



BUFFALO CITY METROPOLITAN MUNICIPALITY

LONG-TERM BORROWING POLICY

<u>TABLE OF CONTENTS</u>	<u>PAGE</u>
1. Definitions.....	3
2. Introduction and Background.....	4
3. Scope and Application.....	5
4. Objectives.....	6
5. Conditions under which Municipal Debt may be incurred.....	6
6. Security.....	8
7. Approval.....	10
8. Internal Control over Borrowing.....	11
9. Reporting and Monitoring Procedures.....	12
10. Financial Viability.....	13
11. Ratios used to determine the city's ability to borrow.....	14
12. Compliance with financial service provider requirements.....	14
13. Annual Review of Policy.....	18
14. Effective Date.....	18

1. DEFINITIONS

In this Policy, unless the context otherwise indicates, a word or expression to which a meaning has been assigned in the Local Government: Municipal Finance Management Act, 2003 (Act No. 56 of 2003) and / or other related legislation / regulations, has the same meaning as in that Act.

- “**Accounting Officer**” – means the Municipal Manager and *vice versa*;
- “**Act**” – means the Local Government: Municipal Finance Management Act, 2003 (Act No. 56 of 2003);
- “**Chief Financial Officer**” – means an officer of the Municipality, designated by the Municipal Manager to be administratively in charge of the financial affairs of the municipality;
- “**Council**” or “**Municipality**” – means the Municipal Council of Buffalo City Municipality as referred to in Section 18 of the Municipal Structures Act;
- “**Creditor**” – in relation to a municipality, means any person or service provider to whom money is owing by the Municipality;
- “**Debt**” – means –
 - (a) a monetary liability of obligation created by a financing agreement, note, debenture, bond, overdraft or the issuance of municipal securities; or
 - (b) a contingent liability such as that created by guaranteeing a monetary liability or obligation of another.
- “**Delegatee**” – means an official / person delegated to perform tasks on behalf of another person;
- “**Financial Statement**” – means statements consisting of at least –
 - (a) a balance sheet (statement of financial position);
 - (b) an income statement (statement of financial performance);
 - (c) a cash-flow statement;
 - (d) any other statements that may be prescribed; and

- (e) any notes to these statements.
- **“Financial year”** – means a year ending 30 June;
 - **“Financing Agreement”** means any long-term agreement, lease, installment purchase contract or hire purchase agreement under which the Municipality undertakes to pay the capital cost of property, plant or equipment over a period of time;
 - **“Lender”** – in relation to a municipality means a person or service provider who provides debt finance to a municipality;
 - **“Long Term Debt”** – means debt which is repayable over a period exceeding 12 months;
 - **“Municipal debt instrument”** – means any note, bond, debenture or other evidence of indebtedness issued by a municipality, including virtual or electronic evidence of indebtedness intended to be used in raising debt;
 - **“Security”** – means a lien, pledge, mortgage, cession or other form of collateral intended to secure the interest of a creditor;
 - **“Short Term Debt”** – means a debt which is repayable over a period not exceeding 12 months;

2. INTRODUCTION AND BACKGROUND

The Municipality may only incur debt in terms of the Municipal Finance Management Act, Act No. 56 of 2003. The Municipality may incur two types of debt, namely short-term and long-term debt.

2.1 Short Term Debt

The Municipality may incur short-term debt only when necessary to bridge:

- (a) Shortfalls within a financial year during which the debt is incurred, in expectation of specific and realistically anticipated income to be received within that financial year; or

- (b) 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:

- (a) Must pay off short-term debt within a financial year; and
- (b) May not renew or refinance its short-term debt.

2.2 Long Term Debt

(1) A municipality may incur long-term debt only in accordance with and subject to any applicable provisions of this Act, including section 19, and only for the purpose of-

- (a) capital expenditure on property, plant or equipment to be used for the purpose of achieving the objects of local government as set out in section 152 of the Constitution, including costs referred to in subsection

- (4): or (b) re-financing existing long-term debt subject to subsection

- (5). (a) a resolution of the municipal council, signed by the mayor, has approved the

- (b) the accounting officer has signed the agreement or other document which

(2) A municipality may incur long-term debt only if debt agreement; and 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

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

A municipality may borrow money for the purpose of re-financing existing long-term debt, provided that-

(a) the existing long-term debt was lawfully incurred;

(b) the re-financing 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;

(c) the net present value of projected future payments (including principal and interest payments) after re-financing is less than the net present value of projected future payments before re-financing; and

(d) 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.

