



**RECEIVABLES POLICY FOR
TRINIDAD & TOBAGO ELECTRICITY COMMISSION**

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Appendix I – Aged Analysis of Receivables as at December 31, 2002

Responding to this Document

All persons wishing to comment on this document are invited to submit their comments by **May 16, 2005**. Responses should be sent by post, fax or e-mail to:

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1. INTRODUCTION

1.1 Background

Act No. 26 of 1998 established the Regulated Industries Commission (RIC) as a statutory body with the primary purpose of regulating providers of public utility services. Under Section 6 (1) of the Act, the RIC is empowered, among other things, to:

- ensure, as far as is reasonably practicable, that the service provided by the service provider operating under prudent and efficient management will be on terms that will allow the service provider to earn sufficient return to finance necessary investment;
- carry out studies of efficiency and economy of operation and of performance by service providers and publish results thereof;
- establish the principles and methodologies by which service providers determine rates for services; and
- carry out periodic reviews of the rating regimes of service providers.

In keeping with the RIC's mandate under the Act, the RIC felt that the issue of receivables of T&TEC was significant enough to warrant closer scrutiny with a view to developing policies, which would facilitate greater efficiency in the collection process. This would in turn reduce the additional costs that the utility would incur by having to source alternative financing to compensate for shortfalls in revenue brought about by late paying and defaulting customers.

1.2 Purpose of the Document

The purpose of this document is to review the billing and collection performance of T&TEC and to propose policies for the reduction of the receivables.

1.3 Structure of the Document

The remainder of the document is structured as follows:-

Section 2 examines billing and collection policies of T&TEC.

Section 3 assesses the costs imposed on the service provider by late paying customers.

Section 4 highlights proposal to improve billing and collection policies of service providers.

2. BILLING AND COLLECTION

2.1 Debt Recovery and Disconnection Policies

Table 1 below summarizes the debt recovery and disconnection policies as are currently applied by T&TEC.

TABLE 1. DEBT RECOVERY AND DISCONNECTION POLICIES

Existing Policy	T&TEC
Billing Cycle	Monthly for Industrial customers Bi-monthly for all other classes
Credit Period	Payment to be made within 14 days of bill date
Late Payment Penalty	Applied after 30 days from bill date at rate of interest on T&TEC's overdraft
Disconnection Policy	Service may be disconnected for any arrears appearing on invoice in excess of security deposit.
Reconnection Fee	\$145.00 plus VAT
Other Collection Strategies	At the discretion of the relevant manager, a disconnection crew may allow a customer to make good on payment of arrears on the day that the crew visits the premises without that customer being disconnected. However, the full disconnection/reconnection charge is still applied.
Uncollectible Revenues	Bad debts
Performance of The Collection Function	Functions associated with management of receivables are carried out by existing revenue collection staff

Source: T&TEC; PUC Order No. 80 of October 1, 1992

2.2 Aged Analysis of Debtors

One indicator that is usually used to measure the relative efficiency of a utility's commercial practices is the "Collection Period" (i.e. Accounts Receivable in days). Delayed collections can lead to significant cash flow problems, causing the utility to seek alternative funding to meet its short-term needs and thereby incur additional costs. **Appendix I** shows the summary of T&TEC's aged analysis of debtors broken down into the major categories.

As at December 31, 2002, T&TEC's accumulated receivables amounted to \$337.5 million, of which the public sector owed \$71.1 million (21.1%) and the private sector \$266.4 million (78.9%). (**Table 2**)

TABLE 2. T&TEC'S AGED ANALYSIS OF DEBTORS

	Total	0 - 30 Days	31 - 60 Days	61 - 120 Days	Over 120 Days
Domestic & General	52,227	26,927	12,305	7,954	5,041
Industrial	267,523	51,261	30,663	48,892	136,707
Street Lighting	17,742	2,170	1,729	2,490	11,353
Total	337,492	80,358	44,697	59,336	153,101

of which:

	Total	0 - 30 Days	31 - 60 Days	61 - 120 Days	Over 120 Days
Government	12,403	4,483	2,702	1,661	3,557
Statutory Boards	57,856	7,835	7,569	5,336	37,116
State Enterprises	830	710	102	18	0.457
Total	71,089	13,027	10,374	7,015	40,673

Source: T&TEC Finance Department, 2003.

