FETAKGOMO TUBATSE
LOCAL MUNICIPALITY

FETAKGOMO TUBATSE MUNICIPALITY

DRAFT DEBT IMPAIRMENT POLICY

2024/2025

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1. BACKGROUND AND PURPOSE

PURPOSE

The purpose of this document is:

- To set out a methodology for the impairment of receivables the municipality in line with the applicable accounting standards.
- To ensure that sufficient allowance is made for the impairment of receivables in the financial statements.
- Ensure that receivables disclosed in the financial statements are stated at amounts that are deemed collectable; and
- To promote transparency as required by sections 215 and 216 of the Constitution when dealing with receivables and debt.

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2. SCOPE

The methodology is applicable to all receivables subsequently measured at amortised cost. This includes the following line items as disclosed on the statement of financial position:

- Consumer receivables.
- Receivables from exchange transactions; and
- Receivables from non-exchange transactions.

3. DEFINITIONS AND ABBRETIATIONS

"Financial year"	means the period 1 July of one year to 30 June of the following year (both days included)
"GRAP"	means Generally Recognised Accounting Practices
"MFMA"	means Municipal Finance Management Act 56 of 2003
"Municipality"	means FetakgomoTubatse Local Municipality
"Reporting date"	means 30 June of each year

4. APPLICABLE ACCOUNTING STANDARDS

GRAP 104 financial instruments sets out the requirements and guidelines for the impairment of financial assets subsequently carried at amortised cost. GRAP 104.46 "a*ll financial assets measured at amortised cost, or cost, are subject to an impairment review…"*

GRAP 104.57 "a*n 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".*

GRAP 104.58 *"a financial asset or a group of financial assets is impaired and impairment losses are incurred if, and only if, there is objective evidence of impairment as a result of one or more events that occurred after the initial recognition of the asset (a loss event') and that loss event (or events) has an impact on the estimated future cash flows of the financial asset or group of financial assets that can be reliably estimated".*

GRAP 104.61 "i*f 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".*

GRAP 104.62 *"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". GRAP 104.63 "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 recognized (such as an improvement in the debtor's credit rating), the previously recognized 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 recognized in surplus or deficit".*

5. METHODOLOGY

In accordance with GRAP 104 (Financial Instruments), an objective assessment of financial assets is made at year end to determine possible impairment. Impairment loss is recognised as an expense in the Statement of Financial Performance. The determination of the impairment loss is guided by the following principles as per GRAP 104. The municipality assesses financial assets individually, when assets are individually significant, and individually or collectively for financial assets that are not individually significant. (Individual Debtors' balances that constitute at least 5 percent of the total debtors book are considered to be individually significant by the municipality).

Where no objective evidence of impairment exists for an individually assessed asset (whether individually significant or not), the municipality includes the assets 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 the collective assessment of impairment. As soon as information becomes available that specifically identifies losses on individually impaired assets in a group (that are collectively assessed for impairment), those assets are removed from the group and assessed individually for impairment.

For collective assessment of impairment, as indicated above, assets with similar credit risk characteristics are grouped together. The credit risk characteristics should be indicative of the debtors' ability to pay all amounts due according to the contractual terms.

The method used in determining the group of assets to be assessed for impairment, is a grading process that considers the:
-Debtor type
-Industry
-Past due status (e.g. days/months that the accounts are in arrears)

Consumer debtors are evaluated at the end of the reporting date and impaired as follows:

a) Timing of Assessment
The Municipality will assess at the end of each reporting date whether there is objective evidence that a receivable account or group of receivable accounts is impaired.

b) Evidence of Impairment
Any one of the following events is considered to provide objective evidence that a receivable account or group of receivable accounts could be impaired:
• All receivables that have been placed under or applied for liquidation or sequestration;
• Indigent accounts;
• Inactive accounts;
• Accounts handed over to debt collectors and/or power of attorney;
• All accounts with balances outstanding 270 days and longer as these accounts are considered to be past due.

c) Calculation and Recognition of Impairment Loss

I. The impairment loss is calculated as the difference between the carrying value at reporting date less the present value of expected future cash flows:

   Carrying Amount at reporting Date - Present Value of Future Expected Cashflows = Impairment Loss

II. The carrying amount (Expected Future Cash Flows) at reporting date is calculated as follows:

   Gross carrying amount Less debtors to be impaired 100% (Indigent debtors, Handed over Debtors, Debtors with balances 270 days and longer)

III. The Discount Rate used is derived from the policy (prime plus 1%), average for the financial year.

IV. The Expected Repayment Term is 30 days (derived from the policy)

6. <u>IMPLEMENTING STRATEGY</u>

The Municipal manager shall submit a report on all debt impairments made under this policy to the Mayor every year.

The Municipal Manager shall be responsible for the implementation and administration of this policy.

This policy will be effective on the date of adoption by Council.

7. EFFECTIVE DATE

This policy will be applied retrospectively.

8. POLICY EVALUATION AND REVIEW

In terms of section 17(1)(e) of the MFMA polices must be reviewed on an annual basis and the reviewed policy tabled to Council for approval as part of the budget process.