

**LOCAL GOVERNMENT**

**VIABILITY:**

**THE IMPORTANCE**

**OF**

**CREDIT MANAGEMENT**

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**LOCAL GOVERNMENT  
VIABILITY:  
  
THE IMPORTANCE  
OF  
CREDIT MANAGEMENT**

BY

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## UITTREKSEL

### **DIE BELANGRIKHEID VAN KREDIET BESTUUR BINNE PLAASLIKE OWERHEDE**

Die finansiële lewensvatbaarheid van plaaslike owerhede in Suid Afrika word onder geweldige druk geplaas as gevolg van die nie betaling vir munisipale dienste. Hierdie tendens van wanbetaling het sy oorsprong gehad toe die sogenaamde vryheids politisie dit as 'n hefboom gebruik het om swart plaaslike owerhede tot 'n val te bring. Na die samesmelting van die blanke en swart plaaslike owerhede het hierdie tendens egter bly voortduur.

Die nie betaling vir munisipale dienste het tot gevolg dat plaaslike owerhede nie genoegsame fondse in om kapitale projekte te kan finansier nie. Groot skaalse kapitale projekte word benodig om die agterstand in die infrastruktuur van die eertydse swart dorpe in te haal. In sommige gevalle is die probleem van so 'n aard dat bedryfsuitgawes nie gefinansier kan word nie. Dit lei daartoe dat plaaslike owerhede nie hulle grootmaatverskaffers kan betaal vir dienste gelewer nie.

Die infrastruktuur in die swart plaaslike owerhede was van 'n lae standaard weens swak instandhouding in die verlede. Die verbruikers het begin eis dat die dienste eers opgegradeer word voordat betaling vir die dienste sal geskied. Dit het die plaaslike owerhede met 'n dilemma gelaat aangesien geld nodig was vir die opgradering van die infrastrukture maar daar slegs 'n beperkte invloed van kontant was.

Die enigste oplossing van die probleem lê in die invordering van die uitstaande bedrae deur effektiewe krediet bestuur. Plaaslike owerhede vanweë hulle monopolistiese aard het egter in die verlede nie die basiese krediet bestuur beginsels toegepas nie. Dit het egter nou nodig geword dat elke plaaslike bestuur 'n behoorlik gedokumenteerde krediet bestuur beleid moet saamstel en laat goedkeur deur sy raad.

Hierdie kredietbestuur beleid moet al die aspekte van munisipale dienstelewering aanspreek aangesien net die sny van elektrisiteit nie meer genoeg is nie. Dit het nodig geword om al die ander dienste ook by die proses in te sluit. Daar moet ook in die beleid aandag gegee word aan die sosio-ekonomiese probleme binne die gemeenskap. Dit kan gedoen word deur tegemoetkomings vir die ekonomies agtergeblewende lede van die gemeenskap in die beleid in te skryf.

Die nodigheid om hierdie krediet bestuur beleid op skrif en goedgekeur deur die raad te kry spruit uit die deursigtigheids beginsel. Die verbruikers moet vooraf kennis dra van die stappe wat gaan volg in die geval van nie-betaling. Net so is dit ook belangrik dat die personeel in die krediet bestuur afdeling duidelike riglyne sal hê waarvolgens hulle moet optree. Dit verseker die regverdige en eenvormige optrede teen al die nie-betalers.

Hierdie skripsie het dus ten doel om ondersoek in te stel na die vlak van krediet bestuur in plaaslike owerhede. Uit die resultate van die ondersoek word dan beoog om spesifieke voorstelle te maak aangaande die uitleg van 'n behoorlik omvattende krediet bestuur beleid vir plaaslike owerhede.

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# CHAPTER ONE

## NATURE AND SCOPE OF THE STUDY

### 1.1. Introduction

Over the decades local government in South Africa has experienced many changes. Local authorities were reasonably financially autonomous until the mid 1980's when the government and freedom movements started utilising municipalities as a political weapon. Through boycott actions and a drastic cutback in government subsidies the predominantly black local authorities were destroyed economically whilst the predominantly white local authorities remained relatively stable.

During early 1994 the government accepted legislation which forced previously separate black and white local authorities to amalgamate. Councillors were appointed in terms of amalgamation agreements. In 1995 and 1996 councils were elected on a quota system. According to the White Paper on Local Government (SA, 1998:12) this transition has resulted in a local government system consisting of 843 local authorities with over 11 000 democratically elected councillors. Approximately one third of these local authorities are facing serious financial difficulties or administrative problems at this point in time.

The process of change in local government has, however, not yet been finalised. The White Paper on Local Government (1998:12) declares the intent of the Central Government to drastically reduce the number of local government institutions in South Africa. After the election held on the 2<sup>nd</sup> of June 1999 the newly established Demarcation Board has the task of establishing new local government boundaries throughout South Africa. In order to give effect to the intention to reduce the number of local government institutions, the Demarcation Board will have no option but to enforce further amalgamations.

Currently the majority of local authorities do not have the financial capacity to accept this burden, especially in view of the fact that the culture of non-payment, which was created to destroy the black local authorities, still exists. The result is that many local authorities are for all practical purposes on the brink of insolvency or even worse, bankruptcy. Many of the local authorities are heavily in debt to suppliers of bulk local government services and regularly do not have sufficient funds to pay their employees.

## **1.2. Background to this study**

Historically, in urban South Africa local government revenue was mainly self-generated through property taxes and the delivery of services to residents and businesses. Whilst this worked well for the former white local authorities this system failed dismally in the former black local authorities.

A consolidated account is sent to the customer each month, which then has to be paid. The accumulated income of all these accounts, together with any grants received from Central and/or Provincial Government, is then utilized by the local authority to cover costs to provide services and to maintain infrastructure. Large projects such as buildings, construction of roads, service networks, etc. are done by utilising borrowed capital. The capital and interest, together with all other operating expenses, must be paid out of funds obtained from the services provided.

The major dilemma for local government at this point in time is not to bill the customer for the services enjoyed, but to convince the consumers to pay. The operating budget of a local authority controls the operations of the local authority. Service delivery to the community is entirely dependent on the collection of all budgeted income. If actual income in a financial year falls short of the budgeted figure, expenditure will have to be reduced which would mean curtailing services or lowering the standard of service.

Without the necessary cash flow the local authority will not be able to pay its creditors which again will have the effect that service provision will come to a complete standstill.

A lesson can be learned from the failure of the former black local authorities which resulted from the non-payment of services. Interventions must be put into place to manage the dilemma to prevent a reoccurrence thereof.

### **1.3. Problem formulation**

The vast increase in the responsibilities of local authorities without a concurrent increase in the income base has placed severe strain on the finances of local authorities.

The “Freedom” politicians, in an effort to destroy the former black local authorities, created a culture of non-payment. After the amalgamation of black and white local authorities this culture that was created over a number of years remained in force. The newly formed local authorities have to change the culture of non-payment to a culture of payment as their livelihood depends on the income received from the payment of services. This change involves the return from a culture of non-payment to a culture of payment. Local authorities are obliged to incur expenditure to purchase bulk services and this culture of non-payment means that consumers are utilizing services, which they have not paid for. This detrimentally affects the cash flow of local authorities and they are therefore experiencing financial stress and in some cases crisis (White Paper on Local Government SA, 1998:8).

The increase in debtors reflects the inability of local authorities to deal with the level of non-payment. The non-collection of outstanding accounts has serious implications for a local authority's cash flow. This emphasizes the need for local authorities to develop and implement stringent credit management tools to stem the escalating arrears debtors' amount and to create a culture of payment for services. The financial survival of local government depends on effective credit management.

## **1.4 Objectives of the study**

### **1.4.1 Main objective**

The main objective of this study is to develop policy guidelines to assist local authorities to implement effective credit management.

### **1.4.2 Sub objectives**

The purpose of the sub-objectives is to investigate current credit management procedures implemented at local authorities in South Africa. This will be achieved by looking into:

- Minimalisation of the effect of non-payment on income sources
- Implementation of correct budget procedures.
- Determination of sound credit management principles.

## **1.5 Defining the field of study**

This study will cover the topics of credit management, budgetary procedures and cash flow. This will be applied to the credit management scenario in local government as experienced today.

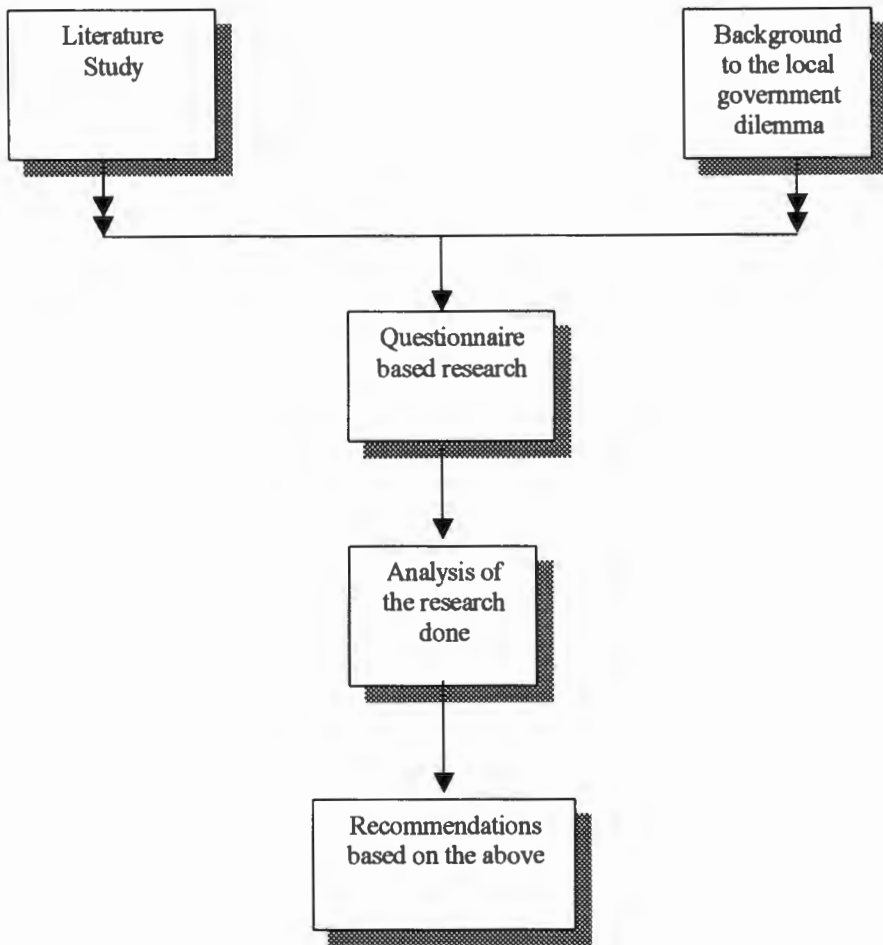
The measures available to local government to collect outstanding debtors are different from those applied in normal commercial practice. Local authorities have to supply services on credit to all customers without first testing their creditworthiness or ability to pay. The credit management function in local authorities could therefore not be directly compared to normal commercial practice.

## **1.6 Research methodology**

This academic study deals with the background of local government in South Africa and the dilemma local government finds itself in. Topics such as credit management, budgetary processes, and change management are covered. Against this background a questionnaire is used to determine what credit management measures local authorities are using. The questionnaire was sent out to a sample of medium to large local authorities throughout South Africa and was addressed to the Town Treasurers of those local authorities. The responses are statistically analysed.

The results from the statistical analysis were used to develop policy guidelines for credit management in local government.

**Figure 1.1 Research methodology – An illustration**



### **1.7 Limitations to the study**

This study will investigate and research the credit management practices applied at medium to large local authorities as they have some track record on limited to successful credit management. Smaller local authorities do not form part of the study although their need for credit management measures is sometimes greater than that of the larger local authorities.

## 1.8 Terminology

The following definitions and terminology are important for the study:

**Cash flow:** The movement of money into and out of a business, as a measure of profitability, or as affecting liquidity (Concise Oxford Dictionary, 1992:173).

**Credit management:** The ability of an organisation to limit and collect amounts owing.

**Electricity disconnection:** Includes one or all of the following:

- The tripping of the circuit breaker at the metering device.
- The disconnection of the supply from the metering device.
- The removal of the supply cable to the metering device or property.

