PORT ST JOHNS MUNICIPALITY

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PROVISION FOR DOUBTFUL DEBTS AND WRITE OFF IRRECOVERABLE DEBTS

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INTRODUCTION

This policy provides guidelines on treatment of the impairment and write-off of debtors for Port St John's Municipality (hereafter, the Municipality). The policy seeks that household consumers with no or lower income are not denied a reasonable service and that the municipality is not financially burdened with non-payment of services.

The Council is faced with a significant amount of outstanding debt and the continuous defaulting by certain consumers who can afford to pay for services. Despite strict enforcement of the previous policies, Council will continuously be confronted by circumstances requiring the possible write-off of irrecoverable debt and Council is required by GRAP 104 to determine possible debt impairment. Provision should therefore be made for this impairment. The following scenarios will necessitate the termination of the debt write off

(1) The Municipal Manager must ensure that all avenues are utilized to collect the municipality's debt. There are certain circumstances that allow for the valid termination of debt collection procedures, such as:-
   (a) The insolvency of the debtor, whose estate has insufficient funds.
   (b) A balance being too small to recover, for economic reasons, considering the cost of recovery.
   (c) Indigent household who has no assets which can be sold for recovery of debt to municipality; or indigents who do have assets (e.g. RDP houses);
   (d) Any debtors' account whose cost to recover is more than the assets of that debtor;
   (e) A deceased debtor who has no assets to recover the debt; and
   (f) Where Council deems that a customer or groups of customers are unable to pay for services rendered.

(2) The municipality will maintain audit trails in such an instance and document the reasons for the abandonment of the action or claim in respect of the debt."

(3) In addition, Council must appoint a committee in terms of its delegations to review and recommend to Council to approve all bad debt write off cases.

(4) The effective management of debtors include, amongst others, the following processes:

(a) Implementation/ maintenance of the appropriate information and communication technology (ICT) systems and business processes;

(b) Accurate billing.

(c) Customer care and accounts enquiry management.

(d) Effective and timeous credit control.

(e) Impairment of debtors (Provision for Doubtful Debtors); and

(f) Write-off of uncollectable debtors.

1. OBJECTIVES OF THE POLICY

The objectives of this policy are:

(1) To ensure that the debtors disclosed in the annual financial statements are stated at amounts that are deemed to be collectable; and

(2) To ensure that uncollectable debt is written off within guidelines of applicable policies and legislation.

2. IMPAIRMENT OF DEBTORS

Consumer debtors, long term receivables and other debtors are stated at cost less allowance for impairment. Impairment is made on an individual basis or based on expected payment.

In accordance with GRAP104, an objective assessment of financial assets is made at year end (June) to determine whether there is any objective evidence that a financial asset or group of financial assets is impaired. Impairment loss is recognised as an expense in the Statement of Financial Performance.

The assessment for impairment will be done based on the Methodology Attached as Annexure A.

3. RESPONSIBILITY / ACCOUNTABILITY

The Council has the overall responsibility for adopting and approving the Provision for Bad Debts and Writing Off of Irrecoverable Debt policy.

4. WRITE –OFF OF DOUBTFUL DEBTORS

The following should be the guiding principles in implementing the policy on writing off of irrecoverable debt:

(1) The policy is in accordance with the Local Government Municipal Finance Management Act 2003, Local Government Municipal System Act 2000, as amended and other related legislation.

(2) Before any debt is written off it must be proven that the debt has become irrecoverable. To ensure that recommendations for write off are consistent and accurate, irrecoverable debt will be defined as:-

   (a) Where the tracing of the debtors is unsuccessful; and

   (b) All reasonable steps, at the discretion of the appointed write off committee, were taken by the officials to recover the debt.

(3) Bad debt write-offs must be considered in terms of cost benefit; when it becomes too costly to recover and the chances of collecting the debt are slim, a write off should be considered.

(4) Time value of money is very important because the older the debt becomes, the more difficult and costly it becomes to collect. It is therefore imperative that a proper system of credit control is implemented and maintained to avoid debt reaching the stage of becoming too expensive to recover.

(5) Differentiation must be made between those household consumers who cannot afford to pay for basic services and those who just do not want to pay for these services.

