



## **BORROWING POLICY**

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## **1. PURPOSE**

- 1.1. To provide the Municipality with a borrowing framework policy.
- 1.2. Set out the objectives, policies, statutory requirements as well as guidelines for the borrowing of funds.

## **2. OBJECTIVES**

- 2.1. The objectives of the policy are to:
- 2.2. enable the municipality to exercise their obligation to ensure sufficient cash resources to implement capital programme in the most cost effective manner;
- 2.3. ensure compliance with the relevant legal and statutory requirements relating to Municipal borrowing;
- 2.4. govern the taking up of short-term and long-term debt according to the legislative framework
- 2.5. manage interest rate and credit risk exposure
- 2.6. maintain debt with specified limits and ensure adequate provision for the repayment of debt and
- 2.7. To maintain financial sustainability.

## **3. SCOPE OF THIS POLICY**

- 3.1. The primary goal in the borrowing of funds is to ensure that the funds are obtained at the lowest possible interest rates at minimum risk, within the parameters of authorized borrowings.
- 3.2. This policy shall apply the Council, Mayoral Committee, all Portfolio Committees, Accounting Officer, Strategic Executive Directors and all staff of the municipality. It is, however, specifically applicable to the council and all officials who have a formal, administrative duty to deal with capital projects and programmes of the municipality and the management of the budget.

## **4. BORROWING ETHICS**

- 4.1. In dealing with financial institutions, the following ethical principles must be adhered to:
- 4.2. The Chief Financial Officer shall not accede to any influence by or interference from councillors, borrowing institutions or any outsiders.
- 4.3. Under no circumstances may inducements to borrow be accepted.

## **5. LEGISLATION**

- 5.1. The legislative framework governing borrowings are:
  - 5.1.1. Local Government Municipal Finance Management Act, Act 56 of 2003; and
  - 5.1.2. Local Government Municipal Regulations and Debt Disclosure, Regulation R492, published under Government Gazette 29966, 15 June 2007.

## 6. COMPULSORY DISCLOSURE WHEN INCURRING MUNICIPAL DEBT

- 6.1. The Municipal Regulations on Debt Disclosure has been promulgated (Government Gazette no. 29966, 15 June 2007) and has been effective from 01 July 2007 for a municipality or municipal entity. Refer to Annexure A2, Municipal Finance Management Act: Municipal Regulations on Debt Disclosure.
- 6.2. The implementation of the regulations will help to strengthen the level of confidence in municipal fiscal affairs and enable the capital markets to effectively participate by providing access to a range of competitive funding instruments for the provision of municipal infrastructure and other capital development in accordance with section 46 of the Municipal Finance Management Act
- 6.3. In the case of short-term debt it must be disclosed whether the debt is to bridge:
  - 6.3.1. Shortfalls within a financial year during which the debt is incurred, in expectation or specific and realistic anticipated revenue to be received with that financial year; or
  - 6.3.2. Capital needs within a financial year, to be repaid from specific funds to be received from enforceable allocation or long-term debt commitments.
- 6.4. In the case of long-term debt, whether the purposes of the debt is for:
- 6.5. Capital expenditure on property, plant or equipment to be used for the purpose of achieving the objectives of local government, subject to section 46(4) of the Act.
- 6.6. Refinancing of existing long-term debt, subject to section 46(5) of the Act.

## 7. PROCESS

The process as required by the Act is as follows:

### 7.1. Short-term debt

- 7.1.1. A municipality may incur short-term debt only if:
  - 7.1.1.1. A resolution of the municipal council, signed by the executive mayor, has approved the debt agreement; and
  - 7.1.1.2. The accounting officer has signed the agreement or other document which creates or acknowledges the debt.
- 7.1.2. A short term debt transaction may be:
  - 7.1.2.1. approve individually; or
  - 7.1.2.2. approve an agreement with a lender for short-term credit facility to be accessed as and when required, including a line of credit or bank overdraft facility, provided that:
    - 7.1.3. the credit limit must be specified in the resolution of the council;
    - 7.1.4. in terms of the agreement, including the credit limit, may be changed only by a resolution of the council; and
    - 7.1.5. if the council approves a credit facility that is limited to emergency use, the accounting officer must notify the council in writing as soon as practical of the

amount, duration and cost of any debt incurred in terms of such a credit facility, as well as options for repaying such debt.

