

Opinions of the State Council on Strengthening the Administration of Local Government Debts

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Note: English version for reference only, Chinese version shall prevail.

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People's governments of all provinces, autonomous regions and municipalities directly under the Central Government, as well as all ministries and commissions of and all agencies directly under the State Council,

The following opinions are hereby set forth in accordance with the spirit of the 18th National Congress of the Communist Party of China and the Third Plenary Session of the 18th CPC Central Committee, in order to strengthen the administration of local government debts and promote the sustainable and healthy development of national economy:

I. General Requirements

1. Guidelines.

Under the guidance of the Deng Xiaoping Theory, the important thought of Three Represents and the Scientific Outlook on Development, by comprehensively implementing the spirit of the 18th National Congress of the Communist Party of China and the Third Plenary Session of the 18th CPC Central Committee, and following the decisions and arrangements of the CPC Central Committee and the State Council, a management mechanism for local government debts featuring consistency in borrowing, utilization and repayment shall be established, to effectively play the positive role of local governments' well-regulated borrowing of money, prevent and defuse fiscal and financial risks financial, and promote sustained and healthy development of the national economy.

2. Basic Principles.

Combining authority granting and regulation. Grant local governments with the authority to conduct debt financing legally and appropriately, and accelerate the establishment of a well-regulated debt financing mechanism for local governments. Meanwhile, local governments are strictly prohibited from borrowing money in violation of laws and regulations.

Clarifying responsibilities. The responsibilities of the government and the enterprise shall be specified clearly. A government shall not borrow money in the name of an enterprise, whereas an enterprise shall not rely on the government to pay off its debt, so that the party borrowing money shall repay the debt and assume the relevant risks on its own. Where public-private partnership is involved, the relevant responsibilities shall be assumed by the parties concerned according to the rules as agreed and the law.

Regulating management. Control the scale of local government debts, strictly define the procedures for government borrowing and the uses of funds, and include local government debts in full-covered budget management according to their classes and categories, so as to achieve consistency in borrowing, utilization and repayment.

Preventing risks. Firmly hold on to the principle that no regional or systematic risk occurs, and effectively prevent and resolve fiscal and financial risks.

Achieving progress steadily. To strengthen debt management, it is necessary to be proactive, prudent and steady in dealing with the relevant affairs. When regulating the management, governments must properly handle the stock of debts, to ensure the orderly progress of projects under construction.

II. Accelerating the Establishment of Standard Debt Financing Mechanism for Local Governments

1. Granting local governments with the authority to borrow money legally and appropriately.

Upon approval of the State Council, governments of provinces, autonomous regions and municipalities directly under the Central Government may borrow money moderately, and the governments at city and county levels that really need to borrow money shall have the money borrowed by the governments of their corresponding provinces, autonomous regions and municipalities directly under the Central Government on behalf of them. A clear boundary shall be drawn between governments and enterprises. Governments may borrow money by themselves or through departments under them only, and shall not borrow money through enterprises or public institutions.

2. Establishing well-regulated debt financing mechanism for local governments. Local governments may borrow money by way of issuing government bonds. For the development of public-good undertakings without any source of income, where it is really necessary for a government to bear a general debt, the local government shall issue general bonds for financing, and the debt will be repaid mainly with the general public budget revenues. For the development of public-good undertakings with certain sources of income, where it is really necessary for a government to bear a special loan, the local government shall

issue special bonds for financing, and the debt shall be repaid with the corresponding government funds or special revenues.

3. Promoting the application of public-private partnership (PPP) model. Private partner is encouraged to participate by franchising or other means in investments and operations regarding public-good undertakings with certain sources of income such as urban infrastructure. Governments may enable the investors to gain long-term and stable income according to the rules on franchise, reasonable pricing, financial subsidies and other benefits as agreed which are published in advance. The investors make investments in accordance with market-based principles, and set up special purpose companies independently or jointly with the governments to build and operate the partnership projects in accordance with the agreed rules. Investors or special purpose companies may borrow money and assume the repayment liability by obtaining bank loans, issuing corporate bonds, project revenue bonds, asset securitization and other market-based approaches. Governments assume the liability relevant to the franchising, reasonable pricing and financial subsidizing to the investors or special purpose companies according to the agreed rules, and do not bear the repayment liability of investors or special purpose companies.

4. Strengthening the regulation of governments' contingent liabilities. The function of government financing shall be separated from the financing platform companies, and the financing platform companies shall not increase government debts. Local governments shall strictly limit their newly incurred contingent liabilities to the scope with legal guarantee, and assume the relevant responsibilities in accordance with the guarantee contracts. Local governments should strengthen their statistical analysis and risk prevention and control for contingent liabilities, and effectively perform the relevant regulatory work.

