# DEBT IMPAIRMENT POLICY

## (Approved by Council on 29 May 2025)

# THEMBELIHLE LOCAL MUNICIPALITY

## IMPAIRMENT OF DEBTORS POLICY

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## 1. OBJECTIVES OF POLICY

a. Section 64 of the MFMA makes the accounting officer responsible for the management of municipal revenue. This includes, amongst others, a requirement that the municipality have an effective revenue collection system consistent with section 95 of the Municipal Systems Act and the municipality's credit control and debt collection policy.

b. Section 96 of the Municipal Systems Act requires that a municipality must collect all money that is due and payable to it and implement a credit control and debt collection policy which is consistent with its rates and tariff policies and complies with the provisions of the Systems Act and MFMA.

c. Ensure any long outstanding debt is evaluated in order to determine the possibility of realizing such income as revenue.

d. Ensure that where it is evident that a particular debt cannot be turned into a revenue such debt be procedurally regarded as irrecoverable.

e. Ensure that the council of the municipality makes provision for debt impairment in the budget.

f. Ensure that the outstanding monies which have been outstanding for a long time after all attempts have been made in terms of recovering them should then be written off.

g. Ensure the identification of bad debts to write-off during the course of the financial year.

h. Ensure the proper delegation of power to the chief financial officer to write off bad debts up to a certain amount.

## 2. LEGISLATIVE AND REGULATORY FRAMEWORK

a. Municipal Systems Act, Act 32 of 2000.

b. Municipal Financial Management Act, Act 56 of 2003.

c. Standards of Generally Recognised Accounting Practice (GRAP).

d. Municipal Standard Chart of Accounts (mSCOA) (charts, applicable MFMA and mSCOA Circulars) (Note: National Treasury's Position Papers have been considered, however, these do not have any legal status).

## 3. SCOPE OF POLICY

This policy be applicable to all categories of debtors.

The categories of debtors include debtors for Electricity, Water, Sewerage, Refuse, Rentals, Levies (Business Service and Regional Service), Housing

Rental, and Other Receivables. Statutory Receivables include debtors for Property Rates and Traffic Fines. Debtors by customer classification include Consumers, Industrial/Commercial, National and Provincial Government.

## 4. WRITING OFF OF IRRECOVERABLE DEBTS

Debt shall be identified to be irrecoverable after the whole credit control and debt collection process has been followed and no payments having been received towards the outstanding account.

Examples of debt considered to be irrecoverable

a. All reasonable notifications and cost effective legal avenues have been exhausted to recover outstanding balances due,
b. The cost to recover the debt does not warrant further action,
c. It has been proven that the debt has prescribed,
d. The debtor is untraceable or cannot be identified so as to proceed with further action, and
e. A court has ruled that the claim is not recoverable.

Where debts are identified as being irrecoverable, the process of write off shall be treated as follows:

### 4.1 Amounts equal to or lower than amounts delegated to the Chief Financial Officer (CFO) by Council resolution from time to time

The Revenue Accountant must prepare a report within the delegated powers of the CFO containing the following:

a. Consumer details;

b. Actions/processes taken to recover the debt

c. Irrecoverable amounts

d. Confirmation that further actions would be fruitless and not cost effective.

e. Requests approved by the Chief Financial Officer will be processed in the accounting records. For example, the accounts which could be used for the debt write-off includes (based on the latest mSCOA chart):

   (i) Expenditure: Bad Debt Written Off,
   (ii) Liabilities: Current Liabilities: Output VAT: Provision for Doubtful Debt Impairment: Recognised (where applicable),

(iii) Assets: Current Assets: Trade and Other Receivables from Exchange Transactions: Trading Service and Customer Service Debtors: Electricity/Water/Waste Water/Waste Management: Debt Write-off,

(iv) Gains and Losses: Reversal of Impairment Loss: Trade and Other Receivables from Exchange Transactions: Electricity/Water/Waste Water/Waste Management,

(v) Assets: Current Assets: Trade and other Receivables from Exchange Transactions: Trading Service and Customer Service Debtors: Electricity/Water/Waste Water/Waste Management: Impairment: Reversal.