7.1.6. A municipality:

- 7.1.6.1. Must pay off short-term debt within the financial year; and
- 7.1.6.2. May not renew or refinance short-term debt, whether its own debt or that of any other entity, where such renewal or refinancing will have the effect of extending the short-term debt into a new financial year.
- 7.1.6.3. No lender may wilfully extend credit to a municipality for the purpose of renewing or refinancing short-term debt that must be paid off in terms of subsection 7.1.6.2
- 7.1.6.4. If a lender wilfully extends credit to a municipality in contravention of paragraph 7.1.6.3, the municipality is not bound to repay the loan or interest on the loan.
- 7.1.6.5. Subsection 7.1.6.1 does not apply if the lender:
  - 7.1.6.5.1. Relied in good faith on written representations of the municipality as to the purpose of the borrowing; and
  - 7.1.6.5.2. Did not know and had no reason to believe that the borrowing was for the purpose of renewing or refinancing short-term debt. Long-term debt

**7.2. Long-term debt**

7.2.1. A municipality may incur long-term debt only if:

- 7.2.1.1. A resolution of the municipal council, signed by the executive mayor, has approved the debt agreement; and
- 7.2.1.2. The accounting officer has signed the agreement or other document which creates or acknowledges the debt.

7.2.2. A municipality may incur long-term debt only if the accounting officer of the municipality:

- 7.2.2.1. has, in accordance with section 21A of the Municipal Systems Act:
- 7.2.2.2. at least twenty one (21) days prior to the meeting the council at which approval for the debt is to be considered, made public an information statement setting out particulars of the proposed debt, including the amount of the proposed debt, the purposes for which the debt is to be incurred and particulars of any security to be provided; and
- 7.2.2.3. invited the public, the National Treasury and the relevant provincial treasury to submit written comments or representations to the council in respect of the proposed debt; and
- 7.2.2.4. has submitted a copy of the information statement to the municipal council at least twenty one (21) days prior to the meeting of the council, together with particulars of:
  - 7.2.2.4.1. the essential repayment terms, including the anticipated debt repayment schedule; and
  - 7.2.2.4.2. The anticipated total cost in connection with such debt over the repayment period.

7.2.3. Capital expenditure contemplated in 5.3(a) may include:

7.2.3.1. Financing costs, including:

7.2.3.1.1. capitalized interest for a reasonable initial period;

7.2.3.1.2. Costs associated with security arrangements in accordance with section 48 of the Act;

7.2.3.1.3. discounts and fees in connection with the financing;

7.2.3.1.4. fees for legal, financial, advisory, trustee, credit rating and other services directly connected to the financing; and

7.2.3.1.5. Costs connected to the sale or placement of debt, and costs for printing and publication directly connected to the financing.

7.2.3.1.6. Costs of professional services directly related to the capital expenditure; and

7.2.3.1.7. Such other costs as may be prescribed.

7.2.4. A municipality may borrow money for the purpose of refinancing existing long-term debt, provided that:

7.2.4.1. the existing long-term debt was lawfully incurred;

7.2.4.2. the refinancing does not extend the term of the debt beyond the useful life of the property, plant or equipment for which the money was originally borrowed

7.2.4.3. the net present value of projected future payments (including principal and interest payments) after refinancing is less than the net present value of projected future payments before refinancing; and

7.2.4.4. the discount rate used in projecting net present value referred to in paragraph (c), and any assumptions in connection with the calculations, must be reasonable and in accordance with criteria set out in a framework that may be prescribed.

7.2.5. A municipality's long-term debt must be consistent with its capital budget referred to in section 17(2) of the Act.

## 8. CONDITIONS

Witzenberg Municipality may incur debt only if:

8.1. the debt is denominated in rand and is not indexed to, or affected by fluctuations in the value of the rand against any foreign currency; and

8.2. section 48(3) of the Act has been complied with, if security is to be provided by the municipality.

