Department of Higher Education and Training

Recommended
Borrowing Policy for Public CET Colleges

Free State
CET College
Community Education
and Training College

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AMENDMENT AND APPROVAL RECORD

Issue	Amendment description	Originator	Approved By	Date

Name of CET College: Free State Community Education and Training College		
Borrowing policy		
Department: Finance **Responsibility : Accounting Officer**		
MA Matlawa **Prepared and submitted by the Accounting Officer to Council** **Date:** 23/01/2018	Mr F.R Sello **Adopted by Council (Signed by Chairperson obo Council)** **Date:** 24/01/2018	**Implementation Date:**

1. Legislative framework and best practice regulations

Key principles contained in the following legislation were applied to develop this policy:

a) CET Colleges Act No.16 of 2006, as amended (the "Act") (formerly the ABET Act);
b) Public Finance Management Act, 1999 (Act No 1 of 1999 as amended by Act 29 of 1999) (PFMA);
c) National Treasury Regulations, March 2005; and
d) GRAP 13: Leases.
e) GRAP 5: Borrowing Costs

2. Purpose

The purpose of this policy is to:

a) enable the College to comply with the restrictions in terms of Sections 24.1(d) and 24.2 of the Act which states that a College may not raise money by means of a loan or overdraft without the approval of the Minister; and
b) provide written minimum standards for the establishment of a control framework for the approval and management of borrowings having regard to the restrictions referred to in paragraph (a).

3. Objective

The objective of this policy is to enable the College to achieve the following:

a) to ensure that, within the legal framework, the College's financing needs and its payment obligations are met at the lowest possible cost, consistent with a prudent degree of risk;
b) to record the circumstances under which the College may incur loans and borrowings;
c) to describe the conditions that must be adhered to by the Accounting Officer when a loan and borrowing application is submitted to the Minister for approval; and
d) to set out the internal control measures with regards to the maintenance and repayments of loans and borrowings.

4. Definitions, acronyms and abbreviations

For the purpose of this policy, unless the context indicates otherwise, the following definitions are set out for the terms indicated:

4.1 ***"Accounting Officer"*** – is the College Principal.

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4.2 ***"Act"*** – is the CET Colleges Act No.16 of 2006, as amended. (formerly the FET Act)

4.3 ***"Borrowing"*** – is the receiving of something of value in exchange for an obligation to pay back something of usually greater value at a particular time or periods in the future.

4.4 ***"College", "CETC"*** – is a Community Education and Training College.

4.5 ***"Department";"DHET"***– is the Department of Higher Education and Training.

4.6 ***"Finance lease"*** – is a lease that transfers substantially all the risks and rewards incidental to ownership of an asset. Title may or may not eventually be transferred.(GRAP13)

4.7 ***"Lender"*** – in relation to a College, is a person or service provider who provides debt finance to a College.

4.8 ***"Loan"*** – is the act of receiving money, property or other material goods from another party in exchange for future repayment of the principal amount along with interest or other finance charges. A loan may be for a specific, one-time amount or can be available as open ended credit up to a specified ceiling amount such as an overdraft limit.

4.9 ***"Long term debt"*** – is a loan or borrowing which is repayable over a period exceeding 12 months.

4.10 ***"Minister"*** – is the Minister of the Department of Higher Education and Training.

4.11 ***"Operating lease"*** – is a lease other than a finance lease.(GRAP13)

4.12 ***"Security"*** – is a lien, pledge, mortgage, cession or other form of collateral intended to secure the interest of a lender.

4.13 ***"Short term debt"*** – is a borrowing which is repayable over a period not exceeding 12 months.

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5. Scope

In terms of Section 24.1.d and Section 24.2, the College may not raise money by means of a loan or overdraft without the approval of the Minister

Section 24.3 further states that without such approval the State and the College are not bound by the contract of lending or the overdraft agreement.

This policy governs loans and borrowings of amounts greater than R500 000.00 which forms part of the Colleges Funding; and may include the following;

a) money raised by means of a new loan;
b) money raised by means of an overdraft;
c) maintenance and redemption of existing loans; and
d) finance leases.

The policy specifically applies to the matters relating to:

a) considerations for external debt financing;
b) security;
c) approval;
d) conditions for Minister to approve the raising of loans by a College;
e) prohibited borrowing practices;
f) internal controls over borrowings; and
g) non-payment or non-servicing of loans.

6. Considerations for external debt financing

6.1 Type of debt:
Subject to the approval by the Minister, the College may raise money by means of a loan, which may be short term or long-term, or by means of an overdraft facility. In determining the acceptable level of borrowings, the following must be considered:

6.1.1 Loans

(a) Short-Term:
The College may incur short-term debt only when necessary to bridge operational funding shortfalls. The College must adhere to the following conditions when short term debt is incurred:

- Short-term debt must be paid within 3 months of its incurrence; and
- Short-term debt may not be renewed or refinanced.