(vi) Assets: Current Assets: Receivables from Non-Exchange Transactions: Property Rates: XX: Debt Write-off

(vii) Gains and Losses: Reversal of Impairment Loss: Other Receivables from Non-Exchange Revenue: Property Rates,

(viii) Assets: Current Assets: Receivables from Non-Exchange Transactions: Property Rates: XX: Impairment: Reversal.

### 4.2. Amounts exceeding the Chief Financial Officer delegated authority.

The Revenue Accounting must prepare a report of irrecoverable debts in excess of the chief Financial Officer delegated powers containing the following:

a. Consumer details;

b. Irrecoverable amount

c. Details on credit and debt collection processes followed to recover the debt;

d. Reasons that led to debt being identified as being irrecoverable:

e. Confirmation that all available avenues to recover debt have been exhausted: and

f. Confirmation that further actions would be fruitless and not cost effective.

The report of the Revenue Manager must be considered by the Chief Financial Officer.

If approved by the Chief Financial Officer, the report shall be submitted to the Financial Cluster Committee and then Council for consideration.

Approvals granted by Council must be processed in the general ledger. For example, the accounts which could be used for the debt write-off includes (based on the latest mSCOA chart):

(i) Expenditure: Bad Debt Written Off,
(ii) Liabilities: Current Liabilities: Output VAT: Provision for Doubtful Debt Impairment: Recognised (where applicable),
(iii) Assets: Current Assets: Trade and Other Receivables from Exchange Transactions: Trading Service and Customer Service Debtors: Electricity/Water/Waste Water/Waste Management: Debt Write-off,
(iv) Gains and Losses: Reversal of Impairment Loss: Trade and Other Receivables from Exchange Transactions: Electricity/Water/Waste Water/Waste Management,
(v) Assets: Current Assets: Trade and other Receivables from Exchange Transactions: Trading Service and Customer Service Debtors: Electricity/Water/Waste Water/Waste Management: Impairment: Reversal.
(vi) Assets: Current Assets: Receivables from Non-Exchange Transactions: Property Rates: XX: Debt Write-off
(vii) Gains and Losses: Reversal of Impairment Loss: Other Receivables from Non-Exchange Revenue: Property Rates,
(viii) Assets: Current Assets: Receivables from Non-Exchange Transactions: Property Rates: XX: Impairment: Reversal.

### 4.3 Application of Prescription Act

The provisions of Prescription Act shall apply to all services debt, excluding assessment rates.

Applications and / or claims for prescription from debtors shall only be assessed if no formal credit control or legal actions have been instituted during prescriptions debt period of three (3) years.

Chief Financial Officer shall assess applications in terms of prescribed requirements. If in compliance with Prescribed Act, approval may be granted to write-off prescribed portion of debt.

Approvals granted must be processed on the general ledger. For example, the accounts (excluding property rates) which could be used for the debt write-off includes (based on the latest mSCOA chart):

(i) Expenditure: Bad Debt Written Off,
(ii) Liabilities: Current Liabilities: Output VAT: Provision for Doubtful Debt Impairment: Recognised (where applicable),

(iii) Assets: Current Assets: Trade and Other Receivables from Exchange Transactions: Trading Service and Customer Service Debtors: Electricity/Water/Waste Water/Waste Management: Debt Write-off,

(iv) Gains and Losses: Reversal of Impairment Loss: Trade and Other Receivables from Exchange Transactions: Electricity/Water/Waste Water/Waste Management,

(v) Assets: Current Assets: Trade and other Receivables from Exchange Transactions: Trading Service and Customer Service Debtors: Electricity/Water/Waste Water/Waste Management: Impairment: Reversal.

## 5. RECOVERY OF IRRECOVERABLE DEBTS

Should there be a payment in respect of the amount which has already been written off, such monies must be allocated to the specific vote number for the recovery of the irrecoverable debts (**for example, based on the latest mSCOA chart: Revenue: Exchange Revenue: Operational Revenue: Bad Debts Recovered**).