The significance of these results can better be appreciated in terms of T&TEC's annual revenue. Based on annual revenue of \$1,338.9 million for 2002, receivables represent approximately 25% of electricity sales. Overall, T&TEC's private sector Industrial customers made up 63.6% of receivables while late paying Domestic and General customers comprised 15.5%. Industrial customers provided 65% of T&TEC's revenue from electricity sales.

2.3 Collection Period

Another gauge that is used to evaluate an entity's receivables is its collection period. This calculation shows the average time that consumers take to pay their utility bills. **Table 3** below shows the average collection period for T&TEC over the five (5) year period 1998 to 2002.

A collection period of 3 months or less is generally considered reasonable for the utility sector. As can be seen from the table, T&TEC's collection period average around 3 months over the period under review. This is a reasonable credit period, especially in light of fact that the Commission employs a bi-monthly billing cycle for all but its industrial customers. Generally a 3-month collection period will not unduly strain the working capital resources of an entity

TABLE 3. COLLECTION PERIOD 1998 - 2002

	Period Ended 31-Dec-2002 TTS'000	Period Ended 31-Dec-2001 TTS'000	Period Ended 31-Dec-2000 TTS'000	Period Ended 31-Dec-1999 TTS'000	Period Ended 31-Dec-1998 TTS'000
T&TEC					
a. Receivables	337,492	368,320	308,866	216,142	222,763
b. Revenues	1,338,909	1,220,757	1,174,227	1,112,150	1,090,870
Collection Period (a ÷ b x 365) - <i>days</i>	91	110	96	71	75
Collection Period (a ÷ b x 12) - <i>months</i>	3.00	3.62	3.16	2.33	2.45

Sources: T&TEC's Financial Statements

The RIC invites comments on what should be an acceptable collection period for T&TEC's receivables.

3. COST OF RECEIVABLES

Carrying costs that are incurred for utility rate collection include:

- Financing costs
- Operating Costs and
- Uncollectibles

Any revenues collected in respect of late payment fees and disconnection/reconnection fees normally go towards offsetting the total of these costs.

3.1 Financing Costs

The faster revenues are collected the lower the utility's need for working capital and thus for external financing. Financing costs represent interest costs which the utility incurs on borrowings that were undertaken to meet shortfalls in anticipated revenues from sales. This cost is therefore imposed on the utility through its late paying customers.

Ordinarily receivables would be financed through short-term borrowing or overdraft. In the case of the utilities however, overdue bills are a recurring problem of sizeable proportion. This therefore creates a long-term financing need which ultimately must be borne by ratepayers.

The financing costs of receivables for T&TEC were evaluated on the basis of an 11.00% overdraft interest rate with the assumption that the longest outstanding balance for T&TEC is one (1) year overdue. This assumption was used because T&TEC's statistics show an average credit period of three (3) months. (**Table 2**). The evaluation indicates that the cumulative financing costs for T&TEC for a one (1) year period is estimated at \$20.6 million or 1.6% of annual revenues.

3.2 Operating Costs

Operating costs are essentially the out of pocket expenses for the Utility, created by late paying customers. These costs include such expenses as postage associated with delivering reminder notices or disconnection notices; the cost of telephone calls to make "personal

contact” prior to disconnection; the cost of sending a crew to customer premises to disconnect service, litigation and other legal costs.

In determining or apportioning operating costs, only those costs that are incurred as a result of the late payment should be included. For example, if a utility uses existing staff for collection activities, the salaries paid to the staff do not impose an additional cost to the entity since these payments would have been incurred even without the performance of the late payment function. In T&TEC’s case, the existing staff performs late payment collection activities.

