

Residual Debt Services Limited (under curatorship)

Unaudited Condensed Interim Financial Statements

31 March 2019

These financial statements were prepared under the supervision of G Raubenheimer CA (SA)

Registration number: 1975/002526/06

**NCR Registration number NCRCP5
An Authorised Financial Services and Registered Credit Provider**

C Du Plessis replaced T Winterboer as curator of RDS effective 1 April 2018, following T Winterboer's resignation as curator effective 31 March 2018. T Winterboer was appointed as curator of Residual Debt Services Limited ((the "Company") previously named African Bank Limited (the "Bank")) on 10 August 2014 by the then Minister of Finance of the Republic of South Africa and pursuant to the Banks Act No. 94 of 1990 (as amended) to manage the affairs of the Company subject to the supervision of the Registrar of Banks.

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STATEMENT OF RESPONSIBILITY BY THE CURATOR

The curator is responsible for the preparation and fair presentation of the condensed interim financial statements, comprising the condensed statement of financial position as at 31 March 2019, the condensed statement of comprehensive income, the condensed statement of changes in equity, the condensed statement of cash flows for the period then ended, and the selected notes to the condensed interim financial statements; which are prepared in accordance with the Framework as stipulated in the Accounting Policies of these Financial Statements and in the manner required by the Companies Act 71 of 2008 of South Africa (“Companies Act”).

The curator’s responsibilities include:

- the management of the Company (subject to the supervision of the Registrar of Banks (“the Registrar”)), and any other person vested with the management of the affairs of the Company as was divested thereof from 10 August 2014; and
- the obligation to recover and take possession of all the assets of the Company.

The curator shall:

- subject to the supervision of the Registrar, conduct the management of the Company in such a manner as the Registrar may deem to best promote the interests of the creditors of the Company and of the banking sector as a whole;
- comply with any direction of the Registrar;
- keep such accounting records and prepare such annual financial statements, interim reports and provisional annual financial statements as the Company or its directors would have been obliged to keep or prepare if the Company had not been placed under curatorship;
- convene the annual general meeting or any other meeting of the Company provided for in the Companies Act, and, in that regard, comply with all the requirements with which the directors of the Company would in terms of the Companies Act have been obliged to comply if the Company had not been placed under curatorship; and
- have the power to bring or defend in the name and on behalf of the Company any action or other legal proceedings of a civil nature and, subject to the provisions of any law relating to criminal proceedings, any criminal proceedings.

Due to the nature of the curatorship, the financial statements are not presented on a going concern basis; rather the financial statements have been presented using the Framework as stipulated in Addendum A to these Financial Statements. The purpose of the Company during curatorship is to collect all outstanding advances retained by the Company, build the required indemnity cash reserves as required by the SARB and where excess cash is collected, to make payment to stub note holders.

Approval of the condensed interim financial statements

The interim condensed financial statements found on pages 4 to 14 were approved by the curator on 20 May 2019

C Du Plessis
Curator

Midrand

A signed copy of the condensed interim financial statements is available for inspection at the registered office.

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CONDENSED STATEMENT OF FINANCIAL POSITION
as at 31 March 2019

R million	Unaudited March 2019	Audited September 2018
Assets		
Cash and cash equivalents	3 895	4 070
Net advances	343	528
Other assets	10	18
Current tax asset	4	4
Total assets	4 252	4 620
Liabilities and equity		
Other liabilities	59	189
Stub instruments	9 507	9 629
Total liabilities	9 566	9 818
Ordinary share capital	121	121
Ordinary share premium	14 283	14 283
Reserves and accumulated losses	(19 718)	(19 602)
Total equity (capital and reserves)	(5 314)	(5 198)
Total liabilities and equity	4 252	4 620

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CONDENSED STATEMENT OF COMPREHENSIVE INCOME
for the six months ended 31 March 2019

R million	Unaudited 6 months ended 31 March 2019	Unaudited 6 months ended 31 March 2018
Interest income on advances	16	38
Credit impairment reversal	477	604
Risk-adjusted income from operations	493	642
Other interest income	153	152
Other income	13	6
Interest expense	(533)	(530)
Operating costs	(221)	(311)
Indirect taxation: VAT	(21)	(35)
Loss from operations	(116)	(76)
Capital items	-	49
Loss before taxation	(116)	(27)
Direct taxation: current and deferred	-	-
Total comprehensive loss for the period	(116)	(27)

