

MOSES KOTANE LOCAL MUNICIPALITY



DEBT IMPAIRMENT AND WRITE OFF POLICY

Original Council Approval		Amended
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1. INTRODUCTION

The Municipal Finance Management Act, Act 56 of 2003 states that the municipality must manage its revenue by ensuring a proper system of internal control exists in respect of debtors and revenue.

The municipality must budget for realistic anticipated revenue less an acceptable provision for bad debts.

The policy aims to ensure that debtors are disclosed in the annual financial statements at the amounts deemed to be collectable and uncollectable debt is written off within the guidelines of existing policies and applicable legislation.

By adopting this policy clear guidelines are set on the treatment of the impairment of debtors and write-off of debtors.

2. OBJECTIVES OF POLICY

The objectives of this policy are to:

- Ensure any long outstanding debt is evaluated in order to determine the possibility of realizing such income as revenue.
- Ensure that where it is evident that a particular debt cannot be turned into revenue such debt be procedurally regarded as irrecoverable.
- Ensure that the Council of the municipality makes enough provision for bad debts in the budget.
- Ensure that 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.
- Ensure the identification of bad debts during the course of the financial year.
- Ensure the proper delegation of powers to the Chief financial officer to write off bad debts up to a certain amount.

3. LEGISLATIVE FRAMEWORK

- Municipal Systems Act, Act 32 of 2000.
- Municipal Finance Management Act, Act 56 of 2003.
- Standards of Generally Recognized Accounting Practice.

4. Scope

This policy will be applicable to all categories but not limited to the following:

- Consumer debtors.
- Sundry debtors
- Traffic fines

5. IDENTIFICATION OF IRRECOVERABLE DEBTS

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

5.2 Once the debt is regarded as irrecoverable during the year it must be grouped with others so that at the latest by May every year the report be submitted to Council to approve the write-off of the identified irrecoverable debts.

6. WRITING OFF OF IRRECOVERABLE DEBTS

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

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

Revenue Manager: Credit Control and Debt Collection must prepare a report within the delegated powers of the CFO containing the following:

- consumer details.
- irrecoverable amount broken down by service;
- details on credit and debt collection processes followed to recover the debt;
- reasons that led to debt being identified as being irrecoverable;
- confirmation that all available avenues to recover debt have been exhausted; and
- Confirmation that further actions would be fruitless and not cost effective.

6.2 The report of the Head of Unit: Revenue must be scrutinized by the CFO and recommend the writing off of the debt to council thereof.

6.3 The Head of Unit: Revenue must annually prepare a reconciliation of debt impairment accounts/votes with supporting documentation to be submitted to the CFO to retain for audit purposes.

7. RECOVERY OF IRRECOVERABLE DEBTS

Should there be a payment in respect of the account which has already been written off, such monies must be allocated to the specific vote number designed for the recovery of irrecoverable debts.

8. SUNDRY MATTERS

8.1 Council may from time to time implement an incentive scheme which may entitle writing off of certain debts.

9. APPROVAL OF WRITE OFF

Any amount shall be written off with the approval of council.

10. IMPAIRMENT OF DEBTORS (PROVISION FOR DOUBTFUL DEBT)

Consumer debtors (accounts receivable), long term receivables and other debtors are stated at cost, less a provision for bad debt.

Significant financial difficulties of the debtor and default or delinquency in payments or all debt outstanding for more than 90 days are considered indicators to determine that debtors should be impaired.

Impairment of debtors (provision for doubtful debt) is recognized as an expense in the statement of financial performance. When an under recovery occurs during the financial year an additional contribution for impairment is made at year end.

Impairment Methodology

10.1 Consumer debtors

The municipality's debtors are divided into non-performing debtors and the performing debtors. Debtors are evaluated at each reporting date and impaired as follows:

- 1. Specific impairment for individually significant debtors.
- 2. Probability of default model for individually insignificant accounts (PD Model).

Specific impairment

All debtors that are individually significant shall be individually assessed for impairment. A Bad Debt Provision Report must be prepared for all individually significant debtors at each reporting date. The report must be prepared by the HOU Revenue and will be reviewed and approved by the CFO.

All debtors above R 500 000 are considered individually significant.

The Bad Debt Provision Report is used as the source document for impairments at reporting date.

PD Model

The PD model calculates the probability of default using the risk ratings based on the latest information at hand.

The PD will be calculated as follows:

$PD = 1 - \text{Recovery rate}$

Whereas the recovery rate = $\frac{\text{Average receipts for the past 3 years (cash collected)}}{\text{Average revenue billed to the client for the past 3 years}}$.

The bad debt provision = Gross debtors* PD.

10.2 Traffic Fines

- Probability of default multiply by total fines debt as at 30 June.
- Probability of default=
$$\frac{\text{(Total prior year debt-total fines paid)}}{\text{Total prior year debt}}$$

10.3 Sundry debtors

Sundry debtors are assessed individually for impairment when necessary.

11. Discounting of expected future cash flows

- The municipality charges interest for extended term hence present valuing the future expected cash flows will not be applicable because, though the timing of payments has changed, the municipality will receive interest on the extended term and the present value of the future principal and interest payments discounted at the debt's original effective interest rate will equal the carrying amount of the debt.

12. IMPLEMENTATION AND REVIEW

- 12.1 This policy shall be implemented once approved by council and it shall be reviewed on annual basis as part of budget processes.