**Indigent:** Household with a combined income of less than R 800-00 per month.

**Large local authorities:** Local authorities on grades 10 to 15.

**Local government:** A system of administration of county, district, parish, etc. by selected representatives who live there (Concise Oxford Dictionary, 1992:695).

**Medium local authorities:** Local authorities on grades 6 to 9.

**Small local authorities:** Local authorities on grades 0 to 5.

**Tampering:** The unlawful action of altering or meddling in the normal operations of a service supply infrastructure

**Water disconnection:** Includes one or all of the following:

- The limiting of the water supply to the property by inserting a flow control device such as a washer
- The closing off of the supply by means of a valve
- The removal of supply pipes to the property

## **1.9 Layout of the study**

The rest of the study is divided into the following parts:

- **CHAPTER 2: BACKGROUND TO THE DILEMMA OF LOCAL GOVERNMENT IN SOUTH AFRICA.**

This chapter deals with the background to the dilemma of non-payment for services in local government. Attention is given to the causes and effects of the current culture of non-payment.

- **CHAPTER 3: THE IMPORTANCE OF EFFECTIVE CREDIT MANAGEMENT.**

In this chapter a study which concentrates on credit management, sound budgetary procedures, and cash flow is done.

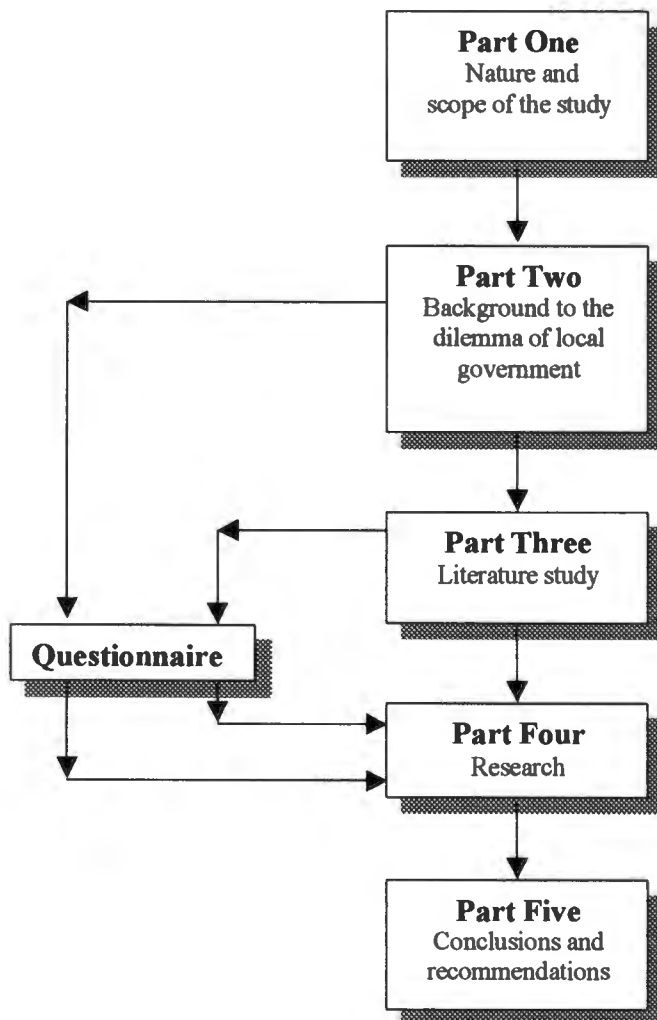
- **CHAPTER 4: COLLECTION AND ANALYSIS OF DATA.**

This chapter covers the research done, the questionnaire distributed to the target population, as well as a discussion on the information gathered by means of analyzing the questionnaires.

- **CHAPTER 5: CONCLUSIONS AND RECOMMENDATIONS.**

In this, the last chapter, the results obtained from the research is discussed as well as the conclusions that were arrived at. The greater part of the chapter is devoted to recommendations on a sound credit management policy and the implementation thereof.

**Figure 1.2 Layout of the study**



## **CHAPTER TWO**

### **BACKGROUND TO THE DILEMMA OF LOCAL GOVERNMENT IN SOUTH AFRICA.**

#### **2.1 Introduction**

This study investigates the development of a credit management policy specifically applicable in the sphere of local government. As some business principles in local government differ from those followed on the open market a background of local government is given.

#### **2.2. Background on Local Government**

Local government according to the Concise Oxford Dictionary is a system of administration of county, district or parish, by selected representatives who live there. These representatives are called councillors in South Africa and their duties, inter alia, entail the making of policy decisions which have to be executed by the officials employed at that local authority.

##### **2.2.1. Functions of Local Government**

In South Africa a number of functions have been delegated to local government by either Central or Provincial Government. These functions may vary between local authorities but the following major functions are found at most of the local authorities.

**Electricity distribution** – Electricity is purchased in bulk by the local authority and then distributed to each consumer connected to its distribution network whether industrial, commercial or residential. The provision and maintenance of the network is the responsibility of the local authority. Consumption is metered and the consumers must pay for their electricity consumption.

**Water distribution** – Potable water is purchased in bulk from a Regional Water Board and then distributed to the consumers. In some instances in South Africa water purification is done by the local authority itself. This, however, is not the norm but rather the exception. As with Electricity the provision and maintenance of the distribution network is the responsibility of the local authority. Consumption is metered and paid for by the consumers.

**Refuse removal** – Most local authorities operate their own refuse dumps. The operations at these dumps are, however, strictly controlled by Central Government because of the risk of polluting the natural water sources of the country as a whole. Refuse in residential areas is removed from each property on a regular basis. At commercial and industrial enterprises the same service takes place only in larger quantities and on a more regular basis. In South Africa recycling is still on a very low key and the operating of disposal sites is costly due to the high volumes of refuse. All users of this service must therefore contribute to cover the costs. The more refuse a person generates the larger his contribution to the cost will be.

**Sewerage and industrial outflow** – The provision and maintenance of the network together with the treatment of the outflow is covered under this function. All the raw sewage and industrial outflow needs to be treated in some way or another before it can be released into the environment. Here again strict regulations from Central Government are in place to ensure that pollution of the environment does not take place. Most local authorities operate their own treatment plants. Coastal local authorities on the other hand have in the past, and in some cases still do, pump their macerated outflow into the ocean.

The users of the waterborne sewer system must also contribute to cover the cost of the system.

**Roads and stormwater** – The internal road and stormwater infrastructure is the responsibility of the local authority. This includes the provision and maintenance of the infrastructure.

**Emergency services** – Fire fighting and fire prevention as well as rescue services and disaster management are done by the local authority.

**Health services** – This encompasses services such as municipal clinics, environmental health and pollution control within the boundaries of the local authority.

**Traffic control** – Traffic control within the municipal boundaries falls within the ambit of local government. The Provincial Government controls all other traffic. In some larger local authorities the function of policing has also been taken over by the local authority. This, however, is the exception rather than the rule.

**Public libraries** – Although this function is subsidized by the Provincial Government the bulk of the costs is carried by the local authority.

### **2.2.2 The Local Government viability dilemma**

The situation local government finds itself in could best be defined as a dilemma and not a problem. A problem is a situation, which needs to be changed, but a solution can be found. Even the most difficult problem can be solved. On the other hand the financial situation in which local government finds itself, as well as the ongoing non-payment of services, can best be described as a dilemma. It will not be solved, as it is an ongoing process. A solution to this scenario does not exist and could at best only be managed.

The emphasis in local government is on service delivery and not on profit making as in other enterprises. This does not take away the essentiality of normal economic principles such as payment for goods and services consumed.

The forced restructuring of local government, which took place in 1994, has a political/ideological as well as an economical foundation. The reasons are very intermeshed and no clear lines can be drawn. In the previous dispensation the Government of the day enforced the establishment of racially separate local authorities. With a few noticeable exceptions such as Soweto, the white local authorities maintained a high level of service in their so-called locations. This changed when the Administration Boards were made responsible for the administration and servicing of the black towns. The level of servicing was reduced considerably until the almost collapse thereof in the latter part of the 1980's and the early 1990's. To the uninitiated new politicians the response seemed to be to give the responsibility for the restoration and improvement of the services to the former white local authorities.

The area within which a local authority had to provide services was doubled or in some cases tripled. This meant that the expenditure on the provision of services increased above proportion with the extended area due to the dilapidated state of the infrastructure.

This vast increase in the expenditure of local authorities aggravated by the fact that most of these newly added local authorities have a culture of non-payment, has placed a severe strain on the finances of local authorities. Local government had to draw up long term capital programs to upgrade the services to an accepted but affordable level. By affordable is meant not only the initial capital outlay but also the capital costs of these projects, which is reflected in the tariffs. One of the problems that has arisen is that the economically active members of a community are not able to carry the additional cost of delivering services to that section of the community which cannot afford these services.

Due to the vast need for capital upgrading and maintenance of services everything cannot be done in one financial year. A long-term capital project plan must therefore be developed and implemented. Councillors do not accept the recommendations of officials regarding the maintenance of existing infrastructure but insist on the establishment of additional infrastructure. This policy aggravates the situation, as the chances to recoup the expenses by means of payment for services are relatively small.

The newly formed local authorities have the task of creating a culture of payment through stringent credit management as their livelihood depends on the income derived from the payment of services.

Not only was it made the responsibility of local government to upgrade the infrastructure but also to change the culture of non-payment into one of payment for services. This change to a culture of payment for services consumed is met with great resistance from the consumers. The new consumers demanded that their services first be upgraded before they start paying. Local authorities on the other hand demanded that the consumers must first pay their arrears before the services could be upgraded (Kapp. 1998:1).

To meet the demand for services both officials and the new councillors have to work together in this process of change to a culture of payment. The officials recommended credit management policies that were too harsh in the eyes of the politicians and a compromise had to be found and implemented. A further complicating factor was that the proposed policies had to be workshopped with the communities before they could be implemented.

This change from a culture of non-payment to a culture of payment for services is painful for the customers who were used to “free” services due to the fact that no action was taken against them in the past. This is especially true of a minority group who cannot afford to pay for services due to ongoing unemployment. The high degree of unemployment in this country has the effect that  $\pm 28\%$  of the households in the area of jurisdiction of a local authority can be classified as indigent.

To be classified as indigent the total household income may not exceed R 850-00 per month. Central Government expects local authorities to accept the social responsibility to provide services to these indigent people, a responsibility that local authorities cannot afford financially.

