



BORROWING POLICY

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1. BACKGROUND

The Municipal Finance Management Act (MFMA) Section 18 requires that the annual budget may only be funded from:

- Realistically anticipated revenue to be collected
- Cash backed accumulated funds from previous years' surpluses not committed for other purposes; and
- Borrowed funds, but only for capital projects

Section 19 of the MFMA also required spending on capital projects may only commence once the funding sources considered, are available and have not been committed for other purposes. Furthermore, Chapter 6 of the MFMA guides on the requirements of obtaining short term and long term debt, conditions to comply with when applying for debt, security, disclosures and municipal guarantees.

The Treasury Regulations issued in terms of the MFMA requires each municipality to have a borrowing policy.

2. PURPOSE

To establish a borrowing framework policy for the Municipality and set out the objectives, statutory requirements and guidelines for the borrowing of funds.

To manage interest rate and credit risk exposure. Maintain debt within specified limits and ensure adequate provision for the repayment of debt.

To ensure compliance with Legislation and Council policy, governing the borrowing of funds.

3. DEFINITIONS

"MFMA" means the Municipal Finance Management Act, 2003 (Act No. 56 of 2003);

"municipal debt" means –

- (a) a monetary liability or obligation on a municipality or municipal entity created

by-

- (i) a financing agreement, note, debenture, bond or overdraft;
- or
- (ii) the issuance of municipal debt instruments; or
 - i. a contingent liability such as that created by guaranteeing a monetary liability or obligation of another;

“borrower” will be the Overberg District Municipality

“bullet payment” means a payment where the entire principal of the loan is due at the end of the term of the loan

“lender”, in relation to a municipality, means a person who provides debt finance to a municipality;

“municipality”, Overberg District Municipality;

“short-term debt”, in relation to a municipality or municipal entity, means debt that is repayable over a period not exceeding one year;

“sinking fund” means a fund established by setting aside revenue over a period of time to fund the repayment of a long-term debt;

“long-term debt”, in relation to a municipality or municipal entity, means debt repayable by the municipality or municipal entity over a period exceeding one year;

“security”, in relation to a municipality or municipal entity, means any mechanism intended to secure the interest of a lender or investor, and includes any of the mechanisms mentioned in section 48(2) of the MFMA;

“financing agreement” includes any loan agreement, lease, rental, installment, purchase contract or a hire purchase arrangement under which a Council undertakes to repay a long-term debt over a period.

4. LEGISLATIVE FRAMEWORK

The relevant legislation and regulations in terms of which borrowing decisions are governed is the MFMA.

5. SCOPE FOR APPLICATION

This policy applies to all funds borrowed by the municipality.

6. RESPONSIBILITIES

Officials are required to adhere to:

- 6.1 Written procedures and these guidelines
- 6.2 Exercise due diligence
- 6.3 Prepare all reports timeously
- 6.4 Ensure strict compliance with all Legislation and Council policy

7. GUIDING PRINCIPLES

- 7.1 **Risk Management:** The need to manage interest rate risk, credit risk exposure and to maintain debt within specified limits is the foremost objective of the borrowing policy. To attain this objective, diversification is required to ensure that the Chief Financial Officer prudently manages interest rate and credit risk exposure.
- 7.2 **Cost of Borrowings:** The borrowings should be structured to obtain the lowest possible interest rate, on the most advantageous terms and conditions, taking cognizance of borrowing risk constraints, infrastructure needs and the borrowing limits determined by Legislation.
- 7.3 **Prudence:** Borrowings shall be made with care, skill, prudence and diligence. The standard of prudence to be used shall be the "prudent person" standard and shall be applied in the context of managing overall debt.

8. CONSIDERATIONS

The Municipality from time to time, will use certain of its internal- and/or surplus funds to fund its Capital programme. The utilization of surplus funds enables the Municipality to reduce its reliance on external debt financing, thereby allowing it to borrow only funds from external sources when favorable market conditions prevail.

8.1 Factors to be considered when borrowing:

- The type and extent of benefits to be obtained from the borrowing.
- The length of time the benefits will be received.
- The beneficiaries of the acquisition or development.
- The impact of interest and redemption payments on both current and forecasted income.
- The current and future capacity of the income base to pay for borrowings and the rate of growth of the income base.
- Likely movements in interest rates for variable rate borrowings.
- Other current and projected sources of funds.
- Competing demands for funds.
- Timing of money market interest rate movements and the long term rates on the interest rate curve.
- The Municipality will, in general, seek to minimize its dependence on borrowings in order to minimize future revenue committed to debt servicing and redemption charges.
- The Municipality may only borrow funds, in terms of the MFMA, for the purpose of acquiring assets, improving facilities or infrastructure to provide service delivery.

8.2 Potential lenders include:

- Development Bank of Southern Africa
- Registered Banks in Southern Africa; and
- Other registered approved financial institutions.

