MOGALE CITY LOCAL MUNICIPALITY

BORROWING POLICY

2024 -2025

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DEFINITIONS

In this Policy, unless otherwise indicated, a word or expression to which a meaning has been assigned in the respective legislation has the same meaning as defined by said legislation, and –

ACCOUNTING OFFICER/MM – Municipal Manager

BORROWING is the temporary acquisition of money with the intent to repay the amount borrowed.

BUDGET– the local authority's financial plan of action for a multi financial cycle. The two types of budget are operational and capital. Capital budget refers to expenditure on assets with a lifespan of more than one year or expenditure on existing assets that improves the life span of the asset or its productivity. Operating Budget deals with recurrent and short term expenditure, like salaries, phone bills, fuel and stationery.

CFO – Chief Financial Officer

EXCO – Executive Committee

FIXED INTEREST RATE is the rate where the interest rate doesn't fluctuate during the fixed rate period of the loan. This allows the borrower to accurately budget for their future payments.

LOAN is a contract between two parties where one party borrows money from the other on the premise that they will pay it back.

LONG-TERM DEBT is loan that its financial obligations lasting over one year period.

MCLM/THE MUNICIPALITY – Mogale City Local Municipality

MFMA – Municipal Financial Management Act, Act No. 56 of 2003

MSCOA – Municipal Standard Chart of Accounts

SHORT TERM DEBT FINANCING is a form of financing involving financial obligations that must be fulfilled within a year and must be paid off within the same financial year

VARIABLE/FLOATING INTEREST RATE is the rate in which the interest is charged on the outstanding balance. This amount fluctuates as market interest rates change. An advantage of a variable interest rate is that if the underlying interest rate or index declines, the borrower's interest payments also fall and if the interest rate increases the borrower's interest increases.

1. INTRODUCTION

Capital-expenditure (CAPEX) projects planned and conducted by the Municipality, is done so with the aim of long-term economic viability for Mogale City. A universal principle has always stood that current ratepayers should not be fully liable to pay for the development as future ratepayers will also benefit from and make use of these developments. There is a strong economic argument to finance this capital expenditure through long-term borrowing in order to accelerate the pace of delivery and to mirror the repayment of funds with the economic life of the assets. The economic life of assets should always be equal to or longer than the tenure of the debt finance.

The Borrowing Policy, herein after referred to as This Policy, will guide Mogale City Local Municipality (MCLM) in which legislation to apply as well as the rules and regulations regarding both long-term and short-term borrowing (while remaining mSCOA compliant) for the purposes of development.

2. OBJECTIVES OF POLICY

To regulate the borrowing framework of the MCLM with the following specific objectives:

1. to maintain or reduce the average cost of borrowing;
2. to maintain the following financial ratios according to MFMA Circular No. 71:
    a. Interest paid and redemption should not exceed 6% to 8% of total expenditure. Based on the ***2022/23 Annual Financial Statement*** ***R 63 652 823/R 3 501 269 681*100=1.81%*** which is below the norm. Operating below the norm could indicate that the Municipality has the capacity to take on additional financing from borrowing to invest in infrastructure projects. It could also result in cash-flow problems where it is unable to access borrowed funds or the funding decisions of the municipality impacts of these levels. On the other hand, exceeding the norm could pose a risk to the Municipality should changes or fluctuations in financial costs (such as interest charges) arise. When assessing this ratio, the cash-flow requirements of the Municipality should also be considered.
    b. Total borrowings to total operating revenue less operational grants should not exceed 45%. Based on the ***2022/23 Annual Financial Statement*** ***R 189 332 792/R 2 897 733 996*100=6,53%***; which is below the norm. The purpose of the Ratio is to provide assurance that sufficient revenue will be generated to repay liabilities. Alternatively the ratio indicates the affordability of the total borrowings. If the result of the ratio analysis indicates less than 45%, then the Municipality still has capacity to take increase funding from borrowings. However, this should be considered within the cash-flow requirements of the Municipality.

3. LEGISLATIVE FRAMEWORK

Chapter 6 of the MFMA and the National Treasury Municipal Regulations on Debt Disclosure must be complied with. The process as required by the MFMA is as follows:

Section 46

"(2) A municipality may incur long-term debt only if-

(a) a resolution of the municipal council, signed by the mayor, has approved the debt agreement; and

(b) the accounting officer has signed the agreement or other document which creates or acknowledges the debt.

