

# POLICY

## Financial Management - Borrowings

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Responsible officer	Manager Finance
Department/Section	Corporate Services
Category	Financial & Asset Management
Community Strategic Plan goal	Responsible Governance <b>5.3</b> - Effective financial and asset management to ensure Council's long-term sustainability



## Policy Statement

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:

- the regulatory requirements of the Local Government Act 1993, Local Government (General) Regulations 2005 and the Minister's Borrowing Order (Revised 29 May 2009).
- borrowings are entered into in accordance with the needs set out in Council's Delivery Program and Operational Plan (DPOP) and Long Term Financial Plan (LTFP).
- If Council is required to increase its proposed borrowings or change the purpose of the initial borrowings as set out in the DPOP and LTFP, a council resolution must be adopted prior drawing down of any funds.
- due process and consideration being given to the appropriate borrowing options available in order to minimise Council's net interest costs over the term of the borrowing and mitigate interest rate movement risks.

## Scope

This policy applies to the provision of loan borrowings from financiers to facilitate the future capital expansion of Council's infrastructure and to acquire strategic assets, as and when required in the interest of the Community.

## Definitions

<b>Act</b>	Local Government Act 1993 (NSW)
<b>Borrowings</b>	Funds obtained from financiers
<b>Debt service cover ratio</b>	Calculated as adjusted operating result adding back interest, depreciation and asset disposals divided by total annual loan repayments.
<b>DPOP</b>	Delivery Program and Operational Plan
<b>Fixed</b>	Pre-determined number, percentage or period
<b>Interest</b>	Cost of funds borrowed or return on funds invested
<b>LTFP</b>	Long Term Financial Plan
<b>Reserves</b>	Funds available for disbursement on Council operations and projects
<b>Vested</b>	In control and/or ownership of Council



## Policy Details

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 receive 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 enterprises provided by Council that receives user fees and charges, such as saleyards, aerodromes 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, 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:

- i. 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 borrowings would have been repaid)
- ii. interest only borrowings

Upper Hunter Shire Council loan portfolio is based on fixed interest rates only so as to have certainty over future budgeted cash flow requirements to service loan borrowings. In order to spread its exposure to interest rate movements, Council will aim to have a variety of maturity dates on its borrowings.

### **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 authorisation of Council. 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 or re-sheeting, sewer & water mains and pipes renewal, 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 operating debt service cover ratio must be greater than 2x.
  - 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 30 years
  - 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.



## Bank Overdraft

Council maintains an overdraft limit for its main working account held at the Westpac Bank.

The bank overdraft facility may be utilised during the course of the financial year only as a cash management tool to smooth out seasonal or temporary fluctuations in cash flows.

The bank overdraft facility is a form of borrowing that is a high cost alternative relative to other forms of funding. The bank overdraft facility shall be limited to minimal use under the authorisation of the Director of Corporate & Community Services and / or Manager Finance.

It is not appropriate for overdraft facilities to be used for medium or long term financing purposes (for example, to purchase assets) and not to be used as an alternative to borrowing.

At no time is the overdraft facility to be used as an outgoing debt facility or to fund anything except short-term cash flow.

The Manager Finance is responsible for monitoring and managing the day to day cash flow requirements of Council and also for ensuring the cash flows are managed in such a way as to minimise the use of the overdraft facility.

Details of any use of overdraft facilities are to be included in Council's monthly finance reporting.

## Responsibilities

### Councillors

Councillors will review and endorse the Policy.

### Particular/relevant Director

The Director Corporate Services will act as per Delegations of Authority.

### Particular/relevant Manager

The Manager Finance will adhere to the Policy.

## References and Related Legislation

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

## Version History

Version No.	Date	CM Ref#	Reason for Review
1	08/12/2020	CD-216/20	Policy expiry date due for review.
2	28/11/2022	CD-63/22	Policy expiry date due for review.