(6) Debt can only be written off if the required provision exists in the Municipality's budget and/ or reserves.

5. CATEGORIES OF DEBTORS THAT MAY QUALIFY FOR THE WRITING OFF OF

IRRECOVERABLE DEBT

Approved Indigent Household Consumers in terms of the Municipality's Indigent Policy

(1) Upon approval for registration as an indigent household consumer, the debtor's interest on the arrear amount will be written off.

(2) Any new arrears accumulated by the debtor (i.e. any amounts in excess of the indigent allowance for free basic services) whilst registered as an indigent consumer, will not qualify to be written off and must be dealt with strictly in accordance with the Municipality's Credit Control and Indigent Household Policy.

Balances too small to recover considering the cost for recovery

(1) Where final accounts have been submitted and paid by the respective consumer and the remaining balance after finalisation of any final readings and other administrative costs results in a balance of one hundred rand (R100) or less, such account must be forwarded once to the consumer for payment.

(2) Where such an account is not paid by the respective consumer within a period of sixty (60) days such amounts will automatically be written off.

Insolvency of the Debtor and Insolvent Deceased Estates

(1) Where a debtor becomes insolvent the Municipality must ensure that a creditor's claim is timeously registered. Any amount not being recovered due to insufficient funds or if there is a risk of a contribution being made to an insolvent estate must, after notification, be written off.

(2) In case of death of the debtor, a creditor's claim must be timeously registered against the deceased's estate. Any amount not being recovered due to insufficient funds or if there is a risk of a contribution being made to a deceased estate must, after notification, be written off.

Untraceable Debtors

(1) Where for any reason the forward address of a debtor becomes untraceable or the debtor becomes untraceable from the current address, such account must be handed over to a collection agent for recovery of the debt. The collection agent will be paid an all-inclusive fee that will be negotiated.

The Terms of Reference (ToR) for such collection agent must include the appointment of a tracing agent to locate the debtor. Should a debtor be untraceable, the collection agent must report to the Municipality on the actions that were taken to attempt to trace the debtor.

(2) Any amount owed by a debtor that has become untraceable must, after notification, be written off or sold to a debt collection agency at a discount.

(3) Debt written off in the above instances will automatically result in the debtor being reported to the credit bureau by the Municipality.

Special Arrangements in order to obtain a Clearance Certificate

(1) In terms of legislation, the Municipality will under normal circumstances not issue a Clearance Certificate on any property unless all outstanding amounts are paid to date, and a guarantee by the attorney handling the property transfer is issued in favour of the Municipality for the balance of the debt.

Special Incentives introduced by Council for Household Consumers in terms of the Approved Revenue Enhancement Strategy

(1) Notwithstanding the Municipality's Credit Control and Debt Collection Policy a debtor may enter into a written agreement with the Municipality to repay any outstanding and due amount to the Municipality under the following conditions:

- (a) The outstanding balance, costs and any interest thereon shall be paid in regular and consecutive monthly installments.
- (b) The current monthly amount must be paid in full; and
- (c) The written agreement has to be signed on behalf of the Municipality by a duly authorised officer.

(2) In order to determine monthly instalments, a comprehensive statement of assets and liabilities and income and expenditure, must be provided by the debtor and reviewed by a BTO official.

To ensure the continuous payment of such arrangement the amount determined must be affordable to the consumer (i.e. amount not to exceed 25% of gross income), considering that payment of the monthly current account is a prerequisite for concluding an arrangement.

(3) Due to ineffective/ non implementation of credit control measures in the past,

the majority of household consumers have accumulated significant arrear amounts and that these consumers are not in a position to pay of these arrear amounts in full together with their current monthly accounts.

In order to improve the current payment levels from consumers the Council of the Municipality may resolve to implement special incentives to address the arrear debt.

6. ESTABLISHMENT OF A COMMITTEE TO MONITOR ANY DEBT TO BE WRITTEN OFF

(1) Council will establish and appoint a committee to monitor the implementation of this policy.

(2) The committee will consist of the following members:

(a) The Municipal Manager (Chairperson).

(b) Chief Financial Officer (Alternative Chairperson).

(c) Member of the Executive Committee for Finance.

(d) One member of the Portfolio Committee for Finance to be nominated by the Portfolio Committee for Finance.