III. Implementing Scale Control and Budget Management for Local Government Debts

1. Implementing scale control of local government debts. Local government debts shall be subject to quota management, without exceeding the approved quotas. The scales of general and special debts of local governments shall be included in the quota management, determined by the State Council and submitted to the National People's Congress (NPC) or its Standing Committee for approval. The quota for each region shall be calculated by the Ministry of Finance within the scale of local government debt approved by the NPC or its Standing Committee based on the debt risks, financial conditions and other factors regarding each region and submitted to the State Council for approval.

2. Strictly defining the procedures for local government borrowing and the uses of funds. Local governments must report the borrowings within the quotas for their regions as approved by the State Council made by them to the people's congresses or their standing committees at the corresponding level for approval. Local governments may not borrow money through enterprises and public institutions. They shall make loans in compliance with the market-related principles. Efforts shall be made to establish a credit rating

system regarding local governments, and gradually improve the market of local government bonds. The borrowings made by local governments may only be used for the public welfare spending and the moderate repayment of stock of debt, and not for recurrent expenditures.

3. Including local government debts into the full-covered budget management according to their classes and categories. Local governments shall include the income and expenses related to general debts into the management of general public budget, and the income and expenses related to special debt into the management of government fund budget, and the expenses such as financial subsidies for PPP projects into the corresponding government budget management by nature. Departments and units under local governments shall include the debt-related income and expenses into their budget management. For contingent debts, where it is really necessary for local governments or the departments or units thereunder to bear the liability for repayment according to the law, the funds for repayment shall be included in the appropriate budget management.

IV. Controlling and Eliminating Local Government Debt Risks

1. Establishing an early warning mechanism for local government debt risks. The Ministry of Finance shall, according to the information on general debts, special debts, contingent liabilities, etc., calculate the debt ratio, new debt ratio, debt servicing ratio, overdue debt ratio and other indicators, and assess the debt risks in each region, to make early warnings against the regions with high debt risks. The regions with high debt risks included in the scope of early warning shall actively take measures to gradually reduce risks. The regions with relatively low debt risks shall reasonably control the scale and growth rate of outstanding debts.

2. Establishing an emergency response mechanism for debt risks. It is imperative to harden budget constraints and prevent moral hazards; local governments bear the liability for repayment of the borrowings made by them, the Central Government implements the no-bailout principles. Governments at all levels shall develop emergency response plans and set up accountability mechanisms. When facing difficulties in debt repayment, local governments shall repay the debts by raising funds through multiple channels by controlling the project scale, reducing public spending, disposing of stock assets, and other ways. Where it is difficult for a local government to repay the debts on its own, such local government shall promptly report the case to its superior government; such local government and its superior government shall initiate the emergency response plans for debt risks and accountability mechanisms to effectively resolve the debt risks and investigate the responsibility of relevant personnel.

3. Strictly enforcing financial discipline. Establish a punishment mechanism regarding financing in violation of laws and regulations as well as illegal use of the funds from local government debt and strengthen supervision and inspection of the management of local government debts. Local governments and departments thereunder shall not borrow money beyond the scope of the budget illegally, borrow money

for recurrent expenditures or government building construction in the name of supporting the development of public welfare undertakings, or embezzle debt funds or change the intended uses of the funds; must comply with laws and regulations in acts such as investing capital into enterprises and granting fiscal subsidies, and may not illegally provide guarantee for the debts of any entity or individual by any means; and may not illegally interfere with the normal business activities of financial institutions, nor force financial institutions and other organizations to provide government financing. Local governments shall further regulate the management of land transfer, and resolutely prevent illegal land transfers and financing activities.

V. Improving Supporting Systems

1. Improving the debt reporting and disclosure system. Improve the statistical reporting system for local government debts, and accelerate the establishment of comprehensive government financial reporting system on an accrual basis, to fully reflect the assets and liabilities of the governments. For government debts arising from implementation of major policies and initiatives introduced by the Central Government such as shanty-town transformation, separate statistics, accounting, inspection and assessment shall be carried out. Efforts shall be made to establish a disclosure system for local government debts and strengthen the development of government credit system. Each region shall periodically disclose the information on government debts and progress of projects within the region, and consciously accept social supervision.

2. Setting up assessment accountability mechanisms. Government debt shall be included in the performance assessment of an official's political career as a mandatory indicator. With the responsibilities put in place clearly, the governments of all provinces, autonomous regions and municipalities directly under the Central Government shall be responsible for the local government debts within their regions. Education and assessment shall be strengthened to correct misleading practices in attaining political achievements. The relevant responsible persons shall be held liable for acts such as borrowing too much beyond the real solvency, borrowing money or providing guarantees illegally, using debt funds illegally, and evading debts maliciously.