## 9. SECURITIES

9.1. Witzenberg Municipality may by resolution of its council provide security for:

9.1.1. any of its debt obligations; and

9.1.2. contractual obligations of the municipality undertaken in connection with capital expenditure by the persons on property, plant or equipment to be used by the

municipality or such other person for the purpose of achieving the objectives of local government in terms of section 152 of the Constitution.

9.2. Appropriate security is contemplated in section 48(2) of the Act.

9.3. Other additional conditions to be complied with are contemplated in section 48(3) to (5) of the Act.

## 10. DISCLOSURE

The Municipality must, when interacting with a prospective Lender or when preparing documentation for consideration by a prospective Investor, disclose all relevant information that may be requested or that may be material to the decision of the prospective Lender or Investor. Reasonable care must be taken to ensure the accuracy of any information disclosed. Whilst this is a standard and acceptable business practice, it is also in compliance with section 49 of the Municipal Finance Management Act.

## 11. GUARANTEES

11.1. The Municipal Finance Management Act provides that the Municipality may not guarantee any debt of any entity unless the entity is a Municipal entity under its sole ownership control. The debt must be reflected in the approved business plan of the entity. The guarantee must be authorized by the Municipality. This must be done in the same manner and subject to the same conditions applicable to any other borrowings. Neither the National nor Provincial Government may guarantee the debt of any Municipality.

11.2. Witzenberg Municipality may not issue any guarantee for any commitment or debt of any organ of state or person, except on the following condition:

11.3. The guarantee must be within limits specified in the municipality's approved budget.

11.4. Neither the national nor a provincial government may guarantee the debt of a municipality except to the extent that chapter 8 of the Public Finance Management Act provides for such guarantees

## 12. SUBMISSION OF DOCUMENTS

When entering into discussion with a prospective lender with a view to incur short-term or long-term debt, the following information must be made available to the prospective lender.

12.1. audited financial statements for the preceding three (3) financial years with audited outcomes;

12.2. approved annual budget;

12.3. the municipal integrated development plan;

12.4. Repayment schedules pertaining to existing short-term or long-term debt.

**13. NOTIFICATION TO NATIONAL TREASURY**

All information prescribed in the act must be provided to National Treasury with respect to a long-term debt proposal.

**Information to be provided with respect to a long-term debt proposal**

	<b>Details</b>	<b>MFMA</b>
A	A copy of the <i>information statement</i> required by section 46(3), containing particulars of the proposed borrowing (debt) instrument.	46(3)(a)(i)
B	If not already incorporated in the <i>information statement</i> , the following information should be provided separately (note QBMR = Quarterly Borrowing Monitoring Return to NT, see over page for further information):  amount of debt to be raised through borrowing or other means purposes for which the borrowing (debt) is to be incurred interest rate(s) applicable (state whether fixed or variable etc) planned start and end date (term of instrument) detailed repayment schedule for the duration of the borrowing (debt) (showing dates and all payments of principal and interest, etc) total estimated cost of the borrowing (debt) over the repayment period type of instrument (select from QBMR) security to be provided (select from QBMR) and provide details source of loan funds (select from QBMR)	46(3)(b)(i) and (ii)
C	A schedule of consultation undertaken, including:  date(s) when the <i>information statement</i> was made public details of meetings, media adverts and other methods used to consult on the proposed long-term borrowing (debt)	46(3)(a)(i), (ii)
D	A copy of the approved budget, and relevant documentation supporting the budget, highlighting the asset(s) to be funded by the proposed borrowing (debt) and the revenue to be received. It must be demonstrated that the proposed borrowing (debt) is consistent with the IDP, the capital budget and the revenue is shown accordingly.	46(6) 17(2) 19
E	If the borrowing (debt) is for the purpose of refinancing existing long-term borrowing (debt), the following information:  description of the asset(s) for which the original loan was required the useful remaining life of the asset(s) the net present value of the asset(s), including the discount rate used	46(5)