The non-payment of services has left local authorities with huge outstanding debtors. One hears and reads about these huge outstanding debts but the criticality of the situation really comes to the fore when reading the Project Viability Report of the Department of Constitutional Development. Project Viability was launched in 1995 with the objective of monitoring the short-term liquidity of municipalities, including payment levels, the position with regard to arrears and the effectiveness of the credit management (collection function). According to this report outstanding debt at local authorities has increased steadily over a period of time. **Table 2.1** reflects the outstanding debtors of the core group of municipalities and is given to illustrate the steady increase of outstanding debtors:

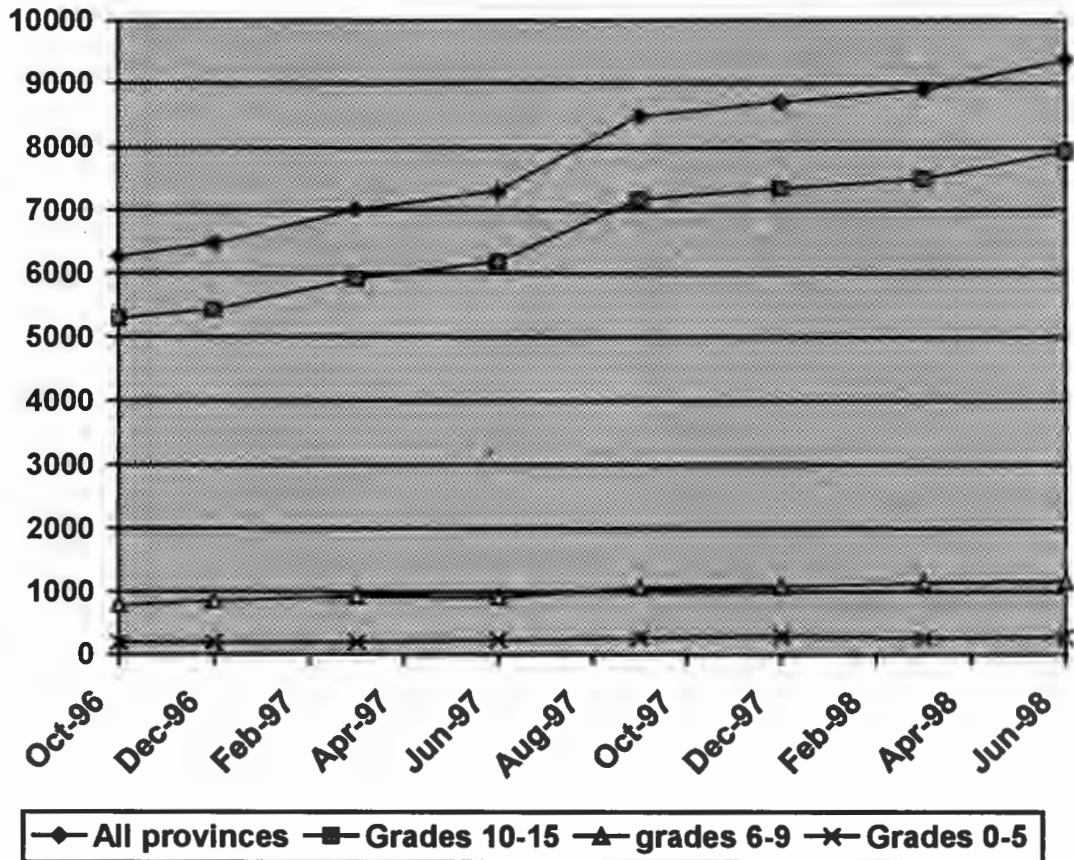
**Table 2.1 Outstanding debtors**

	<b>All provinces</b>	<b>Grades 10 – 15</b>	<b>Grades 6 – 9</b>	<b>Grades 0 – 5</b>
	<b>R</b>	<b>R</b>	<b>R</b>	<b>R</b>
<b>October 1996</b>	6,262,016,293	5,292,819,921	782,107,484	187,088,888
<b>December 1996</b>	6,468,189,630	5,430,689,132	847,159,222	190,341,276
<b>March 1997</b>	7,022,926,233	5,909,626,180	924,502,689	188,797,364
<b>June 1997</b>	7,302,584,607	6,176,627,949	904,655,635	221,301,023
<b>September 1997</b>	8,490,584,743	7,173,749,389	1,055,569,353	261,266,001
<b>December 1997</b>	8,713,089,066	7,348,475,896	1,081,434,806	283,178,364
<b>March 1998</b>	8,889,312,263	7,498,607,497	1,132,710,438	257,994,328
<b>June 1998</b>	9,360,264,568	7,926,659,531	1,155,006,289	278,598,748

Source: Project Viability Report. June 1998

The increase in outstanding debtors as depicted in the table above is more aptly depicted in graphical form. The rising trend can then more clearly be seen and analysed.

**Figure 2.2 Outstanding debtors**



Source: Project Viability Report. June 1998.

The steady increase in debtors reflects the inability of local authorities to deal with the level of non-payment. This is due to the number of accounts in arrears, insufficient contributions for bad debts or lack of credit management policies and support measures to assist indigents. It is also indicative of the measures available to local authorities to collect outstanding debtors in contrast to normal commercial practice, where local authorities supply services on credit to all customers without first testing their creditworthiness or ability to pay. The non-collection of outstanding accounts has serious

implications for a local authority's cash flow. Without money in the bank many local authorities are not able to pay their major creditors for bulk services. The number of local authorities who now have to operate on a bank overdraft has increased from 71 in October 1996 to 82 in June 1998. The aforementioned facts only serve to strengthen the necessity for stringent credit management in local government.

### **2.3 Summary**

The financial position in which many local authorities find themselves is indicative of their inability to implement effective credit management. The politicians and consumers demanding the upgrading of infrastructure before paying for services further complicate this dilemma.

# **CHAPTER THREE**

## **THE IMPORTANCE OF EFFECTIVE CREDIT MANAGEMENT**

### **3.1. Introduction**

In order to best understand the importance of credit management, this chapter will focus on a literature study surrounding the topics of credit management, sound budgetary procedures as well as the importance of cash flow. As far as possible the literature study will be made directly applicable to local government finance as some differences such as budgetary procedures exist.

### **3.2. Credit management**

#### **3.2.1 Defining credit management in Local Government context**

Credit management in local government differs slightly from credit management in commercial practice and for this reason it is necessary to define credit management in a local government context.

Credit management in local government is generally understood to be the functions related to the collection of cash from ratepayers, customers and consumers of the various municipal services. Credit management under this definition would start once an account remains unpaid after a specific due date. In terms of modern practices and approaches, credit management is more aptly defined as an avenue of last resort within the ambit of customer management.

The customer management approach focuses on the client's needs in a responsive and responsible manner, the objective being to encourage payment to prevent the need for enforcement (SA, 1997:4).

### **3.2.2. General principles of credit management**

#### **3.2.2.1. Lack of formalised policy**

Most companies in the private sector do not have a formalised credit management policy in place. This creates two major problems for the company. Firstly when a company's credit section does not have a clear sense of direction it will run into chaos. This not only creates the opportunity to commit fraud but also has a detrimental effect on the effectiveness of the credit section. Secondly when new staff is appointed to this credit section the same mistakes will be repeated (Basson, 1994:41).

This lack of formalised policy is not only found in private practice but also to a great extent in local government. Ramoo (1998:1) states that most rural local authorities do not have credit management and debt collection policies in place. Accordingly, it is imperative that local authorities formally approve, introduce and apply effective credit management and debt collection policies and procedures. Without these policies in place the normal debt collecting procedures will not be effective and outstanding debt will keep on rising.

With no policy in place a further problem in local government arises in that the public may not be treated in a fair and transparent manner. Due to the politicising of the credit management process this crucial factor plays a major role in the effectiveness of credit management in local government.

The abovementioned politicising of credit management as well as other local government functions has compelled Central Government to act. The Auditor General in a circular dated 08 March 1996 reminded local government councillors that they are personally and collectively responsible for the outcome of their decisions. Councillors are therefore subject to possible disallowance and surcharge action by the Secretary of the Department of Local Government and Housing, in circumstances where they have supported a resolution, which is questionable from a sound financial control or a legal point of view.

### **3.2.2.2. The need for a formalised credit management policy**

The growing debt to local authorities and the effect thereof on a local authority's financial viability has been in the national press on a regular basis. This not only affects the local authority but also the economy of the region due to the fact that the local authority cannot pay for goods and services needed to deliver a service.

The White Paper on Local Government (SA, 1998:117) states that it is vital to the long-term financial viability of any municipality that it collects the revenues due to it for services rendered. This means the appropriate credit management mechanisms must be established.

As a first step, municipalities need to be able to measure the volume of services that households consume. This means that metering of services such as water and electricity must take place efficiently. Secondly, households need to receive regular and accurate bills for the services they use, in a format, which is easy to understand. Thirdly, credit management measures will only be successful if targeted relief is available for those households who cannot afford to pay for services.

Fourthly, municipalities need to take strong measures to deal with those households who can afford to pay for services but are not doing so. This means that municipalities must keep proper record of outstanding debtors, and must take action against them after a given notice period. Such action can include the cutting of services or court action to recover debts.

It is clear that the constant increase in debtor amounts indicates a problem in the administration of local government. Credit management is one of the few areas of responsibility where local government, in general, is failing. Due to this the responsibility to improve the quality of life for the disadvantaged communities also cannot be fulfilled. The shortage of funds has the effect that new infrastructure cannot be put into place. In some of the disadvantaged communities there is a huge lack of service infrastructure. The enormous backlogs in service delivery require an approach in which payment for services is vigorously collected (Kapp, 1998:1).

Without cash in the bank it is not possible for a local authority to function effectively, if at all. It must therefore be stressed that income must first be collected to finance the expenditure, as it is the level of income that determines the level of expenditure. It follows therefore that income must be collected during the budget cycle of twelve months. As the collection of income is the responsibility of the chief executive officer it can be concluded that the determination and implementation of credit management measures is also the responsibility of the chief executive officer. He should however consult with his council regarding the measures to be applied (Kapp, 1998:8).

### **3.2.3. Commercial credit practice against Local Government practice**

In contrast to normal commercial practice, local authorities supply services on credit to consumers without first testing their creditworthiness (Kapp, 1998:11). This practice stems from the past when credit management was not as crucial due to the regular payments by consumers.

At present local authorities in South Africa hold the monopoly for the provision of services such as electricity, water, refuse and sewerage removal. This leaves the consumer no alternative but to purchase these essential services from the local authority (Kapp, 1998:13).

This situation however cuts both ways. The consumer must purchase services from the local authority. The local authority on the other hand must “sell” these essential services to the customer whether he or she has a bad credit rating or not.

In commercial practice the credit standing of a customer is determined before services are supplied. New customers complete a credit application form which requires details of trade references, bankers’ references and in the case of individuals, their current earnings. Based on this information and inquiries from trade referees the credit department establish credit limits for customers (Puttick & van Esch, 1998:239). This is however not the case in local government. The Constitution of South Africa gives all consumers the right to basic services.

Weak credit management practices frequently result in excessive bad debts and accounts receivable that may be uncollectable (Arens & Loebbecke, 1997:366). This problem has now taken on critical proportions in local government. Traditionally local government did not provide for bad debts, as the amounts written off annually were negligible. This has now changed and sufficient provision for bad debts must be made. For most companies the provision represents a residual, resulting from the management’s end of period adjustment of the allowance for uncorrectable accounts (Arens & Loebbecke, 1997:369).

### **3.2.4. Ineffectiveness of present credit management methods**

Over the past few years the old methods of credit management in local authorities have become outdated. The local authorities started to get resistance from the community on the high handed methods which were implemented such as disconnecting electricity without prior notice. The composition of the debtors also changed to the extent that approximately one quarter of the households could be classified as indigent.

The present methods of credit management followed by local authorities are ineffective for the following reasons:

- A local authority has no legal right to refuse service delivery, even if a credit assessment proves the customer cannot pay. The refusal to deliver services, such as the collection and disposal of solid waste or sewerage, would in any event give rise to serious health and environmental problems and would thus serve little purpose.
- The disconnection of water supplies poses health problems and raises political and constitutional questions regarding the right to basic services.
- The disconnection of electricity has up to now been the most successful method. Resistance is however developing against the disconnection of electricity to enforce recovery of charges in respect of other services as well. The proposal that has been suggested to divert the electricity industry from the local government sector would also nullify the effectiveness of this method.
- Legal action is lengthy and costly. The initial high cost of R200 to R300 per case does not justify legal steps unless outstanding accounts are substantial. Another aggravating factor is that there are usually a large number of accounts, which are lower than the initial cost of legal action. There is also little point in taking legal action against individuals who have little or no income or assets in the first place (Kapp, 1998: 14).

- Although the number of consumers disconnected has steadily increased over time, the vast difference between disconnection's and reconnections indicates that consumers are going without electricity or are reconnecting cut supplies themselves. In some parts of the country, illegal reconnections have become an industry and are reflective of the level of civil disobedience that municipalities need to deal with (Kapp, 1998:12).

It is due to the above inefficiencies that a need has arisen to investigate methods to counter the rise in outstanding debtors in a fair and transparent way.

