Liability management policy

Effective 1 July 2018

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Author: Northland Regional Council
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Northland
REGIONAL COUNCIL

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Introduction

This document presents the council's policies for managing its borrowing and other liabilities, including its policies on interest rate exposure, liquidity, credit exposure and debt repayment.

This policy should be read in the context of the council's Financial Strategy, which outlines the key financial parameters and limits the council operates within; and the Revenue and Financing Policy which covers how the council funds its activities.

This policy applies to all liability management activity undertaken by the council from 1 July 2018. We review this policy at least every three years.

Management of borrowings and other liabilities

The council's borrowings and other liabilities will be managed to meet the council's expectations of interest rates, liquidity and credit risk exposure.

Council (governance)

- Approve Liability Management Policy, including key limits
- Review liability management performance against policy
- Approve borrowings

Audit and Finance Working Party (governance)

- Review Liability Management Policy, including key limits, and recommend to council
- Recommend policy changes to council
- Recommend borrowings to council
- Receive performance reports from Finance, report to council

Finance (management & staff)

- Develop Liability Management Policy, including key limits
- Develop policy changes
- Continually develop and improve liability management and reporting tools
- Manage liabilities to meet the limits of this policy
- Report liability management performance to Audit and Finance Working Party
- Spread risk through use of fixed and floating debt
- Perform liability management transactions within delegated authorities

The council manages debt on a net portfolio basis. Net debt means financial liabilities less financial assets (excluding trade and other receivables)[1].

To fund its activities, the council can borrow externally through a variety of financial instruments, and from a range of market mechanisms, including from the Local Government Funding Agency. It can also access reserve funds internally.

The council will borrow from external sources, including the Local Government Funding Agency, to fund its investment in capital infrastructure.

[1] Section 22, Local Government (Financial Reporting and Prudence) Regulations 2014

To manage its credit exposure, the council will only borrow using widely used financial instruments with creditworthy counterparties. The council will not enter any borrowings denominated in a foreign currency[2].

The council considers and approves its forecast borrowing requirements by approving financial projections in each Long Term Plan and Annual Plan. The council borrows as it considers appropriate and commercially prudent to do so.

Borrowing limits and interest rate exposure

Borrowing and interest rate exposure limits will be reviewed from time to time. These limits will ensure compliance with any applicable covenants. The council may set limits lower than the highest covenant limits if it considers this to be prudent.

Without a credit rating, net external debt will not exceed 175% of total annual revenue. If the council obtains an external credit rating, this limit could increase to 250%.

Interest rate exposure is the impact that movements in interest rates can have on an organisation's financial performance. To manage interest rate exposure:

- net interest on external debt will not exceed:
  - 10% of total annual revenue
  - 25% of annual rates income.
- the council may target a mix of fixed and floating rate external debt to manage the council's expectations of risk and the cost of borrowing. The council shall determine the best mix of fixed and floating rate debt depending on market conditions at the time.

[2] Section 113, Local Government Act 2002

Liquidity

Liquidity management is the management of liquid assets and funding sources to meet both short and long-term commitments as and when they fall due.

The council minimises its liquidity risk by:

- ensuring that the sum of external debt, committed bank (loan) facilities, and liquid funds (liquid investments) is at least 110% of external debt (liquidity ratio)
- maintaining accurate cashflow forecasts and using these to ensure the council always has sufficient liquid funds available to meet both planned and reasonable unforeseen funding requirements
- avoiding maturity and interest rate re-pricing concentrations by (where appropriate) ensuring rates do not mature on the same dates.

Debt repayment

It is a council priority to reduce its long-term debt by ensuring that loan capital is repaid at the end of each loan term, hence avoiding intergenerational debt wherever possible. However, in cases where an asset funded by debt has an intergenerational useful life, intergenerational debt may be considered.

When the council raises debt:

1. The loan will be drawn down as required to fund activities
2. Targeted rates will be collected immediately and invested until needed to repay the loan
3. At the end of the loan term, the full loan will be repaid
4. Further loans may be raised while others are in progress.

Operating surpluses may be applied to the reduction of debt and/or a reduction in borrowing requirements.

Northland
REGIONAL COUNCIL

WHANGĀREI 36 Water Street, Private Bag 9021, Whangārei Mail Centre,
Whangārei 0148; P 09 470 1200 | F 09 470 1202
DARGAVILLE 42 Hokianga Road, Dargaville; P 09 439 3300 | F 09 439 3301
KAITĀIA 192 Commerce Street, Kaitāia; P 09 408 6600 | F 09 408 6601
ŌPUA Unit 10, Industrial Marine Park, Ōpua; P 09 402 7516 | F 09 402 7510
WAIPAPA Shop 9, 12 Klinac Lane, Waipapa 0295; P 09 470 1200 | F 09 470 1202

Freephone 0800 002 004 | **24/7 Environmental Hotline** 0800 504 639 | **Email** mailroom@nrc.govt.nz
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