3. Strengthening constraints on creditors. Financial institutions and other organizations may not provide financing for any local governments in violation of laws and regulations, or require local government to provide guarantees illegally. Local financial institutions and other organizations shall purchase local government bonds in compliance with regulatory requirements, strictly regulate the credit management when providing financing for enterprise legal persons and other parties that are the entities having contingent government liabilities, and effectively strengthen risk identification and risk management. Where any financial institution or other organization provides government financing illegally, it shall bear the relevant losses on its own, and relevant agencies and personnel shall be investigated for liability in accordance with the laws and regulations including the law on commercial banks and the law on regulation and supervision of the banking industry.

VI. Properly Handling Stock of Debts and Subsequent Financing for Projects in Progress

1. Including the stock of debts into budget management as soon as possible. The stock of local government debts shall be identified based on the audit results of government debts in 2013, in combination with the post-audit increase or decrease in debts, and upon mutual consultation and confirmation by creditors and debtors. The debts incurred by local governments and departments thereunder shall be included in general and special debts accordingly. For the debts incurred by enterprises and public institutions, the part within the scope of debts to be serviced by the governments shall be included into general and special debts accordingly. Local governments shall report the identified stock of government debts upward level by level to the State Council for approval and include it in the budget management by class. For the debts included in the budget management, the original creditor-debtor relationships remain unchanged, and the debt service funds shall be regulated and managed in accordance with budget management requirements.

2. Actively reducing the interest burden arising from the stock of debt. In respect of the identified stock of local government debts included in the budget management, each region may apply for swaps by issuing local government bonds, in order to reduce the interest burden, optimize the maturity structure, and free up more funds for key projects.

3. Properly repaying the stock of debts. Disposal of the stock of debts shall comply with the market rules, with reduction of administrative intervention. For any debt whose principal and interest can be repaid as scheduled with the operating income of a project, the relevant local government shall continue to make repayment with the income of the project. For any debt whose principal and interest cannot be repaid with the operating income of a project, the relevant local government may improve the profitability of the project to enhance the solvency through the measures such as injecting quality assets by law, strengthening management, and intensifying reform. Local governments shall guide and supervise relevant borrowing entities in strengthening financial management, widening the channels for debt service funds, and making overall arrangements for debt service funds. For any debt to be repaid by a local government, the local government shall fulfill the obligations of debt servicing, and may dispose of government assets for repayment of the debt where necessary. Where it is necessary for a local government to perform the obligation of guarantee or bail-out for any debt, the local government shall fulfill the agreement according to the law and make proper arrangements. Relevant borrowing entities and parties holding joint liability shall fulfill the liability for debt repayment in accordance with relevant agreements, specify the time limits for debt repayment, and repay the principal and interest as scheduled; shall not unilaterally change the original creditor-debtor relationship nor shift the debt servicing obligation onto other parties or evade the debts. Where any loss has been generated with respect to any stock of debt, the relevant creditors shall bear the corresponding responsibilities and losses in accordance with commercial principles.

4. Ensuring subsequent financing for projects in progress. Local governments shall make overall coordination for all types of funds, and give priority to the continued construction and closing of projects in progress. For projects in progress that use debt funds, the original lending banks shall review such projects again, and where any project complies the relevant state regulations, the said banks shall continue to provide loans under agreements to promote the project construction; where no other source for construction funds can be found for any project in progress, the subsequent financing shall mainly be solved through the PPP model and issuing local government bonds.

VII. Strengthening Organization and Leadership

All regions and departments shall attach great importance to the management of local government debts, and take action in accordance with the decisions and arrangements of the CPC Central Committee and the State Council. Local governments shall effectively perform the responsibilities of strengthening the management of local government debts and preventing and eliminating fiscal and financial risks, develop specific plans on the basis of the actual conditions, and ensure the implementation of policies with the major principals of the government as the primary responsible persons. A coordination mechanism for local government debts shall be established, to enhance the management of the said debts in a coordinated manner. The finance departments, as the corresponding departments in charge of managing local government debts, shall improve the debt management system, consolidate the debt management capability, and effectively implementing the control of debt scale, issuance of bonds, budget management, statistical analysis and risk monitoring; the development and reform departments shall strengthen the management of government investment programs and relevant project approval, and strict examine and approve new projects in regions with high debt risks; financial regulatory departments shall enhance regulation and correct guidance, and prevent financial institutions and other organizations from providing financing illegally; audit departments shall strengthen the audit and supervision of local government debts according to the law, promote sound debt management systems, prevent risks, and implement well-regulated management, to improve fund utilization efficiency. All regions and departments shall earnestly perform their duties, and strengthen coordination and cooperation, to carry out the work on strengthening the management of local government debts in all respects, and ensure the implementation of policies.