(3) A municipality may incur long-term debt only if the accounting officer of the municipality-

(a) has, in accordance with section 21A of the Municipal Systems Act-

(i) at least 21 days prior to the meeting of 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

(ii) 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

(b) has submitted a copy of the information statement to the municipal council at least 21 days prior to the meeting of the council, together with particulars of-

(i) the essential repayment terms, including the anticipated debt repayment schedule; and

(ii) the anticipated total cost in connection with such debt over the repayment period."

4. APPLICATION AND SCOPE

a. The Borrowing Policy is applicable to all officials and public office bearers within the employ of Mogale City Local Municipality
b. This Policy complies with the legislative mandate
c. Where this policy is in conflict with any law or by-law governing MCLM, the Act or By-Law shall prevail.

5. KEY COMPONENTS OF THE POLICY

5.1. TYPES OF DEBT

This Policy applies to the debt incurred (both short-term and long-term) by MCLM through all forms of borrowing namely:

a. Loans;
b. Leases;
c. Instalment purchase contracts;
d. Hire purchase contracts;
e. Bonds; and
f. All other forms of contractual debenture.

5.2. RAISING OF DEBT

The Municipal Manager is responsible for the raising of debt, but may delegate this function to the CFO. The CFO shall then manage this responsibility in consultation with the MM. All debt shall be raised in strict compliance with the requirements of Section 45(2) and Section 46(2) of the Municipal Finance Management Act 2003 (No.56 of 2003), and only with the prior approval of Council. The Council Resolution has to be signed by the Executive Mayor thereafter. The Accounting Officer has to sign the agreement or any other documentation which creates and acknowledges the debt. The Municipality may only issue guarantees in accordance with the stipulations in Section 50 of the MFMA.

5.2.1. Long Term Debt

Long-term debt shall be raised only to the extent that such debt is provided for as a source of necessary finance in the capital budget of the approved annual budget or adjustment budget. When raising long-term debt, the following should also be taken into account:

- The extent of benefits in incurring debt;
- The length in which these benefits will be received;
- Will it be an additional source of income for the municipality;
- The current revenue vs. the current expenditure;
- Whether the interest rates are fixed or variable; and

- The impact of interest that will be incurred.

5.2.2. Short Term Debt

Short-term debt shall be raised only when it is unavoidable in terms of cash requirements and must be executed in accordance with Section 45 of the MFMA. Whether for the capital or operating budgets or to settle any other obligations, and provided the need for such short-term debt, both as to extent and duration, is clearly indicated in the cash-flow estimates prepared by the CFO. Short-term debt can be increased if there are shortfalls in the financial year and there is a realistic expectation of income generated to settle these debts. Short-term debts also need to be paid within the financial year as per the regulations set out in Section 45(4) of the MFMA. Short-term debt may not be renewed or refinanced where this debt will be carried over on the new fiscal calendar.

5.3. PROVISIONS FOR REDEMPTION OF LOANS

1. Sinking funds may be set up by MCLM to facilitate loan payments. This will be especially beneficial when the loan repayment is met with a bullet or balloon payment on the maturity date of the loan.

2. The maturity date and accumulated value must be directly proportionate to the loan's maturity date and the amount payable by that date.

5.4. MSCOA COMPLIANCE

All municipalities have a chart of accounts. The chart of accounts is a listing of all the accounts used in the general ledger of the municipal entity. This chart is used by the accounting software to aggregate information into the respective municipality's financial statements. MSCOA is the Municipal Standard Chart of Accounts that aims to standardize the chart of accounts of all municipalities and municipal entities within South Africa. The purpose of mSCOA is to accurately record all transactions for more timely financial management which will result in unqualified audit opinions. It will also improve the quality and accessibility of information having the required information tabled for Council decisions. Lastly, it will ensure that the IDP, Budget and Project Plans are aligned thus leading to a positive impact on service delivery. There are 7 segments that need to be complied with namely:

1. Project
2. Function
3. Item
4. Fund
5. Region
6. Costing
7. Municipal Standard Classification

This Policy's compliance to mSCOA regulations and reporting lies in the Funding Segment.