(3) The above committee will meet at least quarterly to receive and review a report from the Chief Financial Officer containing full details of any actions taken by officials with respect to this Policy, and to consider any circumstances not covered by this Policy.

(4) The quorum for the committee shall be 50% of the members plus one.

(5) Formal minutes of committee meetings must be prepared and submitted to Council.

(6) The Chief Financial Officer will, after thorough review of any applications in terms of this Policy, be delegated to write off any amounts to the maximum of;

(a) In the case of a household consumer an amount of R10,000 (excluding interest and penalties) per submission;

(b) In the case of a business consumer an amount of R20,000 (excluding interest and penalties) per submission; and

(c) Any amount in excess of the delegation provided for in paragraph 9.6.1 and 9.6.2 above must be submitted together with a recommendation to the Municipal Manager for consideration. The Municipal Manager will, after thorough review of any recommendation by the Chief Financial Officer and in terms of this Policy, be delegated to write off any amounts to the maximum of:-

- ❖ in the case of a household consumer an amount of R20,000 (excluding interest and penalties) per submission; and
- ❖ in the case of a business consumer an amount of R50,000 (excluding interest and penalties) per submission.

(7) Any amount in excess of the delegation provided for in sub-paragraph of 6(c) above may only be reviewed by the committee to monitor debt to be written off and must be submitted together with a recommendation to the Council for consideration.

7. DELEGATED POWERS ON WRITING OFF INTEREST AND PENALTIES ON RECOVERABLE DEBTS

The Chief Financial Officer will, after thorough review of any applications in terms of this Policy, be delegated to write off interest and penalties, **subject to full settlement account**, to the maximum of;

(1) In the case of a household consumers a total of R10 000 per submission.

(2) In the case of a business consumers a total of R20 000 per submission; and

(3) Any amount more than the delegation provided for in paragraph 1 and 2 above must be submitted together with a recommendation to the Municipal Manager for consideration. The Municipal Manager will, after thorough review of any recommendation by the Chief Financial Officer and in terms of this policy, be delegated to write off interest and penalties, **subject to full settlement of the account**, to the maximum of:

a) in the case of a household consumers a total of R20,000 per submission;

and

b) in the case of a business consumers a total of R50,000 per submission.

(4) Any amount in excess of the delegation provided for in paragraph 1 to 3(b) above may only be reviewed by the committee to monitor debt to be written off and must be submitted together with a recommendation to the Council for consideration.

8. APPLICATION OF PRESCRIPTION ACT

The provisions of Prescription Act will apply to all services debt, excluding assessment rates. Applications and/ or claims for prescription from debtors will only be assessed if no formal credit control or legal actions have been instituted during prescription debt period of three (3) years.

Budget and Treasury officials will assess application in terms of prescribed requirements. If in compliance with Prescription Act, approval may be granted to write-off prescribed portion of the debt in terms of the delegations' paragraphs above.

Reconciliation of the Provision of Doubtful Debtors Account must be prepared annually by the Chief Financial Officer and retained for audit purposes.

9. IMPLEMENTATION AND REVIEW OF THIS POLICY

This policy shall be reviewed on an annual basis by the Council. All future submissions for the writing off of debt must be considered in accordance with this policy.

ADOPTION OF THE POLICY

Policy adopted by Council of Port St Johns Local Municipality for implementation.

Approved by: Council On ______________________

Date

Resolution No. ______________________

Confirmed by the Honourable Speaker ________________________

Signature

Cllr C.S. Mazuza

APPENDIX A: METHODOLODY FOR IMPAIRMENT OF RECEIVABLES

1. PURPOSE

The purpose of this document is:

- To set out a methodology for the impairment of receivables 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;
- To promote transparency as required by sections 215 and 216 of the Constitution when dealing with receivables and debt; and
- To assist to discharge the Council responsibility as per paragraph 4.1.4 of the 'Credit Control, Debt Collection and Consumer Care Policy' which states that the Council must "provide for a bad debt provision, in line with the payment record of the community, ratepayers and residents, as reflected in the financial statements of the municipality".