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

3. SCOPE AND APPLICATION

This policy governs the taking up of new loans, as well as the maintenance and redemption of existing loans. It specifically applies to:

(a) Conditions under which municipal debt may be incurred;

(b) Security;

- (c) Approvals;
- (d) Internal Controls;
- (e) Reporting & Monitoring Procedures;
- (f) Financial viability;
- (g) Ratios used to determine the City's ability to borrow;
- (h) Compliance with financial service provider requirements;
- (i) Compliance with Municipal Regulations on Debt Disclosure;
- (j) Borrowing Process; and
- (k) Notification to National Treasury

4. OBJECTIVES

The objectives of this policy are to:

- (a) ensure compliance with the relevant legal and statutory requirements relating to municipal borrowing;
- (b) record the circumstances under which the Municipality may incur debt;
- (c) describe the conditions that must be adhered to by the Accounting Officer or his / her delegatee when a loan application is submitted to Council for approval;
- (d) set out the internal control measures applicable to the maintenance and redemption of loans;
- (e) ensure timeous reporting on the loans register as required by the Act and in accordance with Generally Recognised Accounting Practice; and
- (f) record the key performance indicators to ensure access to the money markets.

5. CONDITIONS UNDER WHICH MUNICIPAL DEBT MAY BE INCURRED

5.1 Statutory Conditions

The Municipality may incur debt, provided that:

- (a) The debt is denominated in Rand and is not indexed to, or affected by fluctuations in the value of the Rand to other currencies [Sect 47(a) of the Act];
- (b) The debt is approved by resolution of Council, signed by the Executive Mayor, and the Accounting Officer has signed the agreement or other document which creates or acknowledges the debt [Sect 46(2) of the Act];
- (c) The Accounting Officer has, at least 21 days prior to the meeting of the Council at which the resolution is to be considered, published a notice in a newspaper of general circulation:
 - (i) Stating particulars of the draft resolution, including the amount of the loan, the purpose of the loan to be incurred and the particulars of any security to be provided [Sect 46(3)(a)(i) of the Act]; and
 - (ii) Inviting the public to submit written representations to the Council in respect of the draft resolution [Sect 46(3)(a)(ii) of the Act].
- (d) The Accounting Officer has, prior to the adoption of the resolution, submitted an information statement to the Council setting out the purpose for which the debt is to be incurred, the anticipated total cost of credit over the repayment period, the essential repayment terms and particulars of any security to be provided [Sect 46(3)(b) of the Act];
- (e) The relevant resolution was adopted at a meeting of the Council which was open to the public; and

(f) Where security is to be provided, the provisions of section 6 below have been complied with [Sect 47)(b) of the Act].

(g) The table below sets out the information to be provided with respect to long-term debt proposal:

	Details	MFMA
1	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)
2	If not already incorporated in the <i>information statement</i> , please ensure the following information is provided separately (note QBMR = Quarterly Borrowing Monitoring Return to NT, see over page for further information): <ul style="list-style-type: none"> • 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)
3	A schedule of consultation undertaken, including: <ul style="list-style-type: none"> • 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)
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.	46(6) 17(2) 19
5	If the borrowing (debt) is for the purpose of refinancing existing long-term borrowing (debt), the following information: <ul style="list-style-type: none"> • 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 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. 	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 <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.	N/A
8	In the case of a municipal entity, details of any guarantee or other forms of	50

	security to be issued by the parent municipality(s) in respect to the entity's proposed borrowing (debt).	
9	Please note: a copy of the council/board of directors' resolution approving the borrowing (debt) instrument should be forwarded once approved.	N/A

(h) The information detailed above together with the certification of long-term borrowing (debt) should be forwarded the National Treasury and the relevant Provincial Treasury.