Long-term loans will only be approved in terms of Section 46 of the MFMA for CAPEX projects. When specified CAPEX projects are funded using borrowed funds, this will be recorded and reported in the funding segment of mSCOA compliant reporting. Applications for attaining borrowed funds can only be made if there is a CAPEX project plan in place that is present in the IDP.

To ensure full compliance with mSCOA regulations, the details in the Budget Report, Annual Report, IDP and Annual Financial Statements need to parallel and be aligned to:

a. The Municipality's application and approval for loan funding; and
b. The CAPEX projects the Municipality had intended to use this money for once granted.

Misuse and misappropriation of borrowed funds will be regarded as financial misconduct as well as non-compliance to mSCOA regulations.

5.5. OTHER CONDITIONS

Conditions applying to both short-term and long-term debt.

Section 47 of the MFMA states that - A municipality may incur debt only if-

> *"(a) 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*
>
> *(b) section 48(3) has been complied with, if security is to be provided by the municipality."*

Section 48 (Security) of the MFMA states that

> *"(1) A municipality may, by resolution of its council, provide security for-*
>
> *(a) any of its debt obligations; (If security is provided, there are additional conditions to be complied with)."*

Section 49 (Disclosure) of the MFMA states that -

> *“(1) Any person involved in the borrowing of money by a municipality must, when interacting with a prospective lender or when preparing documentation for consideration by a prospective investor-*
>
> *(a) disclose all information in that person's possession or within that person's knowledge that may be material to the decision of that prospective lender or investor; and*
>
> *(b) take reasonable care to ensure the accuracy of any information disclosed.*

(2) A lender or investor may rely on written representations of the municipality signed by the accounting officer, if the lender or investor did not know and had no reason to believe that those representations were false or misleading.

In addition to the above MFMA requirements, the Debt Disclosure requirements must also be complied with in respect of the information to be provided.

The following Information to be provided to National Treasury with respect to a long-term debt proposal:

	DETAILS	**MFMA**
1	A copy of the information statement required by Section 46(3), containing particulars of the proposed borrowing (debt) instrument.	46(3)(a)(i)
2	If not already incorporated in the *information statement*, please ensure the following information is provided separately (note QBMR = Quarterly Borrowing Monitoring Return to NT, see over page for further information): a. amount of debt to be raised through borrowing or by other means b. purposes for which the borrowing (debt) is to be incurred c. interest rate(s) applicable (state whether fixed or variable) d. planned start and end date (term of instrument) e. detailed repayment schedule for the duration of the borrowing (debt) (showing dates and all payments of principal and interest, etc.) f. total estimated cost of the borrowing (debt) over the repayment period g. type of instrument (select from QBMR)	46(3)(b)(i) and (ii)

	h. security to be provided (select from QBMR) and provide details i. source of loan funds (select from QBMR)	
3	A schedule of consultation undertaken, including: a. date(s) when the *information statement* was made public b. details of meetings, media adverts and other c. methods used to consult on the proposed long-term borrowing (debt)	46(3)(a)(i), (ii)
4	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. A detailed Business Case outlining the need for a loan and return on investments.	46(6) 17(2) 19
5	If the borrowing (debt) is for the purpose of refinancing existing long-term borrowing (debt), the following information: a. description of the asset(s) for which the original loan was required b. the useful remaining life of the asset(s) c. the net present value of the asset(s), including the discount rate used and any assumptions in the calculations d. the net present value of projected future payments before refinancing, including the discount rate and assumptions used. e. the net present value of projected future payments after refinancing, including the discount rate and assumptions used.	46(5)
6	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)
7	Schedule of all long-term borrowing (debt) obligations in the format of the QBMR showing principal and interest payments for the life of all loans and any associated investments set up as sinking funds	

8	Relevant supporting documentation of the borrowing must be submitted; including business case indicating revenue to be received and the life span of the assets.	
9	Please note: a copy of the council's resolution approving the borrowing (debt) instrument should be forwarded once approved.	

6. INTEREST RATE RISK

As a general principle, when interest rates are expected to decrease, it is advisable that a floating/variable interest rate be negotiated in order to take advantage of the lower interest rates in the 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.

