Policies and Procedures

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ALLOWANCE FOR DOUBTFUL ACCOUNTS	01/09/2018	

POLICY/ PURPOSE:

The purpose of this policy is to communicate the Company's policies and procedures relating to the proper accounting of uncollectible trade receivables.

SCOPE:

The scope of this subject includes the accounting treatment recommended for recognizing potential bad debt losses, procedures applicable to maintaining the *Allowance for Doubtful Accounts*[1] and the absorption of actual bad debt losses through the *Provision for Doubtful Accounts*.

This policy applies to all of the Company's subsidiaries and business units.

POLICY AND PROCEDURES:

Daikin Accounting policies require Accounts Receivable to be reported in the financial statements at Net Realizable Value. Net Realizable Value is equal to the Gross Accounts Receivable, less an estimated allowance for doubtful or uncollectible accounts. An allowance should be established if it is probable that not all receivables will be fully collected and the amount of future loss can be reasonably estimated.

1.0 POLICY:

1.1 It is Company Policy that all business units establish and maintain an

[1] Words in *Italic* are defined in Section 5.0 of this policy.

Allowance for Doubtful Accounts, to facilitate the reporting of Net Trade Accounts Receivable at an amount equal to expected collectible amounts.

1.2 It is Company Policy to recognize actual and future estimated losses arising from less than full collection of Trade Accounts Receivable as a period expense and to write-off receivables as they are determined to be uncollectible.

2.0 <u>RESPONSIBILITIES OF FINANACE CONTROLLER:</u>

2.1 Ensure that allowance balances are maintained at an adequate level.

2.2 Make necessary allowance provisions and adjustments when deemed necessary.

2.3 Scheduling and conducting periodic (at least quarterly) reviews of receivables for evaluation of doubtful accounts, identification of doubtful accounts and recommendation of their proper disposition.

2.4 Approval of necessary write-offs for accounts determined to be uncollectible.

2.5 Preparation and distribution of quarterly and annual reports.

3.0 <u>ACCOUNTING FOR UNCOLLECTIBLE TRADE RECEIVABLES:</u>

3.1 Establishing the Reserve Provision

A. An estimated provision for bad debts will be established at the beginning of each year. A review will be made at least quarterly to determine the adequacy of the provision. Any required adjustment made to the allowance and the provision will be made at the time the adjustment becomes apparent.

B. The calculation of *Allowance for doubtful accounts* is to be based on the following two step methodology:

a. The Allowance will separately include all known account receivables deemed uncollectible. This will include receivables in litigation and uncollectible receivables as defined in 5.2 and 5.3. Any receivable either currently in litigation or that has been turned over to a collection agency should be reserved at least 50%, unless that item's specific circumstances require a higher percentage. Any item over 1 year past due and any items considered uncollectible should be reserved at 100%. Any exceptions to the above must be approved by the Corporate.

b. Remaining receivables based on aging groupings should be factored for allowance provisions as mentioned in 5.7 as follows.

Past due dates from payment deadline	Allowance rate
0 – 3 months	No provision required.
3 - 12 months	Provision equal to 10% of accounts Past due.
Over 12 months	Provision equal to 100% of accounts Past due

The prior two year's actual activity should be the basis for determining initial percentages.

Where the customer account is covered by credit insurance only 10% of the amount overdue more than 12months which represents the amount not covered by the insurance.

3.2 Accounting for Actual Accounts Receivable Write-Offs and Recoveries

A. Although an account has been reserved for at 100%, there still may be the possibility of collection. Every effort, within reason, should be made, including working with the legal department or outside counsel, to collect amounts due. However, the likelihood of any additional collections diminishes over time. Twice a year, at mid-year and at year-end, uncollectible accounts should be write-off by reducing the allowance for doubtful accounts and the associated receivable accounts. Records of these adjustments should be retained for five years and write-off activity should be reviewed in conjunction with the periodic reserve analysis. All write-offs should be in accordance with the approval process set out in the LOA.

B. It may be possible to recover collections of even accounts previously written off as uncollectible. In these instances, the cash recovery should be posted with a balancing credit to accounts receivable. Accounts receivable is then debited and the allowance charged, so the funds receipt is documented in accounts receivable.

4.0 <u>REPORTING:</u>

At the end of each quarter detail of reserves for bad debts and write-off activity should be reported in the DIVA Pack. Information provided should be in accordance with the DIVA pack instructions.

5.0 DEFINITIONS:

5.1 Doubtful Receivables are those items where there is a reasonable doubt of future collection in full. Normally the potential for a doubtful receivable increases as the age of the receivable increases.

5.2 Receivables in Litigation are those items either placed for collection with a collection agency or where legal proceedings have begun. The potential for less than full collection for these items is higher than for a doubtful receivable.

5.3 Uncollectible Receivables are those items determined to be worthless because of either the debtor's inability to pay, including bankruptcy, or the Company's decision that it is impractical to pursue collection.

5.4 Allowance For Doubtful Accounts is the Balance Sheet account which maintains the expected amount of future potential bad debts which, when combined with Gross Accounts Receivable Trade, results in the Net Accounts Receivable expected to be collected.

5.5 Provisions For Doubtful Accounts is the Profit and Loss expense account utilized to account for changes and adjustments to the Allowance account. The financial impact of expected provisions will be included in the STP of each business unit.

5.6 Aged Accounts Receivable Trade is the tool needed to estimate the collectability of the receivables. It is Company Policy that, at a minimum, accounts be classified as: Current; 1-60 Days Past Due; 61-90 Days Past Due; and Over 90 Days Past Due. Additional age classifications can be utilized.

5.7 The Allowance Method, as opposed to the Direct Write-off Method, is the only acceptable method for establishing and reporting an allowance for doubtful accounts and is the accepted Company Policy. This method utilizes a percentage of each period's aged receivables to estimate future uncollectible amounts. Percentages used are based upon prior actual bad debts history, adjusted for current business conditions.

/s/ Gary Burnett

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