date	subject	item
4/1/93	**CLASSIFYING ACCOUNTS RECEIVABLE**	**K-022**
supersedes		page **1**

A. Purpose and Scope

This item establishes policies and procedures prescribed by the Director of the Budget for all State agencies regarding the classification of State agencies' accounts receivable.

The number and dollar value of a State agency's total accounts receivable provide a limited view of the State agency's management of its accounts receivable. A significant increase in the level of accounts receivable, for example, could be attributed to a number of reasons. These reasons include a substantial increase in new debts, a reduction in debt payments or an agency's inability to collect payment in full.

In addition, a State agency may not be able to collect payment for all of its accounts receivable, so the total accounts receivable may overstate the revenue that the State agency reasonably expects to collect.

To better measure the condition and actual revenue potential of an agency's accounts receivable, the State agency must age its accounts receivable and prospectively estimate an allowance for uncollectible accounts. Moreover, since a State agency is responsible for monitoring the status of debts owed to it, the agency must continue to age debts that it has referred to outside collection entities (e.g., a private collection agency, the Attorney General's Office, and the Department of Taxation and Finance).

In certain instances, a write-off or a discharge may be appropriate.

B. Aging

1. State Agency Responsibilities

For a State agency to estimate the collectibility of its accounts receivable and properly focus its collection efforts, it must "age" each outstanding account receivable relative to its due date. Unless provided otherwise by State or Federal statute, or regulation, contract, coupon book, or in the case of medical debt, the due date of a debt is five days after the first bill is sent to the debtor — day 6.

An account receivable is "due and owing" one day after the due date (five days after the mailing of the first bill — day 6) until 30 days later (35 days after the mailing of the first bill — day 36). <u>If the account is paid in full by the due date or during the due and owing period, it is considered fully satisfied.</u>

However, if the debt is not fully paid by the 30th day after the due date (day 36), then the debt is considered **past-due**, and the debt is aged from its due date (five days after the mailing of the first bill — day 6).

The following table illustrates an accounts receivable aging timeline.

2. Procedure

A State agency's accounts receivable for each fund normally should be placed into eight classes:

i. Due and owing (1-30 days after the due date)
ii. 31-60 days past-due
iii. 61-90 days past-due
iv. 91-120 days past-due
v. 121-180 days past-due
vi. 181 days to 1 year past-due
vii. +1 to 3 years past-due
viii. Over 3 years past-due

Classifying the accounts receivable in the above manner provides a State agency with an ability to analyze and manage its debts. A change over time in the proportion of accounts receivable in each category may be a useful indicator of debt collection performance.

It is important to note that if a State agency refers a past-due debt to the Attorney General's Office or to a private collection agency or certifies a debt to the Department of Taxation and Finance, that State agency must continue to age the referred debt in its accounts receivable records.

C. Estimating Allowance for Uncollectible

1. State Agency Responsibilities

A State agency must prospectively estimate the accounts receivable that it does not anticipate collecting. This estimate is necessary for both sound governmental accounting practices and for the quarterly and annual reports that every State agency must submit to the Division of the Budget as required by Item K-023. Each State agency will be required to report "Net Accounts Receivable" in the quarterly and annual reports. Net Accounts Receivable is defined as

	Gross (total) Accounts Receivable
less:	<u>Allowance for Uncollectible Accounts</u>
	Net Accounts Receivable

The "Allowance for Uncollectible Accounts" represents the State agency's prospective estimate of outstanding receivables that the State agency believes will ultimately be uncollectible. It represents the estimated revenue loss to the State.

It is important to note that estimating an allowance for uncollectible debts <u>does not mean that a State agency is released from its responsibility to use its best efforts to collect debts</u>. Rather, the allowance for uncollectible is a tool to convey a reasonable estimate of collectible revenue. A State agency still should collect payment for every debt, to the degree possible.