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 ABBREVIATIONS

"CFO"	Chief Financial Officer
"Financial year"	Period 1 July of one year to 30 June of the following year (both days included)
"GRAP"	Generally Recognised Accounting Practices
"MFMA"	Municipal Finance Management Act 56 of 2003
"Municipality"	Port St Johns Local Municipality
"Reporting date"	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 "*All financial assets measured at amortised cost, or cost, are subject to an impairment review...*"

GRAP 104.57 "*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.*"

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 "*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."*

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."*

5. METHODOLOGY

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

The following accounts are specifically excluded from impairment testing:

- Receivable accounts with a combined credit balance at reporting date.
- Receivable accounts where the combined balance at reporting date is zero.
- Receivable accounts where the municipality is the owner; and
- Receivable accounts that have no balance outstanding longer than 30 days at reporting date as these accounts are considered not to be past due.

Any one of the following events is considered to provide objective evidence that a receivable account or group of receivable accounts could be impaired.

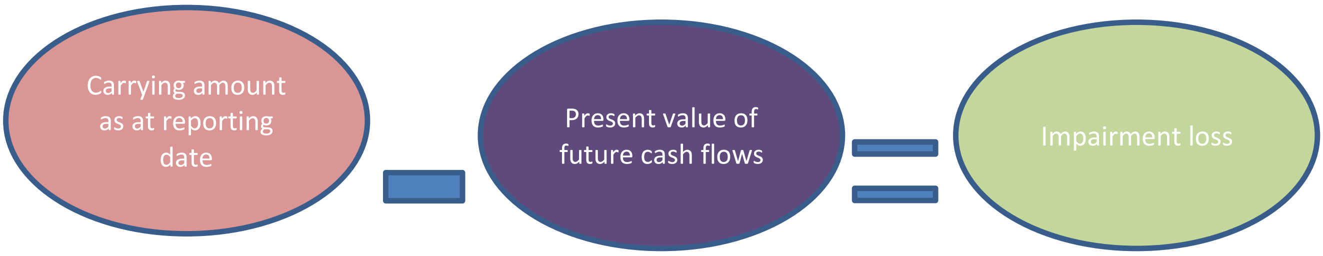
A receivable that has been placed under or applied for liquidation or sequestration.

- Where the last payment date by the customer was before 1 May of each financial year under consideration.
- Accounts handed over to debt collectors and/or attorneys.
- All accounts indicated as in-active accounts on the system;
- When a formal arrangement is made on arrears debt;
- When accounts have been formally presented to the CFO or Mayoral Committee for write off; and

- All accounts with balances outstanding 365 days and longer as these accounts are considered to be past due

c) Calculation and Recognition of Impairment Loss

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



The impairment loss is recognised in the statement of financial performance in the following accounts

Vote number	**Account description**	**Line item on statement of financial performance**
9/244-314-5151	MOVEMENT IN PROVISION	Impairment loss/Reversal of

	FOR BAD DEBTS	impairment loss

The impairment is recognised in the statement of financial position in the allowance accounts:

Account number	**Account description**	**Line item on statement of financial position**
629383160300	PROVISION FOR BAD DEBTS-TRAFFIC FINES	Provisions
629348063500	PROVISION FOR BAD DEBTS - REFUSE	
629348063400	PROVISION FOR BAD DEBTS - PROPERTY RATES	

d) Specifically Identified Receivables

Consumer receivables whose balances are in dispute, or which the Municipality has identified as having special collection risks, will be assessed individually for evidence of impairment.

For sundry receivables management will assess on an annual basis which accounts are individually material. These accounts will be assessed individually for evidence of impairment.

e) Risk Categories

All receivables are categorised into one of three risk categories. These categories are:

- High risk category;
- Medium risk category; and
- Low risk category.

The allocation of receivables into the different risk categories are reviewed annually as indicated below.

i) Consumer receivables

The following receivables are specifically identified as being high risk due to their nature:

1) Approved indigents;
2) Tenant accounts;
3) Non-active accounts;
4) Accounts in disputes; and
5) Account billed to incorrect debtors

The following receivables are specifically identified as being low risk receivables due to their nature and past payment history:

1) Government receivables, excluding government schools

The following receivables are specifically identified as being medium risk receivables due to their nature and past payment history:

1) Government school receivables

The remainder of the consumer receivables are classified as medium risk receivables.

