FINANCIAL MANAGEMENT – POLICY – Borrowing

Policy

This Policy provides for the responsible financial management of loan funding requirements to undertake infrastructure capital projects whilst ensuring the level of Council indebtedness is within acceptable limits to Council, its ratepayers and interested external parties.

Objective

Council will manage its cash on a holistic basis within the constraints of its overall financial strategies and targets. Through this cash management approach, Council must have regard to:

- borrowings in accordance with the needs set out in Council's Delivery Program and Operational Plan (DPOP) and/or Long Term Financial Plan (LTFP).
- due process and consideration being given to the appropriate borrowing vehicles available in order to minimise Council's net interest costs over the term of the borrowing and mitigate interest rate movement risks.

Procedures/Practice

Council recognises that loan borrowings for capital works are an important funding source for Local Government and that the full cost of infrastructure should not be borne entirely by present-day ratepayers, but be contributed to by future ratepayers who will also benefit. Whilst recognising the importance of loan borrowings, Council shouldn't place undue reliance upon loans as a normal course of revenue stream.

Council will restrict all borrowings to identified capital projects that are considered to be of the highest priority and would be detrimental to Council's operations if funded from operating revenue and/or cash reserves (as identified by the adopted budget). Under no circumstances should Council borrow funds for recurrent expenditure.

Borrowing will only be considered as an appropriate funding source in the following circumstances:

- in the context of the strategic objectives of Council
- in the context of long term financial forecasts and objectives
- as an alternative funding source for asset additions
- as a method of spreading the cost of long life (intergenerational) assets.

With Council's diverse operations, the basis in determining whether it is appropriate for Council to obtain borrowings for capital works projects will be guided by the following protocols:

- Capital projects for a service provided by Council that receives user fees and charges, such as water supply, sewerage and waste services etc, should reflect the operating costs of providing the service plus the loan servicing costs in its assessment of user fees and charges for the service provided.
- Capital projects for business enterprise provided by Council that receives user fees and charges, such as saleyards and commercial properties etc, should reflect the operating costs of providing the enterprise plus the loan services costs in its assessment of user fees and charges for the enterprise.
- Other specific capital projects which will not be funded in full or part by user fees and charges such as bridges, community centres, aerodromes etc, should only be considered for loan funding where
the specific project is considered by Council to be beneficial to the majority of ratepayers.

- The term of any borrowing should not exceed the expected life of the capital project's asset being funded.

Council's management of its borrowing portfolio will be determined from its net debt position. Consequently sound cash management practices will dictate that Council will not borrow at higher interest rates when cash reserves funds are invested at lower interest rates. When surplus funds exist, Council will consider applying these funds against planned borrowings however this will be subject to the consideration of maintaining adequate funds for day-to-day management and possible emergency situations faced by Council. It should be noted that Management shall not speculate on interest rate movements when extinguishing planned borrowings from cash reserves.

The risks attached to future movements in interest rates are uncertain in direction, timing and magnitude. To minimise this risk Council will utilise various borrowing mechanisms such as:

- Fixed Interest borrowings (A loan for a fixed term with regular repayments comprising principal and interest, such that at the end of the period the total principal would have been repaid and interest only borrowings)
- Variable Interest borrowings (A loan where principal amounts can be repaid at any time and interest is only payable on amounts of principal outstanding and long term interest only)

Upper Hunter Shire Council loan portfolio may have a mix of fixed and variable borrowings. Council will not set range limits for the mix of fixed and variable borrowings to allow flexibility to adjust in changing circumstances. In order to spread its exposure to interest rate movements, Council will aim to have a variety of maturity dates on its borrowings. Council will be mindful of these issues when making borrowing decisions and will consider the mix of fixed and variable interest rates and loan items.

**Authority to Borrow**

The authority to obtain loan facilities is vested with Council by virtue of the Local Government Act. No officer of Council is authorised to undertake the establishment of a new loan facility without the explicit authorisation of Council obtained following the conduct of an ordinary or special meeting of Council to discuss the proposed borrowing. All borrowings must be approved by Council resolution.

**Borrowing Principles**

The following principles are to be applied when considering undertaking borrowings or other asset financing:

1. **Operating Expenditure** - Council will not borrow funds to meet operating expenditure. This type of expenditure should be funded through operating revenue streams such as rates, fees and charges or operating grants.

2. **Recurrent Capital Expenditure** - Council will not borrow money to fund the acquisition, replacement or renewal of assets that is expected to occur on an annual or similar basis at approximately the same level each year, i.e. recurrent capital works such as road resurfacing, regular plant replacement etc. This type of expenditure shall be funded through operating revenue streams such as rates and user fees and charges.

3. **Borrowing Term** - The term of the borrowing shall be set having due regard to the economic life of the asset being acquired or constructed.

4. **Borrowing Limitations** - Prior to undertaking any borrowing, Council shall assess its capacity to repay and ensure that the community is not burdened with unnecessary risk. Council shall then reassess its capacity to repay on an annual basis as part of its budgeting process. As part of this assessment, the following borrowing limitations apply:
   - total unrestricted debt servicing costs must not exceed 2% of annual general revenue
   - the term for all new borrowings shall be matched, where appropriate, to the life of the asset to which it relates, however no loan term shall exceed a period of 20 years
   - Council does not establish Sinking Funds for new borrowings
   - borrowings shall only be obtained from Australian sources and in Australian currency so as to
ensure Council is not exposed to foreign currency risks

- any borrowing activities will be conducted in accordance with relevant statutory requirements as contained in the Local Government Act 1993 and the Local Government (General) Regulations 2005.

5. Determining the appropriate Lending Institution - Three written quotations shall be sought, or a loan tender called, in order to determine the appropriate lending institution for any loan borrowings. Determination of the appropriate institution will be based on the interest rate and loan costs offered, the terms and conditions of the loan and the financial stability of the lender.

References

- Local Government Act 1993
- Local Government (General) Regulation 2005
- Ministers Borrowing Order – Revised 29 May 2009
- INT-29089/16

This policy was adopted by Council at its meeting on 31 October 2016 and replaces the policy of the same title adopted by Council on 27 April 2015.

Review Date

October 2020, by the Finance Manager.

Authorised by: Waid Crockett, General Manager

Date: 31 Oct 2016