In a municipal environment, however, it is advisable that the interest rate risk be limited as far as possible. This will ensure stability in terms of annual rates increases and reduces the potential of unfunded liabilities arising during the year without the ability to adjust the revenue of the municipality.

The policy directive is to negotiate fixed interest rates on all long-term borrowings.

Variable rates should be used for short term debt only.

7. FORM OF BORROWINGS

Long term borrowings will be taken up in the following forms:

- Loans from registered South African banks and/or other financial institutions offering loans,
- Municipal Bonds through the Bond Exchange of South Africa
- Any other accredited institution approved by Council (from time to time)

8. INTERNAL CONTROL MEASURES

8.1. REPORTING AND MONITORING OF DEBT

The Accounting Officer must make certain that all the legal systems and procedures are put into place when attaining borrowed funds. The MM must also ensure the following:

- Duties should be clearly delegated and separated in the borrowing process so as to avoid financial misconduct;
- Loan agreements and contracts be kept in a proper safe custody;

- Senior Management should oversee and verify all payments made from borrowed funds;
- There should be a proper paper trail of documentation regarding all transactions and repayments;
- The Code of Conduct is adhered to; and
- There are proper procedures relating to borrowing and repayment in place and they are adhered to.

The CFO shall, within 10 working days of the end of each month, submit to the Executive Mayor a report describing (in accordance with generally recognized accounting practice) the loan portfolio of the municipality as at the end of the month.

The report must set out the following:

- The capital value of each loan as at the beginning of the reporting period;
- Any changes to the loan portfolio during the reporting period; and
- The capital value of each loan as at the end of the reporting period.

8.2. OTHER REPORTING AND MONITORING REQUIREMENTS

On a MONTHLY basis, the Municipality shall execute the following control and reporting functions in respect of debt incurred through borrowing:

1. Payment requisition verifications and authorization;
2. Maintain schedule of payment dates and amounts;
3. Cash-flow returns submitted to National Treasury;
4. Submission of particulars of borrowings as legislated in Section 71 of the MFMA

On a QUARTERLY basis the Municipality shall execute the following control and reporting functions in respect of debt incurred through borrowing:

1. Submit the National Treasury Borrowing's Return

9. EXTENT OF BORROWINGS

Mogale City's Long Term Financing Strategy will be used as basis to determine the affordability of loans over the Medium Term Revenue and Expenditure Framework (MTREF) period.

The assumptions of the forecast model will be determined on an annual basis depending on the economic climate.

The amount of borrowings for each year will be approved as part of the annual MTREF approval. Terms of conditions as well as the timing of the loan will be submitted for approval as a separate process after the public consultation process (as legislated within the MFMA) has been conducted. The Municipality is obligated to take all measures necessary to repay all forms of borrowed money in the stipulated timeframes.

10. BREACH OF POLICY

This Policy will be considered breached in the following circumstances:

1. The Municipality is liable for all money borrowed and must repay all loans and debts incurred. Failure to comply with payment terms and deadlines will not only be considered a breach in contract but the Municipality will be given a bad credit rating which will compromise it’s position when the Municipality needs to opt for another loan in the future;

2. In addition to timeously repaying all loans the Municipality must adhere to all covenants stipulated in the loan agreement. Failure to adhere will be regarded as a breach in Policy;

3. Failure to comply with any of the legislation, rules and regulations that governs this Policy will also be regarded as a breach in Policy;

4. Failure to report in the mSCOA format will also be a breach in Policy; and

5. Misuse and misappropriation of any borrowed funds will be regarded as financial misconduct and therefore be a breach to this Policy.

11. CONCLUSION

The provision of municipal and social infrastructure to the community should be fast tracked to ensure that the current backlog is eliminated. In addition, the renewal of old infrastructure assets should also be conducted within the timeframes set by National Government. Delays in these developments will be accepted in reasonable, legitimate and legal reasoning; unforeseen circumstances and matters arising beyond the Municipality’s control. Aside from these instances, legislated development has to be completed. In order to achieve these developmental goals timeously, the borrowing of funds will be amongst the myriad sources of funding applied by Municipality.

12. COMMENCEMENT

After the approval of the Municipal Council, this Policy will be in effect from 1 July 2024.