

3.8 Internal Debt Management

Attachment 5 to Report 99.717

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Internal Debt Management

The treasury function is responsible for administering the Council's internal debt portfolio. Loans are set up within the internal debt portfolio based on planned loan **funded** capital expenditure (or operating expenditure in the case of forestry), and allocated to the department requiring the loan funding. The following operational parameters apply to the management of the Council's internal debt portfolio:

- Capital expenditure details and other internal borrowing requirements are extracted by the Financial Analyst at month end.
- A notional internal loan is set up for all new capital expenditure and other internal borrowing requirements and allocated in the internal portfolio to the department incurring the expenditure.
- Interest is charged by treasury to departments on month-end loan balances at an agreed rate.
- The interest rate is based on the Council's expected weighted average cost of funds, and takes into account factors such as the Council's long term cost of **funds**, anticipated cost of new debt over the next eighteen months, recovery of treasury's operational costs, pricing to reflect the different communities of interest, and a small buffer which provides for certainty in the charging rate and avoids frequent adjustments. The internal rate is reviewed annually and is capped for the next financial year. Where the actual weighted average cost of debt moves to be lower than the budget, an adjustment is made to departmental debt servicing costs (this adjustment is processed at year end).

Treasury uses the internal debt portfolio as an input into determining its external debt requirements. Where possible, the Council's reserves are used to reduce external debt, effectively reducing the Council's net interest cost.

Internal Borrowing Limits

Internal borrowing limits are set to monitor the level of debt utilised by departments and business units. The ratios are consistent with the Council's external borrowing limits outlined in Section 3.2 and consistent with the principle of prudent financial management.

The following limits are monitored monthly by the TMG:

Activity	Ratio	Limit
Regional Water Supply	Net Debt to Levy	300%
Regional Water Supply	Net Financial Costs to Levy	40%
Flood Protection Western Region	Net Debt to Rates	400%
Flood Protection Western Region	Net Financial Costs to Rates	50%

Activity	Ratio	Limit
Flood Protection Wairarapa Region	Net Debt to Rates	80%
Flood Protection Wairarapa Region	Net Financial Costs to Rates	10%
Regional Parks	Net Debt to Rates	50%
Regional Parks	Net Financial Costs to Rates	10%
Corporate Properties	Net Fin Costs to Revenue	50%
Corporate Properties	Debt to Inv's & Cap assets	75%
Forestry	Net Debt to Market Value	60%

In addition, the TMG monitors internal debt targets for each area where there is significant internal debt.

Internal Debt Targets have been established in addition to internal debt limits in order to provide guidance on the long term sustainable debt levels within each area of Council's activity. (N.B. compliance will be monitored primarily against the internal debt limits rather than the internal debt targets.)

The Internal Debt Targets are as follows:

Activity	Ratio	Limit
Regional Water Supply	Net Debt to Levy	220%
Regional Water Supply	Net Financial Costs to Levy	20%
Flood Protection Western Region	Net Debt to Rates	250%
Flood Protection Western Region	Net Financial Costs to Rates	25%
Flood Protection Wairarapa Region	Net Debt to Rates	80%
Flood Protection Wairarapa Region	Net Financial Costs to Rates	10%
Regional Parks	Net Debt to Rates	50%
Regional Parks	Net Financial Costs to Rates	10%
Corporate Properties	Net Fin Costs to Revenue	30%
Corporate Properties	Debt to Inv's & Cap assets	145%
Forestry	Net Debt to Market Value	35%