### **3.2.5. Legislation**

Central government has recognised the dilemma local government finds itself in and is trying to intervene through legislation. In terms of Section 10 G (2) (a) (ii) of the Local Government Transition Act (Act No. 97 of 1996) the Chief Executive Officer was made responsible for the collection of income. This responsibility was further enhanced on the 14<sup>th</sup> of November 1997 when regulations were promulgated in terms of this Act (Notice No. R 1536 – Government Gazette No. 18435) requiring Chief Executive Officers to submit financial indicators to enable the councils to monitor the financial position of their local authority. In order to understand the extensiveness of the indicators that must be reported the following legislation is quoted:

*“Financial Indicators.*

4. *(1) The chief executive officer of every district council, local council, metropolitan council and metropolitan local council shall at intervals prescribed by sub-regulation (2), provide to his or her council a report containing the following financial indicators:*

- a) *A comprehensive analysis of debits with regard to rates, as well as water, electricity, refuse, gas and sewerage service debts which shall reflect the number of debtors and amounts outstanding of current debts outstanding for 30 days, 60 days, 90 days and more than 120 days*
- b) *The turnover rate of all-outstanding monthly recurring rates and services charges. The turnover shall be calculated by expressing unpaid rates and service charges as a percentage of budgeted rates and service charges income for the current financial year. The turnover rate shall be compared with a norm of 11,5% to 15%.*
- c) *The total number of rate payers and consumers liable for service charges and rate payers who did not receive an account during the period of review.*
- d) *In respect of the distribution of electricity, the number of disconnection's and reconnections after payment for the month concerned, as well as the number of consumers not connected, including those for previous periods.*
- e) *In respect of each separate service, or where a consolidated billing system is operated, the number of legal actions instituted in respect of a service or consolidated bill, as the case may be, as compared to the total number of accounts which are in arrears, including the number of summonses issued compared to the judgements obtained.*
- f) *A reconciliation of the cashbook with the bank statement, including an explanation of all reconciling items which have been outstanding for more than three months.*
- g) *The investment portfolio, including the type of investment, interest rates, period of investment and a summary of the exposures to particular financial institutions.*
- h) *The anticipated cash flow for the ensuing six months, which shall include plans to finance any shortfall.*
- i) *The turnover rate of the 20 highest value stock items accompanied by recommendations on how to improve the turnover rate of such stock items.*
- j) *All surpluses and shortfalls in stock levels as well as reasons for such surpluses and shortfalls.*

*k) An age analysis of the 20 highest value monthly paid creditors including the reasons for all amounts outstanding for more than 30 days.*

*3. (2) The reports referred to in sub-regulation (1) shall be submitted at the following intervals:*

*a) In respect of paragraphs (a), (b), (c) and (d), monthly but based on information not older than two months.*

*b) In respect of paragraphs (e), (g), (h) and (k), every three months.*

*c) In respect of paragraph (f), monthly.*

*d) In respect of paragraph (i), every six months.*

*e) In respect of paragraph (j), annually.*

*3. (3) Any report contemplated in sub-regulation (1) shall also be submitted to the MEC concerned within 14 days after submission of a report to the council concerned.*

*3. (4) The chief executive officer of a district council, local council, metropolitan council and metropolitan local council shall on such dates as determined by the minister submit to him or her or an institution or person designated by him or her, the MEC as well as to the municipal council concerned, within 21 days after the aforementioned dates, such information and in such form as may be determined by the Minister or MEC from time to time, and which is aimed at determining whether the finances of a municipality are or may be in the process of becoming unsound.”*

### **3.3 Cash flow**

Cash is the lifeblood of any organisation. Without cash any local authority and the services that it offers the people will grind to a standstill. Local authorities are at present experiencing cash flow difficulties due to the large amounts of money locked in outstanding debtors. Over the past few years the outstanding debtors increased at an alarming rate. The non-payment needs to be turned around and it must be done in the shortest possible time. The only method to reach this goal is to develop and implement fair but very strict credit management procedures.

At June 1998 the total cash and investment situation of the core group of municipalities amounted to R 6,906 billion. Although the cash and investments of municipalities have improved over the last two years, the figure also includes long-term borrowing not yet spent on capital projects. From a national perspective, the overall situation indicates insufficient cash and investments to cover the outstanding debtors, especially considering that the Durban Corporation holds R 3,5 billion of all cash and investments in local government (Kapp, 1998:14).

Cash flow can be seen as a measurement of liquidity. According to Kapp (1998:15) liquidity simply means the ability of a municipality to meet its debts as and when they fall due, i.e. it is the ability of a municipality to meet its short-term obligations. Failure to do this will result in the total failure of the municipality, as it will be forced into liquidation. While income is vital for the future health of a municipality access to cash or credit is often more important. It has happened that profitable companies have gone into liquidation because of a lack of cash.

### **3.4. Budgetary procedures**

#### **3.4.1. Defining a budget**

A budget is a detailed plan for the acquisition and use of financial and other resources over a specific time period. It represents a comprehensive expression of management's plans for the future and how these plans are to be accomplished (Garrison & Noreen, 1997:360).

#### **3.4.2. Budgetary process**

As with all commercial enterprises the compiling, approving and implementing of a budget in local government is important. However, certain local government budgets differ from the typical budget found in commerce. In local government the politicians who normally put a ceiling on the increase in tariffs determine the increases in income. The expenditure budget and capital budget are then drafted to fit in with the budgeted income.

Different companies follow different methods in the budgetary process. Zero-base budgeting is an alternative approach that has received considerable attention – particularly in the governmental and not-for-profit sectors of the economy. Under a zero-based budget managers are required to justify all budgeted expenditures, not just changes in the budget from the previous year. The baseline is zero rather than last year's budget (Garrison & Noreen, 1997:384).

### **3.4.3. Local Government budgets**

The aggregate size of the municipal budget in South Africa is substantial. In the 1996/97 financial year, municipalities budgeted for total expenditure of more than R 48 bn. This represents about 7,5% of South Africa's total gross domestic product, and is equivalent to 20,97% of the country's total public sector budget. Within this, municipal budgets vary enormously, from the metropolitan areas with budgets of several billions to small rural councils with negligible revenues (White Paper on Local Government, SA, 1998:109).

Trading services (electricity, water and sanitation) generate most local government revenue. In aggregate, revenue from trading services accounts for over 60% of local government revenue. Electricity for example constitutes the largest revenue source for many municipalities (White Paper on Local Government, SA, 1998:110).

An important fact is that the success of a budget is dependent on the collection of all budgeted income. Should actual income fall short of the budgeted figure, expenditure will have to be reduced which could mean curtailing services or in the long run lowering the standards of service (Kapp, 1998:12).

Very few municipalities will be able to access the capital market, due to lack of credit worthiness. It therefore appears that the capital development programs of municipalities are over-ambitious, unless debt collection improves dramatically. The only logical conclusion is that municipalities will continue to experience further cash flow difficulties, due to their ambitious capital budgets (Kapp, 1998:19).

All municipalities in South Africa use the accrual method to record income, but most fail to budget for the potential bad debt resulting from the non-payment of rates and service charges. Non-payment or bad debt requires a dedicated funding source. Municipalities have depleted their own funds to finance the current non-payment and are now depending on bank overdrafts to finance their working capital requirements.

The moment that the financial institutions refuse to extend short-term credit defaults on creditor payments become evident. The only short-term solution is to provide for a working capital provision and revert the operating budget to a cash basis. Long term solutions demand a strictly enforced credit management policy (Kapp, 1998:21).

#### **3.4.4. Other budget considerations**

It is also important to build the necessary capacity in the credit management section to enable this section to perform its duties at optimum effectiveness. For this staff and other resources is needed. Thompson & Strickland (1998:310) state that organisational units, especially those charged with performing strategy-critical activities, have to be staffed with enough of the right kinds of people. The sections must also be afforded enough operating funds to do their work proficiently, and have the funds to invest in needed operating systems, equipment and facilities.

In many local authorities not enough funding is channeled to the operating of an effective credit management section. Local authorities should provide ample on their operating budgets to support this function.

#### **3.5. Summary**

Credit management forms an integral part of local government in South Africa. There is however a lack of formalised policies in this regard. This creates problems in the effectiveness of the credit management section. Local government does not test the credit worthiness of its potential clients. Constitutionally a local authority must supply basic services to its inhabitants irrespective of the credit standing of the customer. This creates a high risk of bad debts.

Local authorities must make provision for these bad debts in their operating budgets. Provision must also be made to finance the credit management section to enable it to function effectively. The effectiveness of the credit management section has a huge impact on the cash flow of the local authority. This in turn effects the liquidity and ability of the local authority to perform its core function namely the provision of services.

## **CHAPTER FOUR**

### **THE COLLECTION AND ANALYSIS OF DATA**

#### **4.1. Introduction**

This chapter deals with the compilation of a questionnaire in order to obtain the necessary data for this study. The required data is aimed at the empirical research, which supports this study. The results obtained through the questionnaire as well as an analysis thereof are discussed in detail.

#### **4.2. Collection of data**

##### **4.2.1. Questionnaire design**

A short questionnaire was compiled to establish to what extent stringent credit management is applied at various local authorities in South Africa. The questions dealt with critical performance factors in local government credit management. Most of the answers to the questions can be answered as either “Yes” or “No”. The last question requests the respondent to forward a copy of his or her councils credit management policy. The copy of the policies will be used to aid in the drafting of a generic credit management policy model.

##### **4.2.2. The process of gathering data**

South Africa has 843 local authorities, which vary from the very small to the very large. As the greatest increase in outstanding debtors were evident in the small (48,91%) and large (49,76%) local authorities a more balanced result would be obtained by combining the worst sector (large local authorities) with the best sector (medium local authorities).

For this reason the questionnaire were sent to 34 randomly selected local authorities in the medium to large local authority group. Please see **Addendum A**, for a copy of the questionnaire as distributed.

### **4.3. Results and analysis**

The results obtained from the distributed questionnaire will now be discussed and analyzed. The discussions are aimed at identifying the key performance areas that should be included in a formalised credit management policy. They will also be used to assist in the compilation of a recommended policy for the use at local authorities.

#### **4.3.1. Feedback on questionnaires.**

A total of 34 questionnaires were distributed. Of this, 21 were received back which shows a 61,76% response.

**Table 4.1. Return results of questionnaire**

Total questionnaires distributed	34
Total replies received	21
Total not replied	13
Response percentage	61.76%

#### **4.3.2. Processing of questionnaires**

The departure point of the analysis is to identify the critical performance areas that should be included in a realistic and workable credit management policy for local government.

The various questions with their subsections will be discussed in chronological order.

In order to evaluate the respective responses to the questions and the compliance of local authorities to the critical performance areas the percentage of compliance will be calculated in each case.

#### **4.4. Results and discussion of questions**

In order to analyse the questions meaningfully the questions will be discussed in terms of the following:

- **Introduction** – This will expand on the motivation why the information rendered by the response is important.
- **Results obtained** – The results obtained in Table format.
- **Conclusion** – The conclusion arrived at, by interpreting the obtained information. Information gathered from the respondents' credit management policies will be incorporated in the conclusion. Broad recommendations will also be discussed.

##### **4.4.1. Section 1 General information**

The purpose of this section is to gather general information on the respondents as well as to ensure that the target group falls within the ambit of medium to large local authorities. Each question will not be analysed individually but the section will rather be discussed as a whole. **Table 4.2.** is a summary of the responses received from the local authorities and it is clear that large amounts is owed to local government. These outstanding amounts must be brought under control through strict credit management.

**Table 4.2. Outstanding debtors 1999**

Number of local authorities	21
Total outstanding debt	1 064 000 000

#### **4.4.2. Section 2 Budgetary procedures**

The general purpose of this section is to determine the budgetary procedures implemented by participating local authorities. Specific attention is given to procedures relating to credit management and provision for bad debts.

##### **4.4.2.1. Provision for bad debts**

As with the private sector local government is now compelled to provide for bad debts. Bad debts in the local government scenario mainly consists of debts accrued from services rendered. Property rates are in all cases recoverable through the selling of properties. The purpose of this series of questions was to determine how local authorities provide for the writing off of bad debts through the budgetary process. Also included in this section are questions to determine how the provision is utilised by local government. The results from the questionnaire are shown in **Table 4.3.**

**Table 4.3. Bad debt provision**

Number of respondents	21
Provision out of surpluses	4
Provision out of income	16
No provision	1
Utilisation – Write off's	21
- Other	0

80% of the responding local authorities have indicated that they prefer to make contributions to the reserve fund out of income. Only one local authority indicated that they do not have a bad debt reserve fund.

It is also clear from the results that bad debt reserves are only used for the writing off of bad debts. It could however be reasoned that where the reserve have reached acceptable levels a portion of the available funds could be utilised to prevent bad debts. One such intervention is to install pre-payment meters at the properties, which are in arrears.