## 6. IMPAIRMENT OF DEBTORS

Approach:

1. In a publication entitled Accounting for Covid-19, updated in June 2020, the Accounting Standards Board (ASB) indicates that “Due to the economic impact of the COVID-19 crisis on consumers, taxpayers and businesses, there is a high likelihood that there is observable evidence of an impairment loss, for example, default on the payment terms agreed, or financial difficulty of the counterparty (in line with paragraph .58(f)(ii) of GRAP 104)”.

2. Paragraph .57 of GRAP 104 states the following with regard to the impairment and collectability of a financial asset or a group of financial assets (being accounts receivable):
    - “An entity shall assess at the end of each reporting period whether there is any objective evidence that a financial asset or group of financial assets is impaired.
    - If any such evidence exists, the entity shall apply paragraphs .61 to .63 (for financial assets carried at amortised cost) and paragraph .64 (for financial assets carried at cost) to determine the amount of any impairment loss.

3. Paragraph .61 of GRAP 104 states the following: "If there is objective evidence that an impairment loss on financial assets measured at amortised cost has been incurred, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows (excluding future credit losses that have not been incurred) discounted at the financial asset's original effective interest rate (i.e. the effective interest rate computed at initial recognition). The carrying amount of the asset shall be reduced either directly or through the use of an allowance account. The amount of the loss shall be recognised in surplus or deficit."

4. Paragraph .62 of GRAP 104 states the following: "An entity first assesses whether objective evidence of impairment exists individually for financial assets that are individually significant, and individually or collectively for financial assets that are not individually significant (see paragraph .58). If an entity determines that no objective evidence of impairment exists for an individually assessed financial asset, whether significant or not, it includes the asset in a group of financial assets with similar credit risk characteristics and collectively assesses them for impairment. Assets that are individually assessed for impairment and for which an impairment loss is or continues to be recognised are not included in a collective assessment of impairment".

5. Paragraph .63 of GRAP 104 states the following: "If, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognised (such as an improvement in the debtor's credit rating), the previously recognised impairment loss shall be reversed either directly or by adjusting an allowance account. The reversal shall not result in a carrying amount of the financial asset that exceeds what the amortised cost would have been had the impairment not been recognised at the date the impairment is reversed. The amount of the reversal shall be recognised in surplus or deficit."

6. Paragraph .64 of GRAP 104: If there is objective evidence that an impairment loss has been incurred on an investment in a residual interest that is not measured at fair value because its fair value cannot be measured reliably, the amount of the impairment loss is measured as the difference between the carrying amount of the financial asset and the present value of estimated future cash flows discounted at the current market rate of return for a similar financial asset (see Appendix A paragraphs AG110. and AG111.). Such impairment losses shall not be reversed.

7. Paragraph .17 of GRAP 108 states the following with regard to impairment losses: "An entity shall assess at each reporting date whether there is an indication that a statutory receivable, or a group of statutory receivables, may be impaired. If any such indication exists, the entity shall apply paragraphs .22 - .29".

8. Paragraph .22 of GRAP 108 states the following: "If there is an indication that a statutory receivable, or a group of statutory receivables, may be impaired, an entity shall measure the impairment loss as the difference between the

estimated future cash flows and the carrying amount. Where the carrying amount is higher than the estimated future cash flows, the carrying amount of the statutory receivable, or group of statutory receivables, shall be reduced, either directly or through the use of an allowance account. The amount of the loss shall be recognised in surplus or deficit."

9. Paragraph .23 of GRAP 108 states the following: "In estimating the future cash flows, an entity considers both the amount and timing of the cash flows that it will receive in future. Consequently, where the effect of the time value of money is material, an entity discounts the estimated future cash flows using a rate that reflects the current risk free rate and, if applicable, any risks specific to the statutory receivable, or group of statutory receivables, for which the future cash flow estimates have not been adjusted."

