 Committed and Uncommitted Facilities

The Council shall maintain, as a minimum, sufficient approved financing facilities to cover at least 120% of the peak cumulative anticipated net debt requirements on a rolling 12-month basis.

4.1.2 Maturity Profile of Committed Facilities

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 million. The relevant debt is the total external debt for the Council excluding any leases, table loans and floating rate short-term loan issues. This ratio must be reviewed by the Treasury Review Team if the Council's long-term credit rating from Standard and Poor's falls below AA-.

4.1.3 Liquidity Parameters (Financial management ratios)

a) Total external debt as a percentage of total assets of the Council/CCHL shall be no more than 12%.

b) Total external debt of the Council/CCHL combined as a percentage of realisable assets, (all assets excluding infrastructure and restricted assets), shall be no more than 33%.

c) The ratio of net external debt of the Council/CCHL to funds flow from operations shall not exceed five; i.e. an ability to repay debt over five years. (This calculation excludes net capital additions).

d) Net interest paid on term debt by the Council/CCHL will not exceed 8% of the consolidated gross revenue.

e) Should interest rates rise above 8.5%, the Chief Executive will recommend new ratios to Council.

Note 1: 'term debt' is defined as gross debt less dedicated debt repayment reserves, and 'net external debt' is total debt less all other cash reserve funds.

Note 2: when calculating financial management ratios, the debt levels and liquid investments of Christchurch City Holdings Limited, parent only, are added to the Council figures. Similarly, any reference to consolidated figures means the sum of the Council and CCHL, parent only, numbers.

4.1.4 Funding

a) Borrowed funds will be used to fund capital expenditure, equity investment or to meet short-term liquidity requirements. For the purposes of this clause "short term" means for less than one year.

b) 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 LTCCP and/or the Annual Plan.

c) Except as qualified in clauses (d) and (j) below, all external debt of the Council, including financial leases, must be authorised by the LTCCP or a separate resolution of the Council.

d) The aggregate amount the Council determines as not being so significant as to require specific authorisation under Section 112 (c) (ii) (A), of the Local Government Act 2002, is $1million.

e) Loans raised by the Council should normally be secured by a charge on rates revenue. The Chief Executive is authorised to execute a charge instrument charging rates revenue for the benefit of lenders to Council. Council may authorise other security in special circumstances.

f) Except as qualified in clause (g) below, new loans raised in any particular year are to be no greater than the amount disclosed in the LTCCP and applied only to capital projects and investments listed in that Plan.

g) All new loans required to fund expenditure which was not provided for in the Annual Plan shall require Council approval by a specific resolution of the Council, including the reasons that the expenditure was not originally included. Staff shall have evidence of such approvals before any debt is raised.

h) Where a loan is raised to fund a specific asset, its term must not be longer than the economic life of the asset it funds, except in the case of equity investments. In all cases the term of a loan may be up to, but not longer than, 30 years.

i) A loan may be raised in several parcels for terms less than the economic life of the capital asset it funds or the 30-year maximum loan term permissible. Repayments at maturity of a parcel 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 longer than 30 years.

j) Unless the Council resolves to the contrary and subject to any instruction issued by the Chief Executive, loan funds may be raised by way of bank overdraft to cover short-term cash shortfalls limited to a maximum of $2 million. 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 Chief Executive within two working days. For the purposes of this clause, “short-term” means for terms of less than one year.

k) Debt may be repaid by one or a combination of the following:

   i. 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;

   ii. Annual Contributions to a Loan Repayment Reserve held by the Council for the sole purpose of repayment or reduction of loans;

   iii. Annual table repayment instalments providing for full repayment over the term of a loan being 30 years or less;

   iv. Repayment from revenue or other sources.

l) Debt will be used as a residual funds source after funds generated from depreciation and appropriate capital revenues 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.

m) With the exception of table loans, a minimum of 1.4% of the aggregate of the initial external debt raised by the Council/CCHL shall be repaid annually in accordance with one or a combination of the options set out in (k) above. Where the term of the initial external debt is less than 30 years, an appropriate (higher) rate will be used to ensure repayment within the term. Initial external debt is defined as the original sum of any loan borrowed which has not been fully repaid. Any annual debt repayment provision will be funded from operating revenue.

n) The rate shall be reviewed annually to ensure that with accumulated interest earnings on invested funds, sufficient funds would be available to repay each initial loan parcel at the end of the term.

o) Surplus Sinking Funds and Loan Repayment reserves may be applied to earlier repayment of loans in conjunction with refinancing of parcels, or to the financing of other capital works.