2. Procedure for Estimating Uncollectible Accounts

The method for prospectively estimating the uncollectible portion of accounts receivable will vary by State agency and type of account receivable. Generally, the estimate of uncollectible accounts will be based upon the collection experience of the State agency and the age of the particular accounts receivable. In general, as a debt ages, the probability of collection declines.

In order to establish internal guidelines for estimating the appropriate allowance for uncollectible accounts, each State agency should examine the collection history for each type of account receivable that it maintains within its accounts receivable system. Since these collection histories will vary by State agency, this section does not specify the estimating procedures to be used.

Each State agency is required to provide a copy of its procedures for computing an allowance for uncollectible accounts to the Division of the Budget and to the Office of the State Comptroller for informational purposes.

The following example may be used as a guide to assist State agencies in establishing internal procedures for estimating an allowance for uncollectible accounts.

3. Example

The following procedure demonstrates a general approach to estimating an allowance for uncollectible accounts:

Fund "A" Aged Accounts Receivable Summary:

AGING	FEES	OTHER
Due and owing	$100,000	$50,000
Past-Due:		
31-60 days	5,000	1,000
61-90 days	4,000	800
91-120 days	500	0
121-180 days	500	0
181 to 1 year	500	0
+1 year to 3 years	500	0
Over 3 years	100	0
Total Past-Due	11,100	1,800
Total Accounts Receivable	$111,100	$51,800

A review of outstanding accounts receivable and an examination of the collection history of Fund "A" reveals that the following percentages of each aging category have historically proven to be uncollectible:

AGING	FEES	OTHER
Past-Due:		
31-60 days	1%	1%
61-90 days	2%	2%
91-120 days	3%	2%
121-180 days	7%	3%
181 to 1 year	10%	3%
+1 year to 3 years	15%	3%
Over 3 years	25%	5%

These historical percentages are applied to the balances in the Aged Accounts Receivables Summary to compute the Allowance for Uncollectible Accounts:

AGING	FEES	ALLOW.	OTHER	ALLOW.
Past-Due:				
31-60 days	5,000 x 1%	$50	1,000 x 1%	$10
61-90 days	4,000 x 2%	80	800 x 2%	16
91-120 days	500 x 3%	15	0 x 2%	0
121-180 days	500 x 7%	35	0 x 3%	0
181 days to 1 year	500 x 10%	50	0 x 3%	0
+1 year to 3 years	500 x 15%	75	0 x 3%	0
Over 3 years	100 x 25%	25	0 x 5%	0
Total	$11,100	$330	$1,800	$26

Summary of Allowance for Uncollectible Accounts:

Allowance for "Fees"	$330
Allowance for "Other"	26
Total Allowance	$356

As a result of applying historical collection experience to the accounts receivable, net accounts receivable can be computed:

	Gross Accounts Receivable	$162,900
Less:	Allowance for Uncollectible	(356)
	Net Accounts Receivable	$162,544

D. Write-off

1. Definition
A write-off is an accounting entry by which an account receivable deemed to be uncollectible is removed from the State agency's financial accounting records. A write-off is not to be considered a discharge of debt. Thus, a debt, although written-off, is still owed to a State agency. (A discharge, compromise, or settlement, on the other hand, is a legal extinguishment of debt.)

2. State Agency Responsibilities

While a State agency must pursue collection of its past-due accounts, it may determine that, due to the size and nature of a particular account receivable, continued routine collection efforts for that account are not cost-effective. In these instances, the State agency may decide to write-off the account receivable.

However, a State agency should consider a write-off only after all reasonable efforts to collect payment have been exhausted and the estimated cost of collection makes further collection actions cost-ineffective. Such determination should only be made if a State agency's central fiscal or business office has approved such action.

In addition, the Attorney General's Office may direct a State agency to write-off certain debts that the agency has referred to the Attorney General's Office.

3. Parameters for Write-Off

A State agency must document that aggressive collection efforts preceded any write-off. In addition, the value of the debt should assist in determining whether a debt should be written-off:

a. <u>$1 - 1,000</u>

As a general rule, any debt of $1,000 or less should not be written-off unless it is more than two years past-due and no payments have been made over this period of time.