All other receivables are divided into the three risk categories based on management's knowledge of these receivables.

Summary of risk groups for consumer receivables

High risk	Medium risk	Low risk
Approved indigents	Remainder of consumer receivable accounts	Government receivables, excluding government schools
Tenant accounts		
Non-active accounts		

ii) Sundry receivables

The following receivables are specifically identified as being high risk due to their nature and past payment history:

1) Closed accounts;
2) Marked to be written off; and
3) Handed over accounts
4) Account billed to incorrect debtor.

The remainder of the sundry receivables are classified as medium risk receivables. All other receivables are divided into the three risk categories based on management's knowledge of these receivables.

Summary of risk groups for consumer receivables

High risk	Medium risk	Low risk
Closed accounts	Remainder of sundry receivable accounts	Main service contributions
Marked to be written off		
Handed over accounts		Reallocation costs
Accounts billed to incorrect debtors		

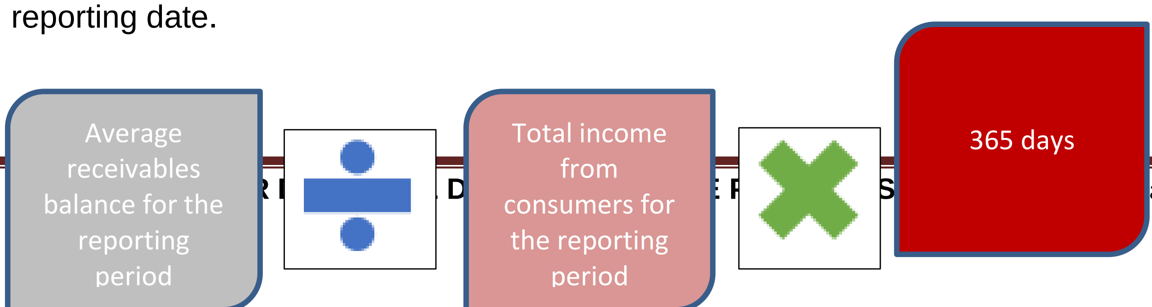
DISCOUNT RATE

The discount rate is set as the yield of the RSA Retail Bonds 3-year fixed rates. The actual yield on the RSA Retail Bonds is sourced from the rsaretailbonds.gov.za website at reporting date.

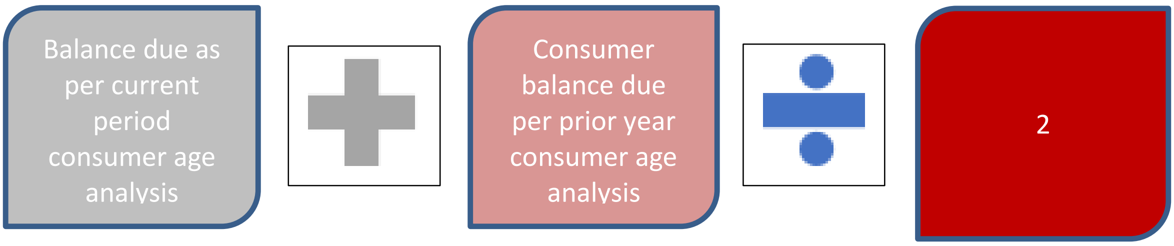
https://secure.rsaretailbonds.gov.za/ViewHistory.aspx

6. EXPECTED REPAYMENT TERM

One (1) expected repayment term is calculated for high, medium and low risk receivables. The expected repayment term is calculated as the receivables' days at reporting date.



The average receivables balance for the reporting period is calculated as follows:



The balance due per age analysis include both debit and credit balance. The total income from consumers for the reporting period includes:

a) Property tax;
b) Refuse;
c) Interest; and
d) VAT

7. EXPECTED FUTURE CASH FLOWS

The expected future cash flows are based on management's past experiences with the different receivable groups.