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

q) The Treasury Review Team may select the specific debt to be repaid in any one year to optimise the mix of debt types retained within the group.

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

s) Where a specific debt-raising resolution requires more restrictive delegation, the requirements of that resolution shall be followed rather than the general parameters of this policy.

4.2 Risk Management Parameters

4.2.1 Interest Rate Management

a) As a benchmark, 75% of all unmatched long-term debt should generally be on a fixed-rate basis, although the Treasury Review Team has the discretion to vary this proportion in a range between 50% and 100%. To the extent that interest rates on borrowing are matched by corresponding interest income streams calculated on the same basis, they may be excluded from this calculation.

b) Net short-term interest rate exposures (i.e. after netting short-term debt with short-term investments) should be managed in the context of the Council's investment intentions, cash flow projections and the current external environment.

c) For the purposes of this policy, floating rate debt is where interest rates re-price within three months of the current month end. Fixed rate debt is where interest rates are fixed for a period greater than three months from the current month end.

d) Derivative interest rate instruments may be used to hedge interest rates under the following circumstances:

   i. They must be applied to a specific class of existing or committed debt or investment of the Council;

   ii. They may be used to avoid an exposure to adverse rates based on the interest rate view formed by the Treasury Review Team;

   iii. They may be used to change the mix of fixed and floating rate debt;

   iv. All hedging contracts longer than twelve months must be discussed with the Director, Strategic Investment, or General Manager, Corporate Services, before being transacted;

   v. Contracts to be taken for periods longer than ten years must be discussed in advance with the Treasury Review Team.

e) Derivatives may not be used for speculative purposes under any circumstances.

4.2.2 Approved Hedging Instruments

a) Interest rate swaps;

b) Forward Rate Agreements (FRAs);

c) Bought options on FRAs, swaps or government bonds;

d) Sold options on FRAs, swaps or government bonds, but only as an integral part of a 1:1 collar;

e) All derivative contracts entered into shall be reported to the Treasury Review Team on the day of the transaction.

4.2.3 Hedging Counterparties

a) All hedging counterparties must be a Registered Bank in terms of the Reserve Bank Act and have a long-term credit rating of 'A' or above from Standard and Poor's, or equivalent from another recognised credit rating agency.

b) Other approved counterparties include the Council, and CCHL subsidiaries, and other recognised financial intermediaries with the appropriate credit rating.

c) The following table summarises minimum credit rating requirements and limits:

Counterparty's Minimum S&P Short-Term Credit Rating	Counterparty's Minimum S&P Long-Term Credit Rating	Total Exposure Limit for each Counterparty
A1+	AA-	$50 million
A1	A	$20 million

d) If any counterparty's credit rating falls below the minimums specified in the above table, all practical steps are to be taken to reduce the credit exposure to that counterparty to zero as soon as reasonable.

e) Exposure to each counterparty is computed as being the total amount borrowed from that counterparty.

f) All settlements shall be by cleared funds.

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5 Reporting – Council and Management

5.1 Treasury Review Team

The Treasury Review Team will review the following on a monthly basis:

a) Cash/debt position; the tracking of cash flow and debt levels against plan, the reasons for variances and updated future cash/debt projections;

b) Risk exposure position; the Council's current interest rate position including underlying physical exposures, hedges in place and the actual net risk position, compared to the risk control limits of the policy;

c) Policy compliance; conformity with policy limits and requirements in the areas of liquidity/funding risk, counterparty credit risk, operational risk and debt covenants and ratios;

d) Funding facility report; actual loans against limits;

e) Cost of funds report; actual cost against plan.

5.2 Council

A summarised report incorporating key elements of (a) to (e) above will be made to the Audit and Risk Management Subcommittee twice yearly and the Subcommittee shall make regular progress reports to Council on the management of treasury operations and results.

6 Performance Measurement

6.1 Review

Measuring the effectiveness of the Council's liability and related interest-rate management activities is achieved through objective measures as follows:

a) Adherence to policy;

b) Comparison of actual monthly and year-to-date borrowing margins against budget rate (as per the Annual Plan) and, for public issued securities, similar New Zealand rated entities issuing into the New Zealand securities markets;

c) Comparison of the financial covenants and ratios to actual borrowing.