#### **4.4.2.2. Budgeting for income**

A new direction of thought has developed in local government on the budgetary procedures to be followed when budgeting for service income. This entails that due to the non-realisation of income, service income should be budgeted on a cash realised basis. The purpose of this sub-section is to determine what method is currently utilised by local government in their budgetary process.

**Table 4.4. Budgetary procedures**

Number of respondents	21
Income on cash realised basis	0
Income on potential income basis	21

As can be seen from the results all participating local authorities prefer to budget for potential income (accrual basis). This method is generally accepted in local government as an alternative to the cash realised basis of income budgeting.

### 4.4.3. Section 3 Changing the culture of payment

Although the change process is more of a political and training issue the effects thereof has a direct impact on the finances of a local authority. The importance of change can not be ignored, as the flow of information from the administration of the local authority to the residents is a key element in the credit management process.

#### 4.4.3.1. Support from councillors

The importance of political power in the process to change the mindset of the people from a culture of non-payment to that of full payment for services should not be under-estimated. It is therefore necessary to determine the extent of support given by the councilors on the issue of credit management.

**Table 4.5. Political support**

Number of respondents	21
Council's in support	21

From the results it seems as if councilors in general supports credit management. The result can be somewhat misleading in that the level of credit management that they support is not known. A very strict credit management policy which includes disconnection of water and sales in execution is not always readily accepted by councilors as it raises political and constitutional questions regarding the right to basic services (Kapp, 1998:4).

#### 4.4.3.2. Transparency and the flow of information

Another important leg of effective credit management is that the customers must be informed of the consequences of non-payment. This question has the aim to

determine the methods followed by the individual local authorities in informing the consumers about the credit management policy.

**Table 4.6. Information flow to consumers**

Number of respondents	21
Public meetings	21

As can be seen from the above all local authorities chose the public meeting avenue to inform the consumers on the credit management policy and the effect thereof. It can therefore be deduced that public meetings are the single most generally used method in getting the support of the people on the ground.

#### **4.4.3.3.Reasons for non-payment**

At the beginning of the payment boycott the reasons for non-payment was purely political. The emphasis later shifted to the delivery of services. The consumers in the black towns demanded the same levels of services as are prevailing in the white towns. Vast improvements in the infrastructure have taken place over the past few years. It is therefore important to determine the latest reasons for non-payment.

**Table 4.7. Reasons for non-payment**

Number of respondents	21
Unemployment	21

It is clear that an emphasis shift has again taken place. Unemployment is now given as the main reason for not paying municipal services.

#### **4.4.4. Section 4 Minimalisation of non-payment effect on income**

The Minimalisation of the effect of non-payment on the income of the local authority forms an integral part of the credit management policy. The purpose of this section is to determine what methods local authorities use to reach this goal.

##### **4.4.4.1. Pre-payment metering**

One of the most effective inventions to minimize the effect of non-payment on the income of a local authority is to install pre-payment meters at all consumers. The purpose of the question is to determine to what extent local authorities are using this intervention.

**Table 4.8. Pre-payment metering**

Number of respondents	21
LA's with pre-payment meters installed	19
Type of service - Electricity	19
- Water	0
Average level of installed meters (Q4.3)	38.0%

As can be seen from the results most of the local authorities have recognised the effectiveness of pre-payment meters in the process of minimizing the affect of non-payment. The sample shows that only 38% of conventional meters have been converted into pre-payment meters.

#### **4.4.5. Section 5 Credit management policies in operation**

The importance of a formalised credit management policy has been stressed throughout this document. To enable the writer to draft a generic policy it is deemed important to determine which aspects of credit management other local authorities have included in

their policies. By merging these policies a comprehensive policy is compiled that can be used as a model by other local authorities.

#### 4.4.5.1. Does your council have a formalised credit management policy?

The crucial importance of having a formalised credit management policy in local government lies in:

- The fair and transparent treatment of its customers.
- The staff will know exactly what steps to follow thus eliminating the possibilities of fraudulent transactions.
- A well-structured policy will prevent chaos and ensure that monies due to the local authority are collected.

The question is asked to determine to what extent local authorities follow the trend of private companies, which has an evident lack of formalised credit management policies.

**Table 4.9. Formalised credit management policy**

Total respondents	21
Local authorities with a formal policy	19
Local authorities without a formal policy	2
Compliance to formal policy	90,48%

Local government in general does not follow the private sector trend as far as formalised credit management policies are concerned. The results show that most local authorities have some sort of formalised policy in place.

**4.4.5.2. Does the formalised credit management policy specifically deal with:**

**Deposits**

*Paying the raised amount in installments*

The central government expects local authorities to fulfill their social responsibilities in respect of the poor. Attention must therefore be given to the plight of the economically disadvantaged when deposits are raised. A mechanism should be in place to enable these people to pay their deposit in installments. The purpose of the question is to determine how many local authorities comply with this requirement.

**Table 4.10. Payment of deposits in installments**

Number of respondents	21
Number with facility	1
Number not addressing the subject	20
Compliance	4,76%

Only one local authority has given attention to this matter in a formalised manner. No credit management policy is complete without some form of relief for the poor. A comprehensive policy should therefore include a mechanism to pay the required deposit in installments. A written agreement stating the due dates and monthly payments should be put in place before a prospective consumer is allowed to pay the deposit in installments.

*Determination of the deposit amount*

In local government the norm on the level of consumer deposits is 2,5 times the average monthly account. In many cases this resulted in small amounts being outstanding after utilizing deposits to cover the final account. In most of the cases

these amounts are too small to economically institute recovering procedures and the amount is then written off as irrecoverable debt.

The determination method of the consumer deposit level should be spelled out clearly. The question has been asked to determine the number of local authorities who have this intervention in place.

**Table 4.11. Determination of the deposit amount**

Number of respondents	21
Included in policy	8
Not included in policy	13
Compliance	38.10%

Less than half of the respondents have included the determination of consumer deposit levels in their credit management policies. The consumer deposit level forms an integral part of credit management and should form part of the formalised policy.

### **The non-payment for services**

#### ***Blocking/disconnection of electricity supply***

It should be clear from the policy whether or not the councillors of a particular local authority support the disconnection/blocking of electricity in the case of non-payment. Disconnection is used in the case of conventional electricity meters to prevent further consumption. In the case of pre-payment meters, blocking entails the refusal to sell further electricity to the consumer. This method is one of the most effective credit management tools available to local government. It is of great importance to determine to what extent this tool is utilised by local authorities.

**Table 4.12. Blocking/disconnection of electricity supplies**

Number of respondents	21
Blocking/disconnection of electricity	21
Compliance	100%

From the results can be seen that all the responding local authorities are implementing this credit management tool. One could therefore assume that all local authorities in South Africa are following this method of debt recovery to some extent.

***Blocking/disconnection of water supply***

The disconnection/blocking of water supplies for the non-payment of services is a very sensitive issue. Water is deemed as a basic service to which all consumers have a right. This method is seen as one of the most extreme measures and is not implemented as a first recourse. It is however important to determine how many local authorities have made provision in their credit management policies for this measure.

**Table 4.13. Blocking/disconnection of water services**

Number of respondents	21
Blocking/disconnection of water services	21
Compliance	100%

As can be seen from the results it is important to have a water disconnection/blocking policy included in a local authority's credit management policy. The implementation thereof must, however, be done with great caution and empathy. The water issue has been politicized to such an extent that any disconnection of water supply is bound to create a feeling of unhappiness in council.

Information was also gathered on the number of days before an arrears consumer's supply is disconnected. The variance in days can be ascribed to local conditions and no fixed period can be recommended that will suit all local authorities. The parameter should however be included in the credit management policy as an aid to the staff and for information purposes to the consumers.

***Payment of reconnection fee***

The disconnection and reconnection of service supplies have direct cost implications to a local authority. Municipal staff with the necessary transport must perform the actual disconnection and reconnection off the meters at each property. These costs should be recouped from the consumer in arrears. As this action has a direct relation with credit management it is important to have the determination of the said fee included in the policy. This section aims to determine how many local authorities include the payment of a reconnection fee in their credit management policy.

**Table 4.14. Payment of reconnection fee**

Number of respondents	21
Number included	15
Number excluded	6
Compliance	71,43%

Many local authorities have included the payment of a reconnection fee in their credit management policies. This again shows the relevance of such a fee in credit management. The necessity to have this fee included in the policy comes from the need to be transparent. With the determination of the reconnection fee and in what instances it becomes applicable written into the policy, it will be clear for the staff and public alike when the fee is payable.

### ***Determination of reconnection fee***

To reconnect the supply of a consumer's service after being disconnected has definite cost implications to a local authority. Experience has shown that every local authority charges different reconnection fees. It is therefore important to determine on what basis these fees are calculated.

**Table 4.15. Determination of reconnection fee**

Number of respondents	21
Cost recovery	21
Other methods	0
Compliance	100%

All participating local authorities indicated that they use cost recovery as basis for determination of the reconnection fee. Local circumstances such as salaries, transport costs, material and equipment costs however play a role in the actual level of the fee. The aim is to recover the full cost of both the disconnection and the reconnection from the consumer.

### ***Property rates in arrears***

Property rates' outstanding forms a large part of the outstanding debtors' amount at local authorities. The recovery thereof is more secure than that of services in that no transfer of ownership can take place before the local authority has not certified that all municipal taxes have been paid. This however does not take away the need to collect all the income as it becomes due.

The participating local authorities were questioned on what steps they take when acting against property rates defaulters. All of the respondents indicated that they follow the route of legal action. Should the owner not respond with payment the property is then sold in execution and outstanding property taxes recovered.

This seems to be an effective method to collect outstanding property rates although the legal process is somewhat lengthy.

### **Tampering with supply**

The tampering with service supplies has become a stark reality that local government in South Africa has to manage. This phenomenon of tampering is most prevalent with residential consumers whether metered by conventional or pre-payment meters. The services then enjoyed by the consumer are not measured and form part of the high distribution losses that local authorities must carry.

### ***Blocking/disconnection of electricity supply***

Over the past few years a pattern has developed that where strict credit management is enforced the tampering rate is higher. All local authorities must put into place policies to deal with these tamperers in a harsh manner as millions of rands worth of electricity is lost to the South African economy through tampering. The purpose of this question was to determine the number of local authorities who included measures to deal with tampering of electricity into their credit management policy.

**Table 4.16. Blocking/disconnecting due to tampering**

Number of respondents	21
Number included	13
Number excluded	8
Compliance	61,90%

A fairly large group of the responding local authorities indicated that punitive measures for tampering by the consumers with the electricity supply are included

in their credit management policies. Due to the direct relationship between credit management and tampering it is important that measures to counteract tampering be included in the documented credit management policy.

***Blocking/disconnection of water supply***

Tampering with the water supply is more difficult to detect due to the fact that most water meters are still of the conventional kind. Less management information is available than in the case of electricity. It is a drastic measure to disconnect/block a consumer’s water supply and it must therefore be implemented with caution. The purpose of the question is to determine how many local authorities have included this sensitive issue in their credit management policies.

**Table 4.17. Blocking/disconnection of water due to tampering**

Number of respondents	21
Measure included in policy	8
Measure not included in policy	13
Compliance	38,10%

The low compliance to having punitive measures for the tampering stems from the politicising of basic services such as water. Very few councils are willing to implement such drastic measures for fear of the reaction of their constituencies. This matter must be addressed in the credit management policy to ensure that, should the need arise, this tool is then available to the officials of a local authority to implement.

***Payment of tampering fee***

Tampering with municipal services with the sole idea of consuming those services without paying therefore must be stopped. Checks and balances must be

instituted on services sold and paid for, and audit systems and processes put in place for metering and billing (Campbell, 1999:5). To audit and replace the suspected tampered meters has a cost implication to council. The purpose of the question is to determine how many local authorities recover the costs from the guilty parties.

**Table 4.18. Payment of tampering fee**

Number of respondents	21
Number included	8
Number excluded	13
Compliance	38.10%

The compliance to the question of a payment of tampering fee is again very low. It might be that local authorities in general do not see this as part of credit management. However it is linked to tampering with service supplies which has a direct relationship to the effectiveness of credit management. The auditing and replacement cost of suspect meters must be recovered from the consumer. The consumer on the other hand needs to know what steps will be taken against him should he tamper with the municipal service supply. It is for this reason that the rules and regulations on the payment of a tampering fee should be included in the credit management policy.