10. Paragraph .24 of GRAP 108 states the following: "In determining whether a statutory receivable, or group of statutory receivables, is impaired, management estimates the cash flows that it expects to collect based on facts and circumstances at the reporting date. These estimates include any cash flows that may be received from any collateral or encumbrances held over property, less any costs incurred to obtain, seize, sell or otherwise liquidate the underlying assets. The cash flows from collateral or encumbrances held are not included in the estimated cash flows when management does not intend to call up the collateral held. For example, an entity may have the ability to seize and sell fixed property to recover any amounts owing, but may choose not to take such action if it is likely to cause economic hardship."

11. Paragraph .25 of GRAP 108 states the following: "The future cash flows of a group of statutory receivables that are collectively evaluated for impairment can be estimated using historical experience for receivables with similar characteristics. Entities that have no entity-specific historical experience or insufficient experience, can use peer group experience (when available) for comparable groups of statutory receivables. Historical experience may need to be adjusted to reflect the effects of current conditions that did not affect the period on which the historical experience is based and, to remove the effects of conditions in the historical period that do not exist currently. Where historical experience is used, the methodology and assumptions used to estimate future cash flows shall be reviewed regularly to reduce any differences between estimated and actual impairment losses".

12. Paragraph .26 of GRAP 108 states the following: "The process for estimating the amount of an impairment loss may result either in a single amount or in a range of possible amounts. In the latter case, the entity recognises an impairment loss equal to the best estimate within the range (the Standard of GRAP on Provisions, Contingent Liabilities and Contingent Assets (GRAP 19) discusses principles in relation to a "range of outcomes"), taking into account all relevant information available before the financial statements are issued about conditions existing at the end of the reporting period."

13. Paragraph .27 of GRAP 108 states the following: "An impairment loss recognised in prior periods for a statutory receivable shall be revised if there

has been a change in the estimates used since the last impairment loss was recognised, or to reflect the effect of discounting the estimated cash flows in accordance with paragraph .23."

14. Paragraph .28 of GRAP 108 states the following: "When the estimates used to determine an impairment loss in a prior period change, either because of changes in the amount that is collectible (such as an improvement in a debtor's financial position) or when it will be collected (such as an improvement in the expected settlement period), the amount of the impairment loss previously recognised is adjusted. Any amount previously recognised is also revised to reflect the passage of time where the estimated cash flows are discounted."

15. Paragraph .29 of GRAP 108 states the following: "Any previously recognised impairment loss shall be adjusted either directly or by adjusting the allowance account. The adjustment shall not result in the carrying amount of the statutory receivable or group of statutory receivables exceeding what the carrying amount of the receivable(s) would have been had the impairment loss not been recognised at the date the impairment is revised. The amount of any adjustment shall be recognised in surplus or deficit."

16. Accounting Standards Board GRAP FAQ 8.1/GRAP 104 Application Guidance (AG) paragraph.87 on <u>Discounting</u>: Short-term receivables and payables are <u>not discounted</u> where the <u>initial credit period granted or received is consistent with terms used in the public sector</u>, either through established practices or legislation. For example, it is common practice for municipalities to allow consumers a period of time, after issuing an invoice, to settle their water and electricity accounts. Specific legislation may also prescribe credit terms for specific types of transactions or entities, which provide an indication of what appropriate credit terms are for certain transactions and events. Where the initial credit period granted is not in line with practices or legislation in the public sector, the effect of discounting is considered if it is material.

Based on the above, GRAP 104 Paragraphs .57, .61 to .64 and GRAP 108 paragraphs .17, .22 to .29 and GRAP 104 AG paragraph .87) are applicable:

17. Debtors are aged, including account balances with current and 30 days outstanding, accounts with balances of 31 to 90 days, and accounts with balances of 90 days or more. The Municipality may estimate readings and read meters in accordance with the period prescribed in the respective water and electricity policies and By-laws. A registered owner remains liable to monitor his /her property as well as meter readings even if all electricity or water services have been disconnected. (The municipality to confirm and any reference to other internal policies/By-laws?).