	and any assumptions in the calculations the net present value of projected future payments <u>before</u> refinancing, including the discount rate and assumptions used. the net present value of projected future payments <u>after</u> refinancing, including the discount rate and assumptions used.	
F	What source of funding will be used to repay the loan? Please specify the revenue stream(s) and whether this is existing revenue, or new revenue.	19(1)(d)
G	Schedule of <u>all</u> long-term borrowing (debt) obligations in the format of the QBMR showing principal and interest payments for the life of <u>all loans</u> and any associated investments set up as sinking funds etc.	
H	A copy of the council/board of directors' resolution approving the borrowing (debt) instrument should be forwarded once approved.	

#### 14. FINANCIAL AFFAIRS OF THE MUNICIPALITY

- 14.1. The following information concerning the financial situation and financial management of the municipality must be disclosed:
- 14.1.1. schedule of all long-term debt obligations stating principal and interest payments for the life of all loans and any security provided to secure such debt;
  - 14.1.2. the amount of any short-term debt outstanding;
  - 14.1.3. the revenue of the municipality for the preceding three (3) financial years stated separately:
  - 14.1.4. Government grants and public donations;
  - 14.1.5. Revenue from rates and service charges and other revenue sources
  - 14.1.6. what source of funding will be used to repay the loan;
  - 14.1.7. details of any default by the municipality on outstanding or repaid debt during the preceding three (3) years;
  - 14.1.8. the reserves of the municipality;
  - 14.1.9. a summary of financial policies and practices; and
  - 14.1.10. The latest credit rating obtained.

#### 15. INTEREST RATE RISK

- 15.1. As a general principle when interest rates are expected to decrease, it is advisable that a floating rate be negotiated in order to take advantage of the lower interest rates in future. If interest rates are expected to increase, it is advisable to obtain a fixed rate so that the benefits of the current low interest rate are maintained.
- 15.2. The interest risk must be limited in so far as possible. The policy directive is to negotiate fixed interest rates for all long-term borrowings. This will ensure stability

of the repayments and reduce the risk for high rates and tariff increases as a result of interest rate hikes in the market.

- 15.3. Variable rates should be considered for short-term debt only.

## **16. LIMITATIONS**

To ensure a financial viable municipality the following ratios are used to determine the municipal gearing ability to borrow:

- 16.1. Long-term credit rating of BBB;
- 16.2. Interest cost to total expenditure to not exceed 8%;
- 16.3. Long-term debt to revenue (excluding grants) not be exceed 50%;
- 16.4. Payment rate mature above 95%; and
- 16.5. Percentage of capital charges to operating expenditure less than 18%.

## **17. PROHIBITED BORROWING PRACTICES**

Witzenberg Municipality shall not borrow for investment purposes, with the sole purpose of investing to earn a return. The cost of debt is almost always more expensive than the return that the Municipality can derive by investing in permitted investments. Foreign Borrowing is permitted in terms of section 47 of the Municipal Finance Management Act, whereby the debt must be denominated in Rand and is not indexed to, or affected by, fluctuations in the value of the Rand against any foreign currency.

## **18. IMPLEMENTATION AND REVIEW**

- 18.1. The Accounting Officer shall be responsible for the implementation and administration of this policy with the assistance of the Strategic Executive Director for Financial Services Department once approved by Council. All future borrowings must be considered in accordance with this policy read with MFMA and Local Government Municipal Regulations and Debt Disclosure, Regulation R492, published under Government Gazette 29966, 15 June 2007 and other directives and guidelines issued by National Treasury.
- 18.2. In terms of section 17(1) (e) of the Municipal Finance Management Act, 2003 this policy shall be reviewed on annual basis to ensure that it complies with changes in applicable legislation and regulation and the reviewed policy tabled to Council for approval as part of the budget process .
- 18.3. This policy must be read together with the Budget and Funding and Reserves Policies; Local Government Municipal Finance Management Act, Act 56 of 2003; and Local Government Municipal Budget and Reporting Regulation, Regulation 393, published under Government Gazette 32141, 17 April 2009.