***Determination of tampering fee***

Tampering with supplies is escalating at a tremendous rate. The first action to take when a tampered meter is found is to disconnect the supply. The nature of the disconnection differs from a normal non-payment disconnection in the sense that it must be made more difficult for the consumer to re-instate his service. The purpose of this question is to determine whether or not local authorities use this fee as a punitive fee or as a cost recovery fee.

**Table 4.19. Tampering fee**

Number of respondents	21
Cost recovery	21
Punitive measure	0
Compliance	100%

All of the respondents indicated that tampering fees are based on cost recovery. A penalty should only be levied in cases where the consumer has been found guilty by a court of law on tampering with the supply. This is very difficult to prove as the customer alleges that he knows nothing about the tamper. The local authority can however justify a tampering fee based on actual costs to restore the legal supply of service.

#### **4.4.5.3. External collections**

##### **Does your council's credit management policy deal with account handovers to external debt collection agencies and attorneys**

The handing over of outstanding debtors to debt collecting agencies or attorneys forms an integral part of any credit management policy. This step is normally followed if the local authority does not have the in-house capacity or all other avenues have failed. The mechanics of how these debtors will be handled should also be spelled out in the credit management policy. The reason behind this is that the debtor has the right to know what actions will be taken against him should he not pay his municipal account. The purpose of the question is therefore to determine how many local authorities have these actions included in their policy.

**Table 4.20. Handovers to external parties**

Number of respondents	21
Included in policy	13
Excluded from policy	8
Compliance	61,90%

More than half of the responding local authorities have included the manner in which outstanding debtors will be handled by external parties in their credit management policies. The exclusion of this section could lead to claims of discrimination against certain categories of debtors. The inclusion will also form a guideline to the staff of the credit management section as to what actions should be taken.

#### **4.4.5.4. Payment agreements**

**Does your council's credit management policy include the entering into payment agreements with arrears debtors**

The current economic downswing and the resultant high level of unemployment are factors that need to be acknowledged in a credit management policy. Government and councillors from local authorities are calling for indigent policies to help the poor. Methods must be developed to ease the plight of the poor. It is for this reason that debtors should be granted the opportunity to pay their arrears amounts in installments. The purpose of the question was to determine how many local authorities have included such a section in their credit management policies.

**Table 4.21. Payment agreements**

Number of respondents	21
Agreements included	18
Agreements excluded	3
Compliance	85,71%

As can be seen from the results most of the local authorities have already recognised this need and have included this section in their credit management policies. The agreements made with the debtors should however be formal and in writing. The exact amounts and due dates must be clearly stipulated in the written agreement. The follow up actions, should the agreement be dishonored, must also be stipulated in the agreement, not only as a warning to the debtor but also as a guideline for the staff members in the credit management section.

The detail on agreements in place at the participating local authorities has been made available through the submission of their credit management policies. The terms of the agreements should also be incorporated into the formalised credit management policy.

#### **4.4.5.5. Relief for the indigent**

##### **Does your council's credit management policy include some form of relief for the indigent**

As with the previous question the need for relief to the poor is emphasized. Other relief such as the writing off of old debt, a moratorium on the raising of interest on outstanding amounts as well as in some cases the paying of a subsidy to the poor is possible. This ties in with the credit management policy as it too affects the total outstanding amount that needs to be collected. The purpose of the question was to determine how many local authorities have such additional measures of relief for the indigent included in their credit management policies.

**Table 4.22. Relief measures**

Number of respondents	21
Additional measures included	9
No additional measures	12
Compliance	42.86%

On this issue a fairly low compliance was obtained. show a disregard for the Relief measures for the poor have a cost implication to the local authority concerned. These costs must be borne by somebody, usually those ratepayers in the community that can afford to pay for their municipal services. Local government cannot, however, tax these consumers too heavily as they soon will then also form part of the group that cannot afford to pay for services. Additional relief must therefore only be implemented to the extent that the local authority can afford it.

#### **Subsidization of indigent accounts**

Relief measures such as lifeline tariffs was implemented in the past with great success. With the high unemployment rate it has become more and more prudent for local government to provide additional means to fulfill its social responsibility. One of these issues is the subsidization of the accounts of the indigent. The purpose of these questions is to determine how many local authorities subsidise the indigent directly and from what source.

**Table 4.23. Subsidisation of the indigent**

Number of respondents	21
Local authorities subsidizing	14
Local Authorities not Subsidizing	7
Source of finance: Governmental transfers	11
: Income	3
Percentage subsidizing the indigent	66.67%

The results show that a large number of local authorities have heeded the call from central government to subsidise the indigent. The main sources of finance for these subsidies emanate from inter governmental transfers.

**4.4.5.6. Does your council list payment defaulters at the ITC (Information Trust Corporation)**

As with private commerce it has become necessary to identify those customers that have a tendency not to pay their accounts. The most successful method is to list payment defaulters with the ITC. The effect is that when the same customer tries to buy on credit the company can assess the risk by accessing the ITC database. The company will then know that the potential customer is a bad credit risk and can either demand a higher deposit or refuse the credit application all together. This method is, however, new to local government and it is important to determine how many local authorities have ITC listings as part of their credit management policy.

**Table 4.24. Information trust listing**

Number of respondents	21
Positive response	7
Negative response	14
Compliance	33.33%

The importance of an ITC listing as a credit management tool must not be underestimated. Only a few local authorities have this tool included in their policies. An ITC listing can also be used with good results when dealing with the indigent. The fear of being listed eliminates to a great extent those who are trying to defraud the local authority by creating the perception that they are indigent. Unnecessary costs can be avoided if only the true indigent can be identified.

#### **4.4.5.7. Request for copy of the local authority's credit management policy.**

The goal behind this request was to collect as many as possible credit management policies from different areas in South Africa. These policies would indicate to a great extent which sections of such a policy are common to all local authorities. A further advantage is the sifting through the proper wording for such a policy to enable the effective functioning of the credit management section. The main aim is to make the wording applicable to most local authorities. The wording might then be slightly adapted by the councils to suit local conditions.

#### **4.5. Summary**

This concludes the analysis of the responses received from the questionnaire. Final conclusions as well as a recommended credit management policy are dealt with in the next chapter.

# **CHAPTER FIVE**

## **CONCLUSIONS AND RECOMMENDATIONS**

### **5.1 Introduction**

There is a great need for a formalised credit management policy for local government in South Africa (Ramoo, 1998:1). A number of local authorities do not have such a formalised policy due to lack of capacity or pure ignorance of the importance thereof. In formulating the recommendations for a generic credit management policy the following work method will be followed:

- Conclusions arrived at through scrutiny of the responses to the questionnaire and the submitted policies.
- A schematic view of the credit management process will be developed.
- Recommendations for a generic credit management policy composed from a combination of theoretical principles, responses to the questionnaire, and the individual policies received.
- Where conclusions and recommendation cannot be directly related to the theory or questionnaire it was made from the credit management policies received from the participating local authorities.

### **5.2. Conclusions**

From the policies implemented by the participating local authorities as well as the responses to the questionnaires the following conclusions could be made.

#### **5.2.1. The importance of a formalised credit management policy**

Basson (1994:41) stated that if a company's credit management section does not have a clear sense of direction it will run into chaos. This also applies to credit

management in local government. Without a formal policy in place the actions of the staff will not be consistent thus compromising transparency. It is of the utmost importance in the present day South Africa that the staff at a local authority acts in a transparent manner. The people on the ground must at all times have the perception that they are treated fairly.

All actions performed by local authorities have become politicised and it is for this reason that it is prudent that the politicians take ownership of the credit management policy. The politicians must advocate the policy and its purpose to all the inhabitants of the town. For the politicians it is important that the policy is formalised to enable them to explain and defend.

#### **5.2.2. Correct levels of deposits**

The outstanding debt after the deposit has been utilised to defer the outstanding balance has become a real problem for local government. These amounts are normally too small to economically recover through the legal process. These amounts then have to be written off against income as irrecoverable debts. To counter this trend the current deposit levels needs to be raised. At present the level is set at 2,5 times the average monthly account. This deposit level should be raised to ensure that no small amounts are left when an account is closed.

#### **5.2.3. The Blocking/disconnecting of services**

Services to consumers, who falls into arrears, on any of the services provided by the local authority, should be disconnected on a monthly basis. The two main services to disconnect are electricity and water. The electricity supply should be disconnected as a first measure and should no payment be forthcoming the water

supply should also be disconnected. The disconnection/blocking of services could take on many forms such as:

- **Physical and total disconnection of the supply.**  
This option is applicable to all so called “conventionally” metered installations and includes water and electricity supplies.
- **Blocking or refusal to sell services.**  
This option is only applicable to installations with pre-payment meters and may include water and/or electricity.
- **Limiting of supply.**  
Only applicable to the supply of water to the consumer and entails the placing of a restrictive device on the supply to the consumer. Only a predetermined quantity of water will then be available to the consumer over a given period of time.

The disconnecting/blocking of the supply should be uniformly applied to all consumers who fall into arrears. Reconnection or unblocking should not take place unless the outstanding amount has been paid in full or suitable payment arrangements have been made. The disconnections must be followed up on a regular basis to ensure that consumers do not illegally reconnect themselves to the supply.

In the event of a cheque returned from the bank and the said cheque was offered previously to the local authority in payment for services, the consumer whose cheque it is must be dealt with in the same manner as consumers not paying their account on or before the due date. The consumer must furthermore be placed on an internal black list and all payments further offered by the consumer should be in cash.

A reconnection fee should also be charged as costs are incurred each time a supply has to be disconnected and/or reconnected. The reconnection charge should be based on the average actual costs incurred. An unblocking fee on pre-payment meters should also be charged as staff time is also taken up in the process. This fee should be based on actual costs. The main purpose of these fees should be cost recovery and not as a penalty to the consumer.

#### **5.2.4. Tampering with supply**

As the local authority clamps down on the non-payment by consumers through disconnections and blocking of the supply, tampering increases. Although tampering is a criminal offence it is difficult to get a conviction if the tamperers are not caught red handed. The level of tampering going on could easily be measured by the huge distribution losses experienced in certain areas. As tampering takes on many forms and new methods are invented every day it is of great importance that a local authority sets aside sufficient funds to perform audits on all its installations.

The local authority should take all possible steps to prevent tampering and one of the most efficient methods is to disconnect the supply in such a manner that further tampering is made very difficult. This in most cases entails the removal of the supply cable. Although the most frequent form, tampering is not exclusively an electrical problem but to a lesser extent also entails tampering with the water supply. External contractors specializing in auditing meters for tampering are available at reasonable cost.

On a more technical point, a local authority's tampering policy should not refer to the tampering with meters but rather to the tampering with the supply. This term will then include the cables/pipes bringing the supply to the consumer as well as the metering device placed on the supply.

A specific policy must be put into place on how tampered installations will be dealt with such as disconnection, payment of all outstanding amounts, payment of a tampering fee and steps that will be taken should a second or third tampering offence take place. The tampering fee must not be seen as a penalty but as a cost recovering method. In the case of tampering no privileges such as the facility to arrange payment of the outstanding amount on an installment basis should be granted. The consumer has committed or allowed a criminal act to be committed, thereby defrauding the local authority of income and must be dealt with severely.

#### **5.2.5. Account handovers**

As with the previous instances a local authority must have a written policy which deals with the steps to be taken when internal actions fail. This is not only necessary from the staff's point of view but also from a consumer's point of view. The consumer has the right to know what steps will follow after he did not react to the internal actions of the local authority.

After disconnection/blocking a consumer's supply due to non-payment a final demand should be issued to the consumer when the account reaches a stage of being overdue for more than 30 days. The final demand must specify the time frame within which the consumer must pay to avoid legal action. The cost of issuing the final demand should be debited against the total outstanding account of the customer. Again this is not a penalty charge but rather a method of recovering costs incurred by the local authority in an effort to collect the monies due to it.

When an account becomes overdue for more than 60 days the account must be handed over to the local authority's attorneys for collection. The local authority's attorneys should immediately proceed with the issuing of summonses, in view of the previous final demand sent to the consumer by the local authority. The messenger of the court serves the summonses. The consumer in arrears should

then be given a very limited time from date of serving of the summons to responding with payment. Failing this, the attorneys must proceed to seek judgement and a warrant of sale in execution.