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(b) Long-Term

- The College will confine long-term borrowing to capital improvements including infrastructure developments and expansions only, to create more access to learning programmes which may generate more funds for the College.
- The College will not use long-term debt for current obligations.

6.1.2 Overdraft Facility

a) The College may enter in an agreement with a financial institution for an overdraft facility subject to the following;

- The overdraft facility needs to be managed by the Deputy Princpal: Finance and must form part of the monthly reports to the DHET.
- When the facility is utilised, the College must ensure that it is only utilised for operational purposes and must ensure that the facility does not remain in overdraft for more than 3 consecutive months.

6.2 Factors to consider when borrowing

(a) Risk management:

The College needs to manage interest rate risk, credit risk exposure and to maintain debt within specified limits. Potential funding sources should be reviewed and analysed by the Deputy Principal: Finance to ensure that interest rate and credit risk exposure is prudently managed.

Regardless of what financing structure is utilised, a feasibility study must be performed for each transaction, including quantification of potential risks and benefits, matching the borrowing period with the useful life of the asset being financed, as well as an analysis of the impact on the creditworthiness, debt affordability and cash flows of the College.

(b) Cost of borrowings:

Borrowings should be structured to obtain the lowest possible interest rate, on the most advantageous terms and conditions, taking cognisance of borrowing risk constraints, borrowing covenants (for example; early repayment penalty clauses), infrastructure needs, and economic forecasts of interest rate movements and any limitations set by the Minister for the specific college.

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The interest rate should be fixed over the term of the loan to eliminate interest rate fluctuations and to create certainty with regards to cash flow forecasting.

(c) Prudence:
Borrowings should be made with care, skill, prudence and due diligence and based on the approval of Minister.

(d) Strategic debt allocation
The College should seek to minimise its dependence on borrowings within its overall ability to service repayments within budgeted cash flows.

The College may only borrow funds for the purpose of achieving the strategic objectives of the College.

6.3 Other Special conditions relating to Borrowings and Finance Leases

a) The debt must be denominated in rand and must not be indexed to, or affected by fluctuations in the value of the rand relative to other currencies.
b) The College may enter into a finance lease agreement subject to the approval of the Council and the Accounting Officer. The Deputy Principle: Finance must ensure that a register is maintained of all finance leases in the name of the College. All finance leases greater than five years will require Ministerial approval.
c) The Accounting Officer must sign the contractual agreement or other document which creates or acknowledges the debt, after approval is obtained from the Minister and and/or Council whichever is relevant in terms of this policy.
d) The rights and obligations to the debt must vest in the College; therefore all loans must be registered in the name of the College.

7. Security

7.1 In order to make borrowing possible and/or lower the cost of borrowing, the Accounting Officer may authorise security to be furnished for any of its debt obligations, provided approval is obtained from the Minister.

7.2 When furnishing security for any of its debt obligations, consideration must be given to the following:

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a) Determine whether the asset or right with respect to which the security is given, is necessary for providing a minimum essential College service; and
b) If so, indicate the manner in which the availability of the asset or right for the provision of that service will be protected.

7.3 If it is determined that the asset or right is necessary for providing a minimum essential service, the lender to whom the College security is given, may not, in the event of a default by the College, deal with the asset or right in the manner that would preclude or impede the continuation of the minimum essential College service.

8. Approval

8.1 To obtain the Minister's approval to apply for a loan or overdraft facility, the Council must submit the motivation to the Department who will review the motivation and submit it to the Minister for approval.

8.2 The motivation must include the following information;
a) The reason why the loan is required by the college
b) Indication of the extent to which the loan would enable the college to develop infrastructure and increase access to students.
c) Indications of the extent to which the loan would be directly linked to the strategic objectives of the college
d) amount of the loan;
e) the purpose for which the debt is to be incurred;
f) the particulars of any security to be provided;
g) a draft loan agreement reviewed and recommended by the College's legal adviser;
h) a cash-flow forecast over the loan period indicating how the loan will be serviced.

8.3 After approval is obtained from the Minister to raise money by means of a loan or overdraft, the College must follow the tender process to select a preferred financial institution. The Accounting Officer subject to the approval of Council, should enter into an agreement with the financial institution recommended by the Bid Adjudication Committee, on behalf of the College.