Certification for long term borrowing (debt)

Name of municipality / entity: _____

Proposed borrowing (debt): R_____

We hereby certify that the proposed long-term borrowing (debt), as specified in the attached *information statement* and supplementary pages complies with sections 17(2), 19, 46 and 108 of the MFMA and will be used for the purposes of capital expenditure on property, plant or equipment:

- for the purpose of achieving the objects of local government as set out in section 152 of the Constitution;
- capital expenditure is appropriated in an approved multi-year capital budget;
- repayments for the duration of the loan are affordable and will be appropriated in future budgets; and
- if the loan is required to refinance existing long-term borrowing (debt), that the original borrowing (debt) was lawfully incurred and the refinancing does not extend the term of the borrowing (debt) beyond the life of the asset for which the money was originally borrowed.

A copy of the council/board of director's resolution approving the loan will be forwarded to the National Treasury and relevant provincial treasury within 7 days of approval.

Signatures:

Accounting Officer

Mayor/Chairperson of the Board

Name:

Name:

Date:

Date:

5.2 Administrative Conditions

- (a) To obtain Council's approval for a bank overdraft, call bond or short-term loan the Accounting Officer or his / her delegatee must submit:
 - (i) A cash-flow statement indicating the anticipated shortfalls and anticipated further income streams that will repay the short-term debt;
 - (ii) Monthly cash-flow reports indicating progress towards the repayment of the bank overdraft, call bond or short-term loan.

- (b) To obtain Council's approval for a long-term loan the Accounting Officer or his / her delegatee must submit:
 - (i) The Bid Committee's recommendation after having obtained and evaluated quotations from at least three financial institutions stating the loan period (repayment period), comparable interest rates and administrative costs;
 - (ii) An operating budget reflecting the effect of the anticipated depreciation of the envisaged asset to be financed and / or capital costs on service charges; and
 - (iii) Statements from the financial institutions that the proposed instruments are in line with national legislation.

6. SECURITY

- (a) The Municipality may, by a resolution of the Council, authorise security to be provided for any of its debt obligations;

- (b) Without contravening the above point, the Municipality when incurring debt, may:

- (i) Undertake to maintain revenues or specific charges, fees, tariffs or funds at a particular level or at a level sufficient to meet its obligations arising from that debt;
 - (ii) Undertake to effect payment directly from monies or sources that may become available and authorise direct access to such sources to ensure payment of those obligations;
 - (iii) Undertake to make provision in its budget for the payment of those obligations, including capital and interest;
 - (iv) Undertake to deposit funds with the lender or a third party as security for the debt;
 - (v) Agree to specific payment mechanisms or procedures to ensure exclusive or dedicated payment to lenders, including payments into special purpose funds / accounts or other payment mechanisms / procedures;
 - (vi) Cede as security any category of revenue or rights to future revenue specified in the financing agreement or information statement contemplated in 5.1(d) above;
 - (vii) Undertake to have disputes resolved through mediation, arbitration or other dispute resolution mechanisms;
 - (viii) Agree to restrictions on debt which the Municipality may want to incur in future; and
 - (ix) Agree to such other arrangements as the Municipality may consider necessary and prudent.
- (c) A Council resolution authorizing the giving of security as referred to in 6.(a):
- (i) Must determine whether the asset or right with respect to which the security is given, is necessary for providing a minimum essential municipal service; and
 - (ii) If so, must indicate the manner in which the availability of the asset or right for the provision of that service will be protected.

- (d) If the resolution has determined that the asset or right is necessary for providing a minimum essential service, the lender to whom the municipal security is given, may not, in the event of a default by the Municipality, deal with the asset or right in the manner that would preclude or impede the continuation of the minimum essential municipal service.
- (e) A determination in terms of 6(c) that an asset or right is not necessary for providing a minimum essential municipal service is binding on the Municipality until the secured debt has been paid in full.