If judgement has been taken, the debtor will appear on the ITC listing, stating the judgements, which have been taken. This listing will have a negative reflection if the consumer tries to apply for credit in the future. All costs incurred in this process must be recovered from the debtor. The warrant of execution will be served by the messenger of the court, and after attachment; the attorneys will apply for a date of sale. Moveable assets should be attached first and thereafter the fixed assets of the debtor. The sale must be advertised in a local newspaper.

In some cases it will be more effective to obtain an emoluments attachment order to enable the employer to deduct a monthly amount from the debtor's salary for payment to the local authority. This is the preferred method but can only be effected where the debtor is gainfully employed.

A balance must however be struck between spending money in order to collect outstanding amounts and the inevitable conclusion that nothing further can be done to collect a debt. The debt and the collection costs must then be written off. It is in those cases where debtors are completely untraceable, where they have no assets or jobs and where they go insolvent or into liquidation that the local authority is forced to write off debts. The leveling out of the economy and the fact that often people are losing their jobs without alternative employment only worsens the position.

#### **5.2.6. Relief for the indigent**

Great emphasis is placed by the central government that local government must act socially responsible by having interventions in place to help the poor. Local

government cannot afford to subsidise the poor but other relief measures can be put into place. One such measure is to enable the debtors to pay their deposits in installments. This measure should also be extended to those debtors who have fallen into arrears.

The relief measures should however be properly documented to enable the staff to make arrangements within specified parameters. The debtor making use of these arrangements must enter into a written agreement with the local authority to ensure that no misunderstanding could develop in future.

Each case will have to be adjudicated on its own merits but a formal policy will make it clear to both the staff and the consumer within what parameters arrangements could be made. The agreement must be in writing and the consumer must sign consent to judgement at the time of making the arrangements on arrears accounts. This is done to ensure that with default of the arranged payment, sale in execution can be effected immediately.

Steps to be taken should the arrangement not be honored should also be documented. This is not only done to ensure that the staff of the local authority knows what actions to take, but also to ensure that the debtor knows what actions will follow. The policy should also be implemented consistently to all debtors and no leniency other than that permitted in the policy should be shown.

The relief measures as set out in the recommendations should only in extreme instances be implemented in cases where tampering took place. Tampering is a criminal offence and the perpetrators should be dealt harshly. The relief measures is meant for those cases of real hardship where the consumer wants to pay but cannot afford to pay the outstanding amount in one amount.

### **5.2.7. Budgetary procedures**

From the results received from the participating local authorities it is clear that all local authorities still budget on a potential income basis. This method has been in use for a number of years and up and until the sudden growth in outstanding debtors was an acceptable method of budgeting. This method now has to be amended to provide for the non-realisation of cash.

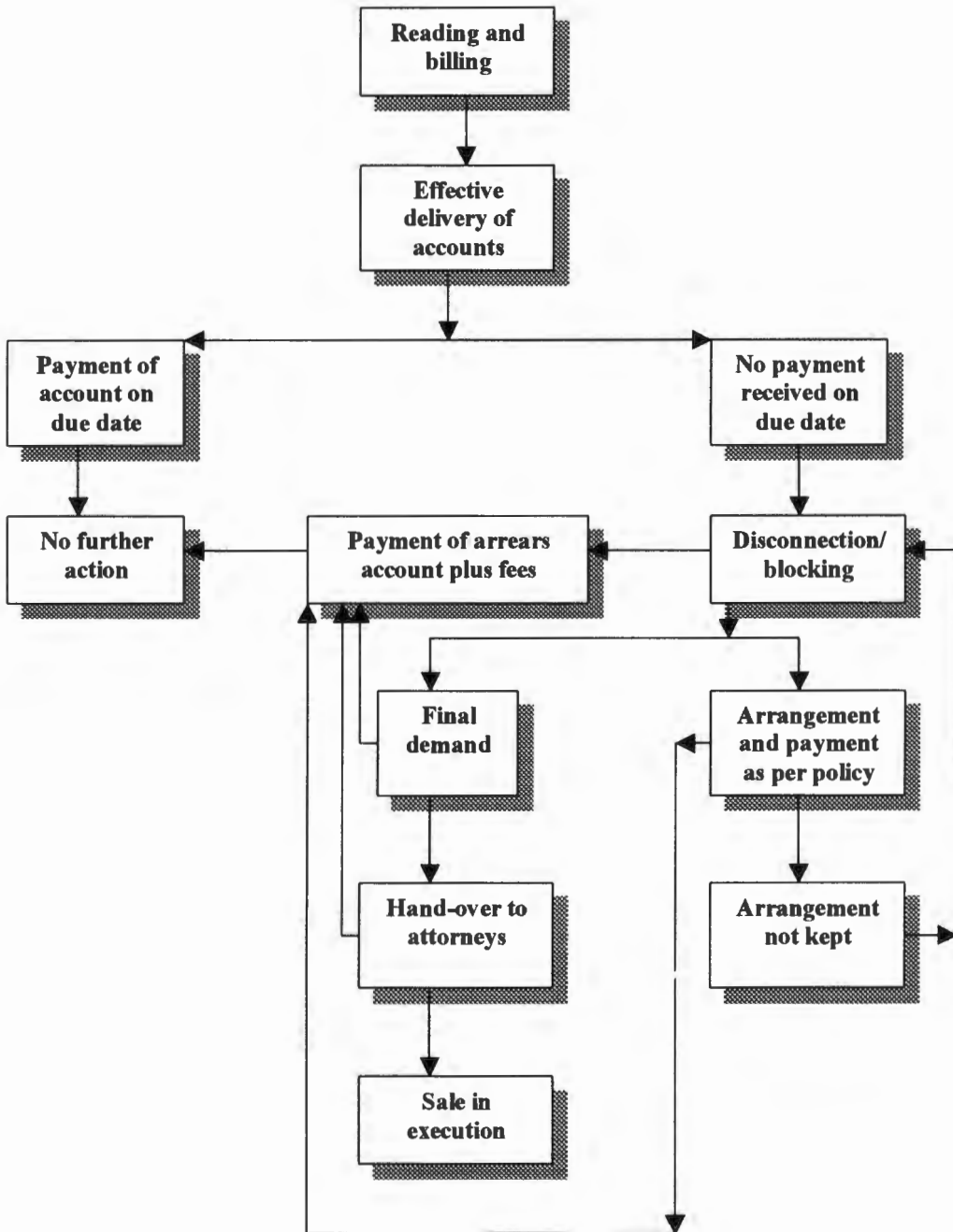
Two methods could be followed namely the cash realised basis where potential income less the percentage of non-payment is taken as budgeted income. The percentage of non-payment is the non-payment rate applicable to the particular local authority. This will bring the budgeted income more or less in line with the income realised.

The second method is to budget for potential income but a contribution out of income must then be made towards a bad debt reserve. Through the investigation it was apparent that this is the preferred option as it leaves the local authority with a bit more freedom as with the cash realised basis.

The local authority can under the potential income option decide on what level it can afford to contribute towards the reserve. Should there be an operating surplus at the financial year-end a further contribution out of the un-appropriated surplus can then be made.

### 5.3. Schematic proposal of credit management

Figure 5.1 Credit management



## **5.4. Recommendations**

Each local authority should have a formal credit management policy approved by the council. Specific circumstances such as income per capita and unemployment unique to that local authority will have an influence on the exact wording of that local authority's policy. The credit management policy as set out in this chapter should therefore be seen as a model, which could be amended to suit local conditions.

The importance of having such a policy approved by the council lies in the political backing needed to achieve effective credit management in the local scenario. The whole issue of non-payment was created by the politicians of the past to overthrow black local authorities. This culture created over a long period of time now needs to be changed. This can only be achieved through the aid of the present day politicians or councillors publicly demonstrating and voicing their support for payment of services and credit management.

A formal credit management policy will also ensure that the administrative staff performs credit management in a uniform manner to all citizens of that local authority.

### **5.4.1. General policy statements**

5.4.1.1. Council undertakes to correctly and at regular intervals bill the inhabitants of the town for property rates, and other municipal services supplied to the inhabitants by the local authority.

5.4.1.2. Council undertakes to ensure that the consolidated accounts are posted/hand delivered to the respective consumers, to reach the consumers before the due date printed on the account.

5.4.1.3. Council expects from the consumer to pay, in full, the account rendered on or before the due date. Failure to comply will result in debt collection actions instituted against the consumer in default.

5.4.1.4. Before being provided with electricity, water and or other consumer services the consumer must sign a supply agreement in which inter alia the consumer agrees that the electricity and or water payment system may be used for the collection of arrears service charges.

5.4.1.5. The income budget will be based on potential income with the proviso that a percentage contribution out of income towards a bad debt reserve will be included in the budget.

5.4.1.6. The level of the bad debt reserve be set at a percentage of the total outstanding amount and the town treasurer be delegated the authority to, as and when needed, contribute further amounts to this reserve from un-appropriated surpluses.

#### **5.4.2. Consumer deposits**

5.4.2.1. Business and domestic deposits be determined at a number of times the average monthly account with a minimum amount for water and for electricity respectively for domestic consumers and a minimum amount for electricity and or water in respect of commercial consumers.

5.4.2.2. New consumer deposits for business and industrial consumers must be re-assessed three months after the initial deposit date.

5.4.2.3. All deposits reviewed biennially and/or when a consumer's service requires disconnection/blocking as a result of non-payment.

5.4.2.4. Deposits to be paid in cash or bank guaranteed cheque. A bank guarantee is accepted in cases where the deposit exceeds an amount set by the council. Such bank guarantee to be delivered in person at the council offices during normal office hours.

5.4.2.5. All deposits to be paid at least 2 days prior to occupation of the property. Failure to comply may result in a delay with the connection of services.

5.4.2.6. No electricity deposit is required if a pre-paid meter is installed at the property.

5.4.2.7. Deposits levied may be paid off monthly over a maximum period of 6 months in respect of existing consumers where conventional electricity and water meters are installed. Aforementioned only to become applicable after entering into a written agreement with the local authority.

### **5.4.3. Disconnection for non-payment**

#### **5.4.3.1. General**

The supply be blocked/disconnected (whether pre-payment or conventional) in the case of consumers receiving other services and who fall into arrears on those services and shall be charged the applicable re-connection fee.

Where a service agreement with the local authority have not been entered into by the customer, water and/or electricity will be disconnected until such time as a service agreement has been signed and the applicable deposits paid.

Where electricity and/or water supply has been disconnected erroneously a written apology will be dispatched within seven workdays.

#### 5.4.3.2. Electricity

Services to customers with conventional electricity meters in respect of which service accounts are in arrears, shall be disconnected monthly, at a set number of days after the due date and charged the applicable re-connection fee. The service will not be re-instated before the account is paid in full or satisfactory arrangements in terms of the credit management policy have been made and honored.

The electricity will be disconnected before 13:00 on the day disconnections are made. Reconnections will commence as soon as practically possible.

Electricity not be sold to consumers with pre-paid meters if the consumer's municipal services account is not paid in full or satisfactory arrangements in terms of the credit management policy have been made and honored.

Meters to be marked clearly when the supply was disconnected for non-payment in order to prevent the possibility of disconnected meters being reported as faulty.

Consumers who have offered a cheque as payment for services, and which cheque is returned by the financial institution, will be disconnected and or blocked at the soonest opportunity. The account will be flagged and no further cheque payments will be accepted.

Standby electricians/meter readers/contractors are not permitted to restore service to consumers without authority from treasury.

Follow up disconnections within a set number of days must be made to ensure that consumers that have not settled their arrears are still without services.

Consumers who have reconnected themselves will be dealt with under clause 5.4.4. of the credit management policy.

#### 5.4.3.2. Water

Services to consumers with conventional water meters in respect of which service accounts are in arrears, shall be disconnected regularly after the time period of the notice have lapsed and charged the applicable reconnection fee.

In all cases where water is disconnected a lockable three functional valve be installed to facilitate future reconnections and disconnections. The service will not be re-instated before the account is paid in full or satisfactory arrangements in terms of the credit management policy have been made and honored.