9. DEBT REPAYMENT PERIOD

Whilst the period for which loan debt may be received will vary from time to time according to the requirements of the various Lenders, presently the typical debt repayment period for loans in the current economic climate is between 10 to 15 years. Cognizance is taken of the useful lives of the underlying assets to be financed by the debt, and, moreover, careful consideration is taken of the interest rates on the interest yield curve. Should it be established that it is cost effective to borrow the funds on a shorter duration (as opposed to the life of the asset) as indicated by the interest yield curve, the loan will be negotiated to optimize the most favorable and cost effective benefit to the Municipality.

10. SECURITY

The MFMA provides that the Municipality may provide security for any of its debt obligations, including the giving of a lien, pledging, mortgaging or ceding an asset, or giving any other form of collateral. It may cede as security any category of revenue or rights of future revenue. Some Lenders may require the Municipality to agree to restrictions on debt that the Municipality may incur in future until the secured debt is settled.

11. OVERDRAFT

Overberg District Municipality can apply for an overdraft facility. However, while in a sound financial position, this facility will not be utilized or made available. Overdraft facility to be reviewed and approved by Council on an annual basis.

12. SHORT TERM DEBT

The MFMA provides that the Municipality may incur short term debt only when necessary to bridge shortfalls within a financial year during which the debt is incurred, in expectation of specific and realistic anticipated income to be received within that financial year; or capital needs within a financial year, to be repaid from specific funds to be received from enforceable allocations or long term debt commitments.

The Municipality must pay off short term debt within the same financial year and may not renew or refinance its short term debt. The Municipality may, in terms of the MFMA, incur short term debt only if the Chief Financial Officer has made a prior written finding that the debt is either within prudential limits on short term debt as previously approved by Municipality, or is necessary due to an emergency that could not reasonably have been foreseen and cannot await Council approval.

13. DISCLOSURE

Any official involved in the securing of loans by 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 MFMA.

Borrowing is classified into short- and long-term borrowing according to the prescribed municipal standard chart of accounts.

14. APPROVAL OF LOANS BY THE MUNICIPALITY

Section 46 of the MFMA stipulates that the Municipality may incur long-term debt only if a resolution of the Council, signed by the mayor, has approved the debt agreement and the Accounting Officer has signed the agreement or other document which acknowledges the debt. At least 21 days prior to the meeting of the Council at which approval for the debt is to be considered, the Municipality must make 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. The Public, the National Treasury and Provincial Treasury must be invited to submit written comments or representations to the council in respect of the proposed debt. A copy of the information statement must be submitted to Council at least 21 days prior to the meeting to discuss the proposed loan, together with particulars of –

- a. the essential repayment terms, including the anticipated debt repayment schedule; and
- b. the anticipated total cost in connection with such debt over the repayment period.

15. PROVISION FOR REDEMPTION OF LOANS

Overberg District Municipality may borrow from Institutions and set up long term funds to facilitate loan repayments, especially when the repayment is to be met by a bullet payment on the maturity date of the loan. These sinking funds may also be invested directly with the Lender's Bank. The maturity date and accumulated value of such investment must coincide with the maturity date and amount of the intended loan that is to be repaid. Use can also be made of guaranteed endowment policies to facilitate the payment on maturity date.

16. NON-REPAYMENT OR NON-SERVICING OF LOAN

Overberg District Municipality must honor all its loan obligations timeously. Failure to effect prompt payment will adversely affect the raising of future loans at favorable costs of borrowing. In addition to the timeous payment of the loans, the Municipality must adhere to the covenants stipulated in the loan agreements.

17. PROHIBITED BORROWING PRACTICES

In the past some Municipalities have borrowed funds with the sole purpose of investing them to earn a return. The motive was clearly speculative. The cost of debt is almost always more expensive than the return that the Municipality can derive by investing in permitted investments. Consequently, as a principle, Overberg District Municipality does not borrow for investment purposes, but depending on the shape of the interest yield curve may borrow in advance of its capital cash flow needs in a given financial year to take advantage of an inverse interest yield curve. Foreign Borrowing is permitted in terms of section 47 of the MFMA, whereby 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.

18. NATIONAL TREASURY REPORTING AND MONITORING REQUIREMENTS

The Municipality submits numerous returns to National Treasury. It is mainly coordinated by the Budget and Treasury Office. Reporting is in terms of the Budget- and Reporting Regulations.

19. OTHER REPORTING AND MONITORING REQUIREMENTS

Regular reporting mechanisms are in place in order to access the borrowings portfolio and to ensure compliance with policy objectives, guidelines and applicable laws.

19.1 Quarterly activities:

- National Treasury Borrowings return

19.2 General:

- Report actual borrowings (in compliance with Section 71 of the MFMA) to the mayor and Provincial Treasury

Annually:

- Preparation of Annual Budget
- Preparation of Annual Cash Flow
- Forecast Preparation of Annual Financial Statements
- Confirmation of Lender balances at financial year end obtaining written certification of loan balances at year end

22. RELATED POLICIES

The following policies are related to this policy: None

23. REVIEW

The Chief Financial Officer will for the purposes of ensuring that this policy is aligned to the legislation, consider if and when necessary to amend the policy. In the event of the policy not being amended during the budget process, the approved policy will

remain applicable.

24. EFFECTIVE DATE

This policy shall come into effect on 1 July 2023.