8.4 The Accounting Officer must ensure that the final term and conditions of the loan are as approved by the Minister.

8.5 The Accounting Officer must ensure that a Register is maintained of all Loans, Overdrafts and Securities.

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9. Conditions for Minister to approve the raising of loans by Colleges

The purpose of setting the conditions under which the Minister may approve the raising of loans by the colleges is to ensure that these loans are indeed required by colleges. Also to ensure that they would serve as an investment by way of enabling colleges to develop infrastructure that might generate more funds through fees collected from offering additional programmes.

Another purpose is to protect colleges from becoming highly indebted due to loans taken which are not in the best interests of the college and cannot be directly linked to promoting quality education at the college.

9.1 The motivation should be received by the Minister at least one month prior to the date by which the College intends to apply for the loan.

9.2 A long term loan may only be applied for for infrastructure development

9.3 A short term loan or an overdraft facility may be applied for operational purposes only.

9.4 On request, the College must disclose other loans or overdraft agreements entered into, which are not yet settled by the College.

9.5 The new loan, together with any existing unsettled loans, cannot exceed 5% of the total income of the College including grant income and income received for skills programmes.

9.6 The College must show positive growth in income and accumulated profits over the previous three years.

9.7 In addition to the above, the Minister will also consider whether the following balance sheet ratios are within acceptable ranges; on a case by case basis; to ensure that the College is not over indebted and that it has the potential to repay the loan.
  a) Return on capital employed;
  b) Current ratio working capital ratio;
  c) Debt Equity ratio.

9.8 The Minister will consider all the information submitted and use his/her discretion for the approval of the loan or overdraft.

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10. Prohibited borrowing practices

10.1 No foreign borrowing are permitted
10.2 The College may not guarantee the debt of any other entity or individual.
10.3 The Department may not guarantee the debt of any College, entity or individual.
10.4 The College may not refinance existing debt without approval from the Minister.

11. Internal control over borrowings

In order to prevent losses arising from fraud, misrepresentations or error, a system of internal control must govern the administration and management of the borrowings portfolio. Internal controls over the following functions, as a minimum, should be implemented:

11.1 Repayments made on loans

a) The budget and cash flow forecast must be updated to facilitate the repayment of the debt.

b) Payments should be made in terms of the amortisation schedule or notices from the financing institution for the respective loans due for repayments.

c) The copy of the amortisation schedule or notice from the financing institution, detailing the capital and interest payable, must be attached to each loan repayment.

11.2 Accounting records

a) The accounting records, including the loan register, must be updated regularly.

b) Monthly reconciliations are to be performed between the ledger and the statements from the financial institutions to confirm the capital balance outstanding and that the interest has been correctly charged to the income statement.

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c) The Deputy Principle: Finance must report to the finance committee on the progress of the loan repayments against the forecast. Any material deviations from the forecast must be reported to Council.

11.3 Loan register

The loan register must include the following details:

a) Loan number;
b) Date issued;
c) Type of loan;
d) Name of financial institution;
e) Purpose of loan;
f) Loan period;
g) Interest rate (a fixed interest rate is recommended)
h) Installment (capital and interest);
i) Due dates for capital and interest payments (monthly / quarterly / half-yearly / yearly);
j) Security (if any);
k) Final redemption date;

The following reconciliations must be performed and reviewed on a monthly basis:

a) Capital balance outstanding, as reflected in the amortisation schedule, to the general ledger; and
b) Interest paid, per the amortisation schedule, to the general ledger.

11.4 Maintenance of documentation

The following loan documentation must be maintained and safeguarded at all times:

a) Approval from Minister;
b) Loan agreements;
c) Any applicable security agreements;
d) Copy of annual loan register;
e) Signed copy of monthly reconciliations of loan records to the general ledger;
f) Copy of all repayments made; and
g) Copy of amortisation schedules.

12. Non-payment or non-servicing of loans

12.1 The College must honour all of its loan obligations timeously. Failure to effect prompt payment may jeopardise the College's credit rating and will adversely affect the prospect raising of future loans.

12.2 In addition to the timeous payment of the loans, the College must adhere to the covenants stipulated in the loan agreements and the under-mentioned are some examples of typical covenant requirements:

a) furnish audited annual financial statements on a timely basis; and
b) long term credit rating not to decline below a certain level.

13. Adoption of policy

This policy is effective from the date on which it is adopted by the Council.

14. Availability of borrowing policy

A copy of this policy and other relevant documentation should be made available on the College website.

15. Annual revision of policy

This policy will be subject to an annual review by College management to ensure its relevance. Colleges should forward any inputs and recommendations to the CET Branch of the DHET for possible consideration during the annual review process.

Any recommended changes agreed by the CET Branch of the DHET to the borrowing policy should be presented to the College Council for adoption.

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