Water not to be sold to consumers with pre-paid meters if the consumer's municipal services account is not paid in full or satisfactory arrangements in terms of the credit management policy have been made and honored.

Meters to be marked clearly when the supply was disconnected for non-payment in order to prevent the possibility of disconnected meters to be reported as faulty.

Standby plumbers/meter readers/contractors are not permitted to restore service to consumers without authority from treasury.

Follow up disconnections to be made within a set number of days to ensure that consumers that have not settled their arrears are still without services. Consumers who have reconnected themselves will be dealt with under clause 5.4.4. of the credit management policy.

In cases where water leaks are discovered on the property of the consumer and he does not react timeously to rectify the problem a restricting washer be installed to curb water losses and to limit the amount of water to be charged to the consumer.

A written notice will be served on the consumer, stating the intention of the local authority, to disconnect the water supply within a set number of days.

#### **5.4.4. Tampering**

5.4.4.1. Where an electrical/water supply is found to be tampered with or bypassed, the electricity/water supply be disconnected in such a way that no further electricity/water consumption at that premises is possible in whatsoever way. The applicable recommissioning and reconnection charges to be applied.

5.4.4.2. Tamperers be dealt with in the following manner;

##### *First tampering offence*

- Isolate supply at the point of supply.
- Notify the occupier by letter of the action to isolate and to pay the applicable recommissioning fee for a first offence plus the calculated services consumed.
- Services to be re-instated after the required amount has been paid.

##### *Second tampering offence*

- Disconnect supply at point of supply
- Notify the occupier by letter of the action to disconnect and to pay the applicable recommissioning fee for a second offence plus the calculated services consumed.
- Notify the owner that the supply to his property has been tampered with twice and to warn him that the supply will be removed should further tampering take

place. He will further be responsible to pay the recommissioning fee and arrange for an inspection if the supply is tampered with for the third time.

- Services only to be re-instated after the required amount has been paid.

#### *Third tampering offence*

- Remove the service supply including cable/pipes and meter.
- Notify the occupier of the action to remove services and of any outstanding fees and calculated consumption due and if the money due has not been paid by a specified date and time, the matter will be handed to debt collection specialists.
- Notify the owner that the service supply has been removed and that a new supply will only be installed when the following conditions have been met:
  - The occupier is not the defaulter or alternatively satisfactory proof is given that the defaulter has been rehabilitated.
  - The fee for a new connection including the cable/pipe cost as well as all service consumption and all other outstanding amounts has been paid.
- Services to be re-instated after the required amount has been paid.

5.4.4.3. The tampering fee together with the full outstanding service account to be paid in full before the supply will be re-instated. Arrangements in terms of the credit management policy may only be made on outstanding service account portion of the total due amount.

5.4.4.4. Council reserves the right to enforce any other rights given to council by the Water Act, Water by-laws, Electricity Act and Electricity by-laws.

#### **5.4.5. Agreements**

5.4.5.1. The town treasurer or his delegate be authorized to enter into agreements with the debtors with arrears accounts and to grant such debtors extensions for payment on merit subject to:

An immediate payment of a percentage of the outstanding debt.

Defaulting agreement the first time an immediate payment of a higher percentage as in (5.4.5.1.2.) of the outstanding debt.

Defaulting agreement the second time the treasurer be delegated the authority to enter into further negotiations/agreements subject to an immediate payment of an amount equal to or more than half of the outstanding amount.

5.4.5.2.No interest will be charged on the arrears amount of such an agreement, provided that the consumer honors the agreement.

5.4.5.3.Only account holders with a positive proof of identity or an authorized agent with a Power of Attorney will be allowed to complete an Acknowledgement of Debt.

5.4.5.4.Extension for the payment of arrears together with their current accounts should not exceed the maximum periods as set out below with the first installment within 30 days of date of agreement:

Initial arrears smaller than R 500,00	No. Months
Initial arrears from R 501,00 to R 1 000,00	No. Months
Initial arrears from R 1 001,00 to R 2 000,00	No Months
Initial arrears from R 2 001,00 to R 4 000,00	No. Months
Initial arrears above R 4 001,00	No. Months

In cases of merit the town treasurer may determine other periods of repayment.

5.4.5.5.An acknowledgement of debt must be completed with all arrangements for paying off arrears accounts. One copy must be handed to the client and a copy filed at the credit management section.

5.4.5.6. Consumers who were already summonsed can also apply for credit facilities but all costs already incurred will be for his/her account and an initial payment of at least half of the outstanding debt will be applicable. These consumers must also sign an acknowledgement of debt, which includes legal fees to date.

5.4.5.7. Failure to honor the agreement will lead to immediate blocking/disconnection of services.

5.4.5.8. A voluntary garnishee order/ emolument order should where possible be obtained if the debtor is employed.

#### 5.4.6. **Hand-overs**

5.4.6.1. A final demand is to be issued in respect of all debtor accounts reflecting an amount outstanding for longer than 30 days and, if said accounts still reflect an arrears amount after a further 30 days, such accounts are to be handed over for collection by external debt collecting specialists.

5.4.6.2. The following procedure is to be followed:

Service accounts from R 100,00 to R 1 500,00 to be handed to debt collecting agencies on a basis of no collection – no fee.

Outstanding service accounts in excess of R 1 500,00 are to be handed to attorneys for collection.

5.4.6.3. Outstanding accounts in respect of assessment rates are to be handed to the attorneys for collection.

5.4.6.4. The town treasurer be delegated the authority to determine the economic viability of all arrears accounts before these accounts are handed over to the attorneys for collection.

5.4.6.5. The town treasurer investigates ways and means of assisting consumers before attaching movable or immovable property.

#### **5.4.7. Listing at Credit Bureau**

5.4.7.1. Council to enroll as member of the ITC.

5.4.7.2. Consumers falling into arrears on a regular basis to be black listed at the ITC as a “slow payer”.

5.4.7.3. Judgements against consumers resulting from legal proceedings instituted by council to be listed at the ITC.

5.4.7.4. Consumers registered with the local authority as indigent be listed as such at the ITC.

#### **5.4.8. General**

5.4.8.1. All arrears accounts in respect of the sale of erven are dealt with in accordance with the applicable cancellation clause in the sale agreement.

5.4.8.2. The town treasurer to be authorized to write-off all terminated accounts with outstanding balances below a set amount after all steps as set out in this policy have been implemented and the amounts are deemed irrecoverable. The aforementioned authorization also be extended to include the following:

- All amounts below R 100,00 will be written off, 30 days after a letter of final demand has been served and no reaction received.
- All amounts below R 10,00 will be written off as they occur.

5.4.8.3. Suitable persons be tasked (Councilors and Officials) to workshop the credit management policy with the community.

5.4.8.4. Regular meter audits will be carried out and disconnections following from the audits effected.

5.4.8.5. A consumer not be allowed to selectively nominate any money paid by him or her for specific services and that the allocation of payments automatically be done in the order preferred by council. The town treasurer be delegated the authority to determine the order of preference.

5.4.8.6. Consumers who are in arrears with either rent or housing installments for two or more months, immediately be handed over to council's attorneys for eviction from the property after the necessary notice in terms of the law has been served upon the owner/tenant.

5.4.8.7. In the event of mass disconnections, same-day reconnections cannot be guaranteed, however, under normal circumstances same-day reconnections will be effected.

5.4.8.8. No disconnection of services due to non-payment shall occur on a Friday, the day preceding a public holiday or after 13:00 on any day.

5.4.8.9. The town treasurer be delegated the authority to appoint debt collection specialists as well as the authority to enter into agreements with such agencies in terms of the Contingency Fee Act.

5.4.8.10. The non-compliance of any clause pertained in this credit management policy due to computer hardware or software failure will not be seen as a failure to comply with a council resolution.

## **5.5 Conclusion**

The model of a credit management policy as given in this chapter must not be seen as a quick fix. This is only a guideline for local authorities around which it must build its own policy to suit local conditions. The policy should also be revised as local conditions change. After approval by council and workshopping with the community it is important to strictly adhere to the policy when performing credit management. The results will only become really visible after a period of 2 years as the community takes time to get used to this new culture of payment for services. The judicial process is also very slow and contributes to the long period before the effects of a properly documented credit management policy will be visible.

# ADDENDUM A

## QUESTIONNAIRE

*Note: Please answer all the questions by placing an X in the appropriate block.*

### Section 1 General information

- 1. Name of local authority
- 2. Grading of local authority
- 3. Number of debtors
- 4. Total amount outstanding
- 5. Average number of days outstanding

### Section 2 Budgetary procedures

- 1. Does your council make provision for bad debts?

Yes	No
<input type="checkbox"/>	<input type="checkbox"/>

- 2. Which of the following methods does your Council use to provide for bad debts?

- 2.1. Provision out of surpluses at the end of the financial year?

Yes	No
<input type="checkbox"/>	<input type="checkbox"/>

**2.2. Out of operating budget as a contribution?**

Yes	No

**2.3. If contribution out of operating budget – what percentage of total income?**

**2.4. If none of the above methods are followed please describe the method followed at your local authority.**

.....

.....

.....

**3. Indicate what portion of the provision is annually spent on:**

- **Workshopping of the community**
- **Bad debt write off**
- **Other methods to prevent bad debt**

**4. Does your council budget for service income on a:**

- **Cash realised basis**
- **Potential income basis**
- **Which would you prefer**

**5. What is your council's average payment percentage?**

**6. To what extent does your council provide for bad debts**

- 30% of outstanding debt
- 50% of outstanding debt
- 100% of outstanding debt

**Section 3 Changing the culture of non-payment**

**1. Do councillors publicly support the credit management policy?**

Yes	No
<input type="text"/>	<input type="text"/>

**2. Have the residents been informed about the need to pay for services?**

Yes	No
<input type="text"/>	<input type="text"/>

**3. How was the residents informed?**

.....  
.....  
.....

**4. What reasons were given by the community for non-payment?**

.....  
.....  
.....

5. What other methods were employed by your council to change the culture of non-payment?

.....  
.....  
.....

**Section 4 Minimalisation of non-payment on income**

1. Has your council installed pre-payment meters?

Yes	No

2. For which services has pre-payment meters been installed

Water	Electricity

3. Percentage pre-payment meters installed for each service

Water	Electricity

4. What other methods are followed by your council to prevent non-payment

.....  
.....  
.....

## Section 5 Credit management policies in operation

1. Does your Council have a formalised credit management policy?

Yes	No

2. Does the formalised credit management policy specifically deal with:

2.1. Deposits

2.1.1. Paying the raised amount in installments?

Yes	No

2.1.2. Determination of deposit amount?

Yes	No

2.2. Non-payment

2.2.1. Blocking/ disconnection of electricity supplies?

Yes	No

2.2.2. Blocking/ disconnection of water supplies?

Yes	No

2.2.3. Payment of a reconnection fee?

Yes	No

2.2.4. On what is the reconnection fee based?

.....  
.....  
.....

2.2.5. After how many days in arrears are consumer services disconnected?

.....  
.....  
.....

2.2.6. How do you treat the non-payment of property rates?

.....  
.....  
.....

**2.3. Tampering with supply**

2.3.1. Disconnection of electricity supplies?

Yes	No

2.3.2. Disconnection of water supplies?

Yes	No

2.3.3. Payment of a tampering fee?

Yes	No

2.3.4. On what is tampering fee based?

.....  
.....  
.....

**3. External collections**

**3.1. Does your council's credit management policy deal with account handovers to external debt collecting agencies and attorneys?**

Yes	No

**3.2. Number of days outstanding before account is handed over?**

**3.3. Estimated success rate of handovers**

**4. Payment agreements**

**4.1. Does your council's credit management policy include the entering into payment agreements with arrears debtors?**

Yes	No

**4.2. What arrangements can be made?**

.....  
.....  
.....

**5. Relief for the indigent**

**5.1. Does your council's credit management policy include some form of relief for the indigent?**

Yes	No

**5.2. Does your council subsidize indigent accounts?**

Yes	No

**5.3. From what source are these accounts subsidized?**

.....  
.....  
.....

**6. Does your council list defaulters at the ITC (Information Trust Corporation)?**

Yes	No

**7. Please attach a copy of your credit management policy to this questionnaire.**

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