18. Assessed whether objective evidence of impairment exists individually for each debtors balance by analyzing the payment history of each individual debtors. (Please check for example on government debt and indigents? Is government debt excluded/individually assessed? Any reference to be made to separate indigent support policies? For example: The municipality may

grant assistance to any person who is regarded as an indigent customer, in accordance with qualifying criteria as set out in the Indigent Policy and subject to the availability of a budget provision, as determined by Council at its annual budget meeting. A person who qualifies as an indigent customer must be prepared to convert to pre-paid metering. The municipality to review).

19. Debtors with similar payment history were considered to be having the same credit risk.

20. Grouped the debtors into different credit classes based on the payment history of each individual debtor.

21. Provided for impairment on the basis of the risk classes identified.

**Note:**

Should a debtors' account show signs of nonpayment through accumulation of arrear balance, the debtor will be considered as a delinquent debtor. Such debtors are provided for as they are considered to be impaired. The provisions will be provided on the specific debtors' balance that are considered impaired.

**The Grading has been done based on the following Basis:**

a. Customer accounts with up to date payments with no arrear balance outstanding, in the "not settled balance" range (0%-10%).

b. Accounts with balance with a history of payment, but with arrear balance outstanding, in the "not settled balance" range (11%-50%).

c. Accounts with balance with a history of payment, but with arrear balance outstanding, in the "not settled balance" range (51%-95%).

d. Customers with no history of payment (accounts have been considered delinquent), in the "not settled balance" range (96%-100%).

| **Grading** | **Range** | **% Impairment** | **Comment** |
|---|---|---|---|
| A | 0%-10% | 0% | No provision |
| B | 11%-50% | 30.5% | Average |
| C | 51%-95% | 73% | Average |
| D | 96%-100% | 100% | Impair full balance |

## 7. MSCOA IMPLICATIONS

The Minister of Finance promulgated Government Gazette No. 37577, Municipal Regulations on Standard Chart of Accounts (mSCOA), on 22 April 2014. All municipalities are required to transact in compliance with the mSCOA Regulations from 01 July 2017.

Revenue Cycle Billing, Valuation Roll Management, Real Estate and Resources Management, Customer Care, Credit Control and Debt Collection, Financial Accounting, Municipal Budgeting, Planning and Financial Modelling, Costing and Reporting are part of the 15 Business Processes. The Revenue Management Module gives effect to MFMA Section 64.

In the context of mSCOA a standard approach in the accounting treatment is preferable in order to ensure a uniform classification of transactions (i.e. the recognition, measurement and disclosure of revenue and receivables in a consistent and transparent manner).

The accounting consequences of the debt management function should be as follows:

a. Bad debts written off following resolution of Council must be expensed and accounted for as Expenditure: Bad Debt Written Off, disclosed on the face of the Statement of Financial Performance [Item Segment Expenditure: Bad Debt Written Off].

b. Impairment assessment for debtors, in terms of Standards GRAP 104 and GRAP 108, must be conducted on an annual basis. The effects of the movement in the impairment allowance must be recognized in the Statement of Financial Performance [Item Segment Gains and Losses].

c. Separate accounts are available within mSCOA to recognize an increase and/or decrease in the impairment of debt per selected debt type.

## 8. REVIEW OF POLICY

This policy must be reviewed and submitted for consideration by Council on an annual basis.

VERSION CONTROL

Version 1

Date

Summary: This document describes the Debt Impairment Policy that will be applicable to Thembelihle Municipality starting 1 July 2024 and will be revised annually. For further information on the policy the Chief Financial officer can be contacted at 053 20 30 005/8

Approval

SIGNATURE ACCOUTING OFFICER:………………………………………………………….

DATE:……………………………………………

SIGNATURE: (MAYOR)………………………………………………………………….

DATE:…………………………………………………………………

COUNCIL RESOLUTION NUMBER:……………………………………………….

DATE:…………………………………………………………………