LEPHALALE

LOCAL Municipality

DRAFT
DEBT IMPAIRMENT METHODOLOGY
2025/2026

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 annual 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.

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:

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

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."*

METHODOLOGY

1. 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.

2. Evidence of Impairment

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 are impaired.

The following accounts are specifically excluded from impairment testing:

- Receivables with credit balances
- Accounts due for less than 90 days
- Accounts in the name of the Municipality
- Government debtors.

The Municipality will make provision for doubtful debts by first assessing significant debtors individually. The following will be taken into consideration when debtors are being assessed.

- Aging of the debt
- Payment rate of the debtor.
- Property location.
- Category of the debtor

3. Significant receivables

The significance of a debtor depends on the amount determined by Management to be material for a type of a customer. The consumption of services and property rates differ according to the type of a customer. The amount considered significant for household, business and industrial differ and management has determined the significant debtors as follows:

- **Households:** A household debt is regarded as significant if such debt is more than R20 000 and over 90 days in arrears.
- **Businesses:** A business debt is regarded as significant if such debt is more than R60 000 and over 90 days in arrears.
- **Industrial:** A household debt is regarded as significant if such debt is more than R200 000 and over 90 days in arrears.
- **Farms:** All farm accounts are significant and impaired at 75% of the debt over 90 days.

Debtors are evaluated at the end of the reporting period and impaired as follows:

Risk category	Rate on amount over 90 days	Debtor Location
High risk	100%	Marapong and Thabo Mbeki
Medium risk	75%	Farms
Low risk	50%	Lephalale Town & Onverwacht

4. Insignificant debtors

Provision for impairment shall be made on insignificant debtors that are older than 120 days at a rate of 100% as follows:

- **Households:** A household debt is regarded as significant if such debt is less than R20 000 and over 120 days in arrears.
- **Businesses:** A business debt is regarded as significant if such debt is less than R60 000 and over 120 days in arrears.
- **Industrial:** A household debt is regarded as significant if such debt is less than R200 000 and over 120 days in arrears

Insignificant debtors are evaluated at the end of the reporting period and impaired as follows:

Risk category	Rate on balance over 120 days	Debtor Location
High risk	100%	Marapong and Thabo Mbeki
Low risk	100%	Lephalale Town & Onverwacht

5. Risk Categories

All receivables are categorised into one of three risk categories according to their location. These categories are:

- High risk category (100%)
- Medium risk category (75%); and
- Low risk category (50%).

6. Non-discounting of expected future cash flows

Appendix A to GRAP 104- Application guidance which is an integral part of the standard was considered in developing debt impairment methodology.

AG 5.10 Once the due date for short-term receivables has elapsed and payment is not received, an entity shall consider whether there is any indication that the receivable may be impaired, either because interest is not levied on outstanding amounts (using a market related rate of interest), or because the principal amount may not be collected".

It may be deduced from the above paragraph that receivables may be impaired because of one or both of the following two conditions:

1. Principal amount may not be collected
2. Interest is not levied on outstanding amounts (using a market related rate of interest)

The first condition that principal amount may not be collected

The second condition that interest is not levied on outstanding amounts or interest is charged at lower rate than market related does not exist as Municipality is charging interest on long outstanding receivables.
The interest charged is more than prime rate or government bond rate as the guide those rates may be used as market related. Therefore, additional impairment because of discounting future cash flows does not exist hence is not determined and recognized.

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
Group Accounts for Lephalale & Onverwacht	• The risk of receiving the payment on this category of debtors is low hence the impairment percentage is set at 50% • The culture of payment in town and Onverwacht is better compared to other geographical areas • The accountholders are the working class and substantial

	payments are coming from this group • The electricity supply is controlled by the Municipality and municipality is able to disconnect.
Group Accounts for Farmers	• The accounts in the Farmers' group are rated as medium risk • The risk of receiving the payment on this category of debtors is medium hence the impairment percentage is set at 75% • The electricity on the farmers is mostly provided by Eskom and the Municipality does not have control on the electricity supply where the electricity could be disconnected. • The municipality collects on farmers accounts when they sell their properties. • Farm accounts are mostly charged property rates and no other service chages.
Group Accounts for Marapong & Thabo Mbeki	• The accounts in the Marapong and Thabo Mbeki group are rated as high risk • The risk of receiving the payment on this category of debtors is high hence the impairment percentage is set at 100% • The electricity on the Marapong and Thabo Mbeki group is provided by Eskom and the Municipality does not have control of the electricity supply where the electricity could be disconnected. • The Municipality collects mostly on accounts when they sell their properties. • The culture of payment in Marapong and Thabo Mbeki group is lowest compared to other categories