3.3 Uncollectibles

Gross uncollectibles or provision for bad debt, represent revenues due to the utility that, for whatever reason, the entity does not expect to collect. These are essentially the “bad debt” element. Net uncollectibles are gross uncollectibles less revenues that were written off in a prior period but were collected during the current period, i.e. recoveries. As shown in **Table 5**, it is the net uncollectibles that are included in the cost of receivables computations.

In 2002, uncollectibles of \$78.4 million were included in T&TEC’s receivables of \$337.5 million.

Collection Efficiency Indicator

One indicator that is normally used to measure improvements in efficiency of commercial practices is the level of a utility’s provision for Bad and Doubtful Debt. **Table 4** below shows T&TEC’s annual provision for bad debt for the period 1998-2002. An increase of 42% from \$55.1 million in 1998 to \$78.4 million in 2002 is observed. However, when the provision for bad debt is expressed as a percentage of sales, little variation is seen. This implies that T&TEC’s provision for bad debt policy has remained fairly constant over the 5-year period.

TABLE 4. PROVISION FOR BAD AND DOUBTFUL DEBT 1998 - 2002

	2002	2001	2000	1999	1998	Average
Provision for Bad and Doubtful debts (TT\$M)	78.39	59.26	51.78	49.40	55.10	58.78
Bad Debt Expense (TT\$M)	19.22	5.85	7.39	5.71	10.25	9.68
Sales Revenue (TT\$M)	1,338.9	1,220.8	1,174.2	1,112.2	1,090.9	1,187.4
Provision for Bad and Doubtful debts as % of Revenue	5.85%	4.85%	4.41%	4.44%	5.05%	4.92%
<i>Collection Efficiency (%)</i>	<i>94.15%</i>	<i>95.15%</i>	<i>95.59%</i>	<i>95.56%</i>	<i>94.95%</i>	<i>95.08%</i>
Bad Debt Expense as % of Revenue	1.44%	0.48%	0.63%	0.51%	0.94%	0.80%
<i>Collection Efficiency (%)</i>	<i>98.56%</i>	<i>99.52%</i>	<i>99.37%</i>	<i>99.49%</i>	<i>99.06%</i>	<i>99.20%</i>

The treatment of bad debt is a persistent area of difference of opinion among utilities and regulators. Regulators generally consider poor collection efficiency as an administrative failure on the part of the utilities.

There are two main areas of concern namely, provisioning for bad and doubtful debt and writing-off of bad debt. While regulators are not averse to allowing some provision for bad and doubtful debt in the course of normal operations of the utility, such provisioning needs to be backed up with processes to identify consumers who are not paying and then making adequate attempts to collect from such consumers.

With respect to writing-off receivables, there must be a clear policy and procedure for identifying and writing-off receivables and the utility must write-off unrecoverable arrears against the total provision. Any ad-hoc write-off proposals are generally not acceptable to regulators. Furthermore, a detailed study should be conducted periodically to ascertain the appropriate percentage for write-off for each category of customer and to update the percentage so determined.

T&TEC's policy on bad debt provision, as stated in its audited accounts is as follows:-

“Trade receivables are carried at original invoice amount less provision for impairment of these receivables. A provision for impairment of trade receivables is established when there is objective evidence that the Commission would not be able to collect all amounts due according to the original terms of receivables”

Research shows that regulators in other developing countries allow a bad debt provision of 3.00% of the total value of sale of electricity for purposes of computing the revenue requirement. **In light of the above, the RIC will be willing to permit reasonable provisions for bad and doubtful debt so long as the service providers demonstrate the will and diligence to identify and write-off actual bad debt while making necessary efforts to recover the amounts that are collectable.** The RIC emphasises that in the absence of a clear policy and procedures for identifying and writing-off receivables, the RIC will be guided by best practice to determine an adequate provision for bad and doubtful debt in computing the service provider's revenue requirement.