7. **APPROVAL**

- (a) Once Council approves the loan, the Accounting Officer has to enter into an agreement with the recommended financial institution on behalf of Council. The Chief Financial Officer must ensure that the terms and conditions are as originally agreed before the Council is committed;
- (b) All municipal loan commitments must be recorded in a Loans Register reflecting at a minimum the:
 - (i) Loan number;
 - (ii) Type of loan;
 - (iii) Financial institution;
 - (iv) Date issued;
 - (v) Purpose of loan;
 - (vi) Loan period;
 - (vii) Interest rate;
 - (viii) Installments (capital and interest);
 - (ix) Due dates (quarterly / half-yearly / yearly);
 - (x) Security (if any);
 - (xi) Final redemption date;

- (xii) Opening balance at the beginning of the financial year;
 - (xiii) Amounts received during the financial year;
 - (xiv) Capital amounts redeemed during the financial year; and
 - (xv) Closing balance at the end of the financial year.
- (c) Sufficient provision must be made in the budget to depreciate assets linked to the loan;

8. INTERNAL CONTROL OVER BORROWINGS

8.1 Draw-down claims on loans

Regular claims must be prepared, signed and submitted for processing to the financing institution providing the loan facility.

The following supporting documents must be attached to each draw-down claim:

- (a) Signed copy of Certified Statement, signed by an authorised representative of the Municipality;
- (b) Signed copy of Application for Loan Draw-down, signed by an authorised representative of the Municipality; and
- (c) Expenditure summary listing the expenditure being claimed.

8.2 Repayments made on loans

Loans are paid at the end of each quarter, being September, December, March and June. Payments are made in terms of the amortization schedules or notices from the financing institution for the respective loans due for repayments

The following supporting documents must be attached to each loan repayment:

- (a) Signed copy of requisition; and

(b) Copy of amortization schedule or notice from financing institution detailing the capital and interest amounts due and payable.

8.3 Reconciliations between General Ledger / Loans Register and Financing Institutions

The following reconciliations are performed between the Loans Register, Statements / Amortization schedules of financing institutions and the General Ledger and are examined by a senior official under the direction of the Chief Financial Officer:

(a) Loans Register to General Ledger on a monthly basis;

(b) Capital redemptions per the General Ledger to the redemptions schedule on a monthly basis;

(c) Interest paid per the General Ledger to the interest schedules on a monthly basis; and

8.4 Documentation kept on record

The following loan documentation and certificates, at a minimum, must be safeguarded at all times:

(a) Loan agreements;

(b) Any applicable security agreements;

(c) Copy of annual loans register;

(d) Signed copies of monthly reconciliations;

(e) Copies of all repayments made;

(f) Copies of amortization schedules;

(g) Copies of quarterly National Treasury returns.

9. REPORTING AND MONITORING PROCEDURES

Regular reporting mechanisms shall be put in place in order to assess the overall standing of the Municipality's borrowings and to ensure that the current

borrowings comply with policy objectives, guidelines, applicable legislation and regulations.

As a minimum, the following reports shall be prepared:

9.1 For Internal Treasury management

- (a) A monthly schedule of loans detailing each loan; and
- (b) A monthly reconciliation of all interest / capital repaid and capital received.

9.2 For the Executive Mayor and Council

A monthly report, within 10 working days of each month, on the borrowing portfolio to the Executive Mayor and thereafter to the Finance Portfolio Committee for information, detailing:

- (a) Date issued;
- (b) Interest rate;
- (c) Loan number;
- (d) Reference number;
- (e) Redemption date;
- (f) Institution funding source;
- (g) Opening balance at the beginning of the financial year;
- (h) Amounts received during the financial year;
- (i) Capital amounts redeemed during the financial year; and
- (j) Closing balance at the end of the financial year.

9.3 For External parties

- (a) A schedule of the Municipality's borrowings must be published as part of the annual financial statements;
- (b) Any information to be submitted to the financing institutions and or security providers / guarantors as and when required.
- (c) Borrowings Monitoring return for National Treasury
- (d) Audit certificates from the financing institution(s)

10. FINANCIAL VIABILITY

The Accounting Officer or his / her delegatee must ensure that the Municipality is financially viable and will be able to access the capital market. A report in this regard must be submitted to Council after the completion of the financial statements at the end of every financial year.