If an account receivable is between $25 and $1,000 and qualifies as a past-due legally enforceable debt, the account should not be written-off until the State agency has certified the account to the Department of Taxation and Finance for offset at least once and such debt has undergone one tax cycle.

However, if an account receivable cannot be certified to the Department of Taxation and Finance as the result of missing required data, such as a Social Security Number, and the State agency can demonstrate that it has made diligent efforts to acquire the missing data, lack of certification shall not bar write-off of the account.

b. <u>Over $1,000</u>

As a general rule, any account receivable over $1,000 should not be written-off before it is five years past-due and no payments have been made over this period of time. Accounts receivable that are over $1,000 and qualify as past-due legally enforceable debts should be certified for offset prior to being written-off.

Certain cases may not fall into these parameters and an agency may determine that write-off is warranted. For example, conditions may exist where the estimated cost of collection exceeds the recovery value or the applicable statute of limitations has expired.

4. Internal Guidelines

Each State agency must establish its own internal guidelines regarding procedures for write-off and clearly designate the agency representatives who are authorized to write-off debts.

Agency guidelines must ensure consistency across the programs and regional offices of the State agency. The State agency must submit its internal guidelines for write-off to the Division of the Budget for approval and to the Office of the State Comptroller.

5. Procedure

When a State agency writes-off a debt, it must adjust both the gross accounts receivable and the allowance for uncollectible debt. In this manner, the net accounts receivable remains the same. For example, if a State agency wrote-off a debt for $100, it would adjust its accounting records in the following manner:

		Before Write-off	After Write-off
	Gross Accounts Receivable	$96,000	$95,900
less:	Allowance for Uncollectible	(9,600)	(9,500)
	Net Accounts Receivable	$86,400	$86,400

6. Documentation

The State agency must maintain complete documentation of the reasons for writing-off any account receivable. The State agency must maintain documentation on written-off accounts for five years.

7. Inter-agency Receivables

   Inter-agency receivables, such as internal service accounts receivable and appropriated loan receivables, cannot be written-off without the approval of the Division of the Budget.

E. Discharge, Settlement, Compromise

1. Definition

   Discharge, settlement, and compromise involve the legal extinguishment of disputes, claims, and controversies — in full or in part.

2. State Agency Responsibilities

   In certain instances, a State agency may determine that it will be unable to collect full or partial payment of a debt. Unlike a write-off, which adjusts a State agency's accounting records, a discharge, settlement, or compromise means that the debtor no longer owes all or part of the original debt and that the State agency will not pursue any further collection measures. Thus, it is appropriate to permanently remove the debt from the State agency's financial accounting records.

3. Limitations

   Unless provided otherwise by State or Federal statute, only the State Attorney General may authorize a discharge, settlement or compromise of a debt.

4. Procedure

   a. If a State agency determines that discharge, settlement or compromise is appropriate, it must submit a request in writing to the Attorney General's Office, unless provided otherwise by Federal or State statute.

   b. The State agency cannot take any further action until the Attorney General's Office notifies that State agency in writing that the debt has been discharged, settled, or compromised.

   c. If the Attorney General's Office determines that discharge, settlement or compromise of an account that has been referred to the Attorney General's Office is appropriate, it will advise the referring agency in writing of its determination without the need of a separate request from that agency.

d. If the State agency receives written notification from the Attorney General's Office that a debt has been discharged, settled, or compromised, then the State agency should adjust its financial accounting records accordingly.

Specifically, if the agency has not already written-off the debt, it should adjust its Beginning Gross Receivables for the quarter in which the Attorney General's Office discharged, settled, or compromised the debt. For example, if a $1,000 debt was discharged, the State agency would make the following adjustment:

Beginning Gross Receivables	$100,000
Adjustments: Increase (decrease)	(1,000)
Gross Receivables	$ 99,000

e. The determination of how to reconcile the records of an account that has been discharged, settled or compromised should be based on guidelines provided by the Office of the State Comptroller.