The expected future cash flows can be summarised as follows:

Group	Expected future cash flow
1. Indigent receivables	Accounts marked as indigent do not expect any re-payment and is therefore included at 100% in the allowance calculation
2. Inactive accounts	No payment expected and therefore provide for 100% impairment
3. Accounts marked as bad debts	No payment expected and therefore provide for 100% impairment
4. Accounts with balances paid only in current (30 days and less)	Fully recoverable
5. Accounts with no payment received in the last 0 - 365 days	Some payment expected and therefore provide for 80% impairment
6. Accounts with balances due between 0- 30 days	Some payment expected and therefore provide for 20% impairment
7.Accounts with balances due between 31- 60 days	Some payment expected and therefore provide for 40% impairment
8.Accounts with balances due between 61- 150 days	Some payment expected and therefore provide for 60% impairment
9.Accounts with balances due between 151 and above	Some payment expected and therefore provide for 75% impairment

8. PRESENT VALUE OF EXPECTED FUTURE CASH FLOWS

The present value of expected future cash flows is calculated using the present value formula in MS Excel. The data for input in the formula is the obtained from point 6, 7 and 8 above.

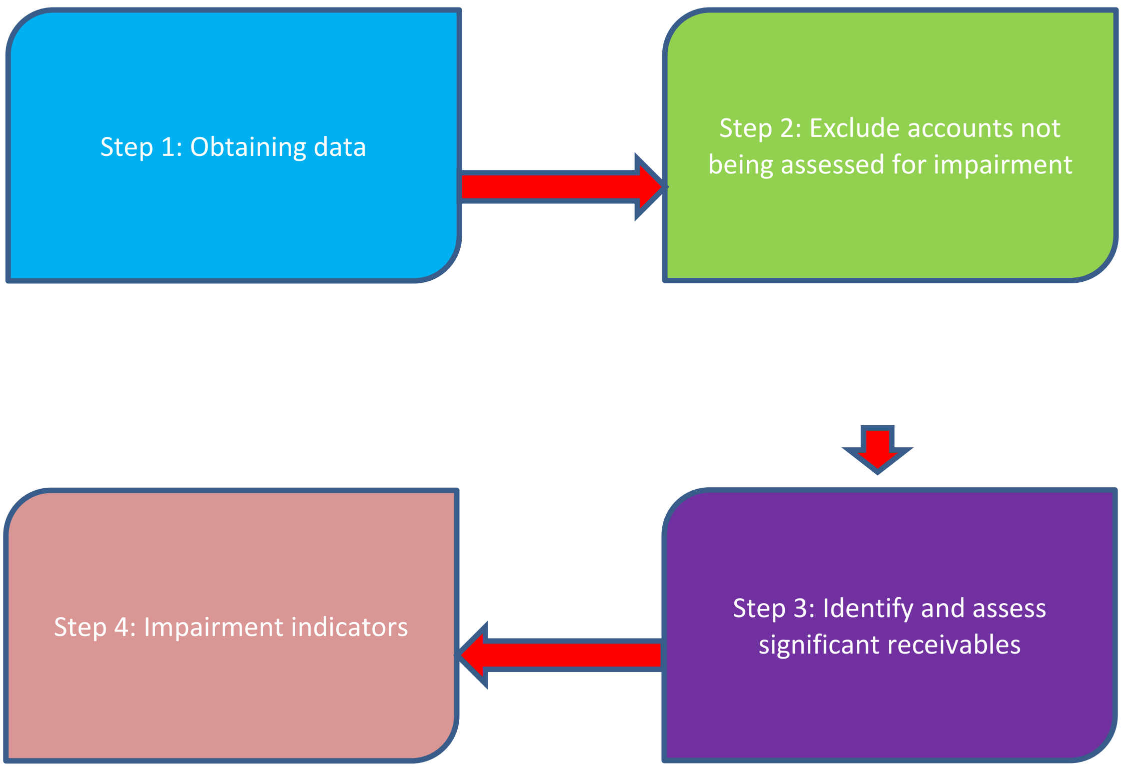
9. REVIEW OF METHODOLOGY

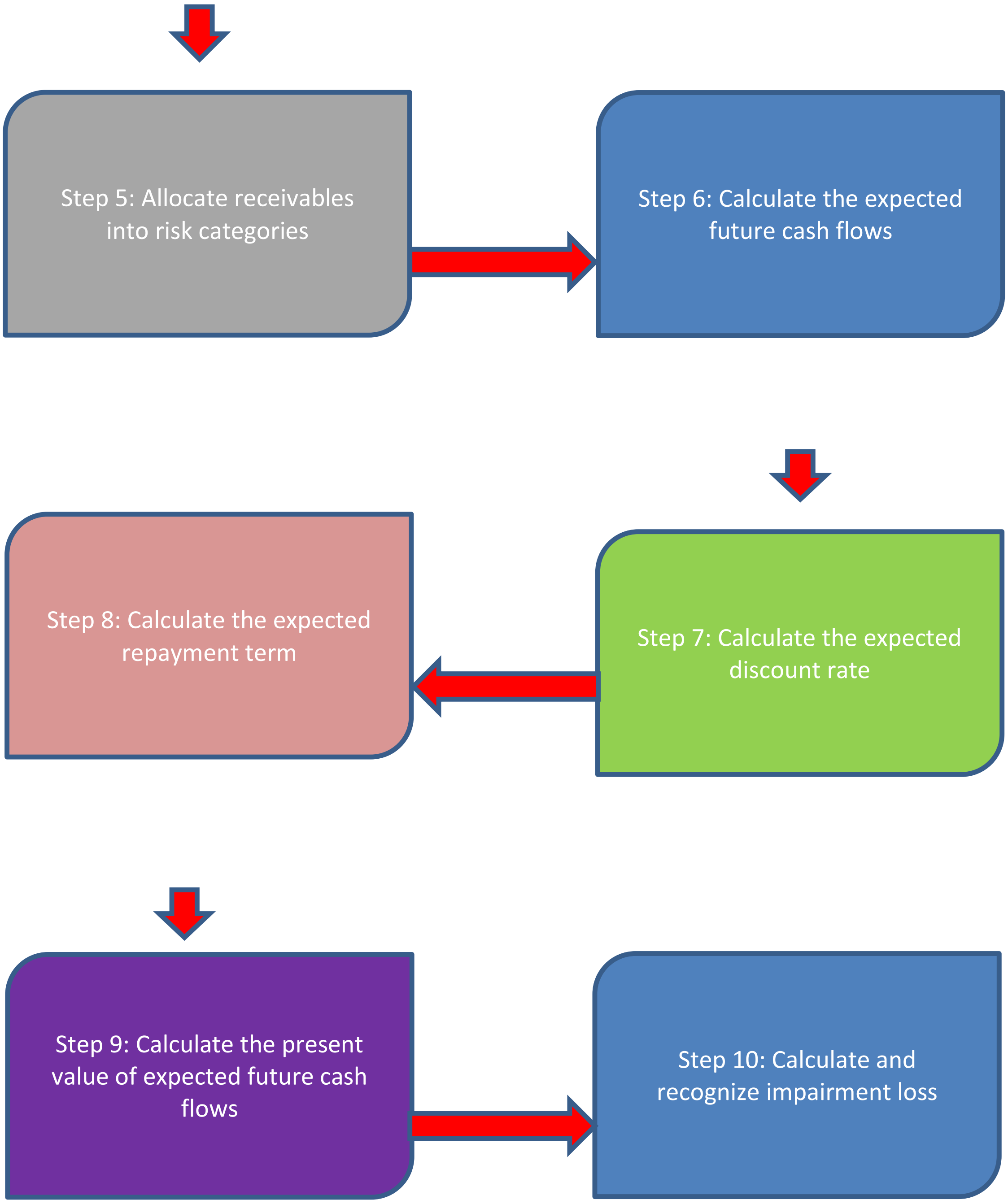
In terms of section 17(1)(e) of the MFMA polices must be reviewed on an annual basis and the reviewed policy tabled to Council for approval as part of the budget process.

10. SOURCE

a) GRAP 104 Financial Instruments issued October 2009 (Revised 1 April 2017)
b) GRAP 104 Application Guide issued October 2009
c) National Treasury Accounting Guidelines GRAP 104 Financial Instruments

APPENDIX B - WORK PROCEDURES – CONSUMER RECEIVABLES




Step 5: Allocate receivables into risk categories
Step 6: Calculate the expected future cash flows
Step 7: Calculate the expected discount rate
Step 8: Calculate the expected repayment term
Step 9: Calculate the present value of expected future cash flows
Step 10: Calculate and recognize impairment loss