The RIC invites comments on its above stated position on writing-off bad debt and an adequate provision for bad and doubtful debts.

3.4 Offsetting Revenues

Utilities are sometimes allowed to assess a charge on overdue amounts that are outstanding beyond the credit period. A reconnection fee is also charged by utilities when reconnecting a customer that was terminated for nonpayment. These charges provide revenues that defray some of the costs incurred when payments are made late.

T&TEC currently assesses a late payment charge on amounts outstanding after 30 days from bill date at the rate of the Commission overdraft interest. T&TEC's reconnection after disconnection fee is \$145 plus VAT. The RIC views these as reasonable practices that should be continued in the future.

Table 5 below summarises the costs incurred by T&TEC in 2002, arising directly from T&TEC's late paying customers. **These have been estimated to be \$44,698,000.**

TABLE 5. T&TEC'S COST OF RECEIVABLES, 2002

COSTS 2002	\$TT'000
Annual Financing Costs (estimated @ 11.00% p.a.)	\$20,573
Operating Costs	\$4,988
Gross Uncollectibles (gross increase in bad debt provision)	\$44,291
Offsetting Revenues (recoveries)	(\$25,154)
TOTAL	\$44,698

The RIC invites comments on its above method of calculating the costs imposed on T&TEC by late paying customers.

4. PROPOSED POLICY MEASURES

The following proposals take the above-mentioned factors into consideration and provide suggestions that are practical and that can be easily implemented to improve collections.

4.1 Reserve Vote

Public Sector customers accounted for \$71.1 million or 21.1% of T&TEC's receivables as at December 2002 (**Appendix I**). A reserve vote can be set up for all public sector enterprises that receive a subvention from the central government through budgetary allocations.

Arising from the national budgeting process, funds are allocated to each Ministry under individual votes. The Reserve Vote system makes specific, separately identified allocations for utility bill payments. These funds are 'reserved' under a separate line item in each Ministry's vote and *can only be used* for the stated purpose i.e. payment of utility bills. This measure ensures that the utility receives its rate payments from Government and that the Ministries do not divert the funds to its other expenses.

It is proposed that this system be reintroduced and, further, that a similar mechanism be put in place for other state bodies that receive a subvention from Government. Since public sector enterprises do not have a vote, a variation of the reserve vote system could be implemented. This system could be administered either at the level of the Ministry of Finance (where releases could be sent directly to the service providers), or through the various line Ministries, for those state bodies which fall under their purview. The relevant Ministry would be charged with the responsibility of remitting funds allocated for utility payments directly to the service providers without having these releases pass through the state bodies for onward transmission. If Government agencies are delinquent then it would be difficult to control others. The RIC hopes that the Ministry of Finance would issue strict instructions so that this practice of late payment is stopped. In the interim, the Government may wish to consider advancing an interest free loan to compensate T&TEC for electricity rates owed by government ministries, state enterprises and other public sector agencies.

The RIC invites comments on the suggested:

- *Reintroduction of a Reserve Vote for addressing the problem of T&TEC's public sector debtors.*
- *Variation of the reserve vote system for addressing the problem of public sector enterprises.*

4.2 Conversion to *Monthly* billing cycle

An entity's collection period will clearly be a function of its billing cycle. T&TEC currently operates a bi-monthly billing cycle (with limited exceptions). This automatically means that the Commission has to wait an additional 30 days to collect the earlier month's revenues. It follows therefore, that if T&TEC were to introduce monthly billing, all things being equal, the utility should be able to reduce its non-industrial receivables by approximately 33%.

This measure would also be beneficial from the consumer's point of view since the average householder budgets on a monthly basis. Monthly billing would therefore better coincide with customers' cashflow cycle.