11. RATIOS USED TO DETERMINE THE CITY'S ABILITY TO BORROW

To ensure a financially sustainable City, the following ratios are used as guidelines to determine the City's ability to borrow:

- a) Total Debt to Total Assets;
- b) Debt (Total Borrowings) to Total Operating Revenue;
- c) Capital Cost (Interest paid and redemption) to Total Operating Expenditure;
- d) Average interest paid on Debt
- e) Gearing:
- f) Current Ratio
- g) Liquid Ratio

12. COMPLIANCE WITH FINANCIAL SERVICE PROVIDER REQUIREMENTS

12.1 Financial Ratios

- a) Where it has been decided that funding will be sourced externally, the financial service provider may, when considering an application for external debt from the City, take certain ratios into consideration.

- b) The CFO must determine the applicable ratios for long term funding and suggested performance levels.
 - c) The ratios should be monitored to ensure that the City is able to meet its requirements to access external debt from financial services providers of its choice
 - d) Where these performance levels, relating to the financial ratios, are not attained, corrective action should be taken to prevent non adherence to the loan covenant
- (a) The Chief Financial Officer must complete a financial analysis of at least the following ratios and the achievement of the following targets / norms must be included in the report:
- (i) Percentage of Total Debt to Assets:
 - $A = B / C \times 100$; were
 - A = Percentage Debt in relation to Assets,
 - B = [Long-term Liabilities + Current Portion of Long-term Liabilities],
 - C = Total Assets
 - Target = Less than 10%
 - (ii) Debt (Total Borrowings) / Revenue
 - $A = B / C \times 100$; were
 - A = Debt (Total Borrowings) / Revenue
 - B = (Overdraft + Current Finance Lease Obligation + Non-current Finance Lease Obligation + Short Term Borrowings + Long term borrowing)
 - C = (Total Operating Revenue - Operational Conditional Grants)
 - Target = Less than 45%

(iii) A Capital Cost (Interest Paid and Redemption) as a % of Total Operating Expenditure

$A = B / C \times 100$; were

- A = Capital Cost(Interest Paid and Redemption) as a % of Total Operating Expenditure
- B = Capital Cost(Interest Paid and Redemption)
- C = Total Operating Expenditure and Taxation Expense
- Target = Between 6% - 8%

(iv) Percentage of Interest Paid to Operating Expenditure:

$A = B / C \times 100$; were

- A = Percentage Interest Paid in relation to Operating Expenditure,
- B = Interest Paid,
- C = Operating Expenditure
- Target = Less than 5%

(v) Percentage of Total Debt to Equity:

$A = B / C \times 100$; were

- A = Percentage Debt in relation to Equity,
- B = [Long-term Liabilities + Current Portion of Long-term Liabilities],
- C = Funds & Reserves
- Target = Less than 10%

(vi) Gearing:

$A = B / C$; were

- A = Ratio of Equity in relation to Long-term Debt,
- B = Funds & Reserves,
- C = [Long-term Liabilities + Current Portion of Long-term Liabilities]
- Target = Above 10%

(vii) Current Ratio:

A = B / C; were

- A = Current Ratio
- B = Current Assets
- C = Current Liabilities
- Norm = Between 1.5 – 2.1

(viii) Liquid Ratio:

A = B / C; were

- A = Ratio of Cash Assets in relation to Current Liabilities,
- B = Cash Assets (e.g. Call Deposits, Cash, Bank),
- C = Current Liabilities
- *Norm = At least 1.5 : 1*

(ix) Remuneration as % of Total Operating Expenditure

A = B / C x 100; were

- A = Remuneration as % of Total Operating Expenditure
- B = Remuneration (Employee Related Costs and Councillors' Remuneration)
- C = Total Operating Expenditure and Taxation Expense
- Norm = between 25% - 40%

(b) The Accounting Officer must indicate the steps to be taken in order to address deviations from the set targets and / or any other actions required to ensure access to the capital market on a continuous basis.

13. ANNUAL REVIEW OF POLICY

This policy will be reviewed regularly or when so required by changes to legislation. Any changes to this policy must be adopted by Council and be consistent with the Act and any National Treasury regulations.

14. EFFECTIVE DATE

The effective date of this policy shall be 1 July 2023.