The RIC invites comments on the introduction of a monthly billing cycle for all T&TEC's customers

4.3 Measures for Reducing Costs of Receivables

The under-mentioned measures could be implemented to help the utilities control the costs associated with managing receivables:

- In order to determine level of expenditure that is appropriate to improve the collection process, a simple break-even model could be developed. Historical data could be used to determine the changes in capital costs and uncollectibles the entity would experience if it were to invest a fixed proportion (suggested 0.50%) of its revenues in collecting overdue accounts. This measure is intended to set an

upper limit for expenditure on receivables. In this way the benefits to be derived from each additional \$1.00 of expenditure will determine whether or not the additional collection measure should be undertaken.

- Inability to locate consumers could contribute significantly to utilities' uncollectibles. One means of reducing this problem is for the entity to demand positive identification from all prospective customers. The utility may also wish to consider enlisting the assistance of the Trinidad and Tobago Postal Corporation (TTPost) to obtain independent verification of customers address information. A third option is for the utility to collect a deposit as a condition for providing service. T&TEC's tariff structure allows for (and the Utility enforces) a refundable service charge of \$95 for domestic and commercial customers and the minimum demand charge of one (1) month for industrial customers.
- In an effort to reduce its uncollectibles, T&TEC may wish to consider referring its long overdue balances (outstanding for over 1 year) to outside collection agencies, credit bureaus or attorneys for further action. Collection agencies in particular are useful in locating and collecting from customers who have migrated to other countries.
- Additional revenues earned through the utilities' reconnection charge would go some way toward offsetting the cost of receivables. This charge should reflect current costs in order to compensate the utility for its outlay on the disconnection/reconnection process. T&TEC's reconnection rate of \$145 plus VAT reflects 1992 prices when the last rate increase was awarded. The RIC feels that the tariff structure should allow for periodic reviews and updates of the reconnection charge to better reflect current market prices.
- A late payment charge (LPC) is another possible source of revenues for reducing receivables costs. The primary purpose of the LPC is to compensate the utility for expenses associated with delinquent payments. These expenses are identified at

Section 3 above. T&TEC currently assesses a late payment charge on amounts outstanding after 30 days from bill date at the rate of the Commission's overdraft interest. It is a common practice among regulators to allow a late payment charge of 2.00% per month on the amount outstanding after 1 month from the bill date. The RIC views this benchmark favourably for tariff setting purposes and believes that the 2.00% charge will not only assist the utility in gaining compensation for its out of pocket expenses but it would also serve as an inducement to customers to pay their bills promptly.

The RIC invites comments on:

- *a cost based reconnection-after-disconnection charge for T&TEC.*
- *other proposed measures for reducing costs of receivables.*

4.4 Other Collection Measures

- A common practice among utilities is to transfer the unpaid balance to another known service address that is used by the delinquent customer. Service may subsequently be disconnected at the new location if the previous balance is not resolved.
- Opening of cash collection centers for longer hours would facilitate bill payment for consumers who are at work during regular opening hours

- Making locations for bill payment more accessible to customers would also go some way towards improving the collection process. This is especially true for the rural areas. T&TEC may wish to set up mobile offices with specific schedules for addressing this option.

5. ISSUES FOR CONSULTATION

Consistent with its commitment, the RIC will consider the views of the stakeholders and other interested parties before reaching a final position.

The RIC will welcome comments on the following more detailed issues raised in this paper:

- *An acceptable collection period for T&TEC's receivables.*
- *The RIC's position on writing-off the receivables and provision for bad and doubtful debts.*
- *The RIC's method of calculating the costs imposed on T&TEC by late paying customers.*
- *On the suggested:*
 - *reintroduction of a Reserve Vote for addressing the problem of T&TEC's public sector debtors.*
 - *variation of the reserve vote system for addressing the problem of public sector enterprises.*
- *Introduction of a monthly billing cycle to replace the existing bi-monthly billing*

- *A cost based reconnection-after-disconnection charge for T&TEC.*
- *Other proposed measures for reducing costs of receivables.*