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CONDENSED STATEMENT OF CHANGES IN EQUITY
for the six months ended 31 March 2019

R million	Ordinary share capital	Ordinary share premium	Accumulated losses	Total
Balance at 30 September 2017 (audited)	121	14 283	(19 606)	(5 202)
Total comprehensive loss for the period	-	-	(27)	(27)
Balance at 31 March 2018 (unaudited)	121	14 283	(19 633)	(5 229)
Total comprehensive profit for the period	-	-	31	31
Balance at 30 September 2018 (audited)	121	14 283	(19 602)	(5 198)
Total comprehensive loss for the period	-	-	(116)	(116)
Balance at 31 March 2019 (unaudited)	121	14 283	(19 718)	(5 314)

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CONDENSED STATEMENT OF CASH FLOWS
for the six months ended 31 March 2019

R million	Unaudited 6 months to March 2019	Unaudited 6 months to March 2018
Cash generated from operations	145	112
Cash received from collection activities	42	45
Recoveries on advances previously written off	347	385
Cash paid to suppliers*	(244)	(318)
Decrease in gross advances	280	553
Interest received on cash reserves	170	152
Indirect and direct taxation paid	(120)	(47)
Cash inflow from operating activities	475	770
Cash inflow from investing activities	-	49
Cash outflow from financing activities	(650)	(500)
Interest paid to senior unsecured stub instrument holders	(650)	(500)
Increase in cash and cash equivalents	(175)	319
Cash and cash equivalents at the beginning of the period	4 070	3 675
Cash and cash equivalents at the end of the period	3 895	3 994

* Renamed from “cash paid to suppliers of funding and services” as applied in the prior period, due to cash paid to suppliers of funding being reflected under financing activities.

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NOTES TO THE CONDENSED INTERIM FINANCIAL STATEMENTS

1. General information

Residual Debt Services Limited (under curatorship) (“RDS”) is a public company incorporated in the Republic of South Africa. The Company’s shares are held by African Phoenix Investments Limited (the new registered name for African Bank Investments Limited “ABIL”).

RDS (previously named African Bank Limited) was placed under curatorship on 10 August 2014 in terms of section 69 of the Banks Act by the South African Reserve Bank (“SARB”). The SARB decision followed a period of growing uncertainty surrounding the Company, after a series of financial losses were announced by the Company’s holding company ABIL. Furthermore, Ellerine Furnishers Proprietary Limited and Ellerine Holdings Limited, which are fellow subsidiaries of the Company, were placed under business rescue on 7 August 2014 and 22 August 2014 respectively.

2. Basis of preparation

Due to the nature of the curatorship, the Company’s financial statements have been prepared on a “run-down” basis. The result of the “run-down” business model is that the Company as a legal entity is no longer regarded as a going concern and as such the financial statements are not presented on a going concern basis. The financial statements have been presented using the Framework as stipulated in the Company’s accounting policies disclosed in Addendum A to these financial statements.

The purpose of the Company during curatorship, is to collect the outstanding advances of the Company, build the indemnity cash reserves as required by the SARB and, where excess cash is collected, to make payment to stub note holders in accordance with the cash flow priority of payments (“Distribution Waterfall”).

These condensed interim financial statements should be read in conjunction with the 30 September 2018 annual financial statements; which were prepared on a “run-down” basis due to the implementation of the restructure described in the Curator’s report for the financial period ended 30 September 2018.

3. Significant accounting judgements and key sources of estimation uncertainty

In the application of the Company’s accounting policies, the Curator is required to make judgements, estimates and assumptions about income, expenses and the carrying amounts of assets and liabilities that are not readily apparent from other sources. The estimates and associated assumptions are based on the historical experience and other factors that are considered to be relevant. Due to the inherent uncertainty in making estimates, actual results reported in future periods may be based upon amounts which differ from those estimates, judgements and assumptions.

In preparing these condensed interim financial statements, the significant judgements made by the Curator in applying the Company’s accounting policies and key sources of estimation uncertainty were the same as those that applied to the annual financial statements for the year ended 30 September 2018.

The Company is a single segment collection entity operating within the South African economic environment. The business is widely distributed with no reliance on any major customers. The Company’s primary business is to collect the remaining advances book and there are no clients that account for more than 10% of revenue. For this reason, the Company did not prepare a segmental report.

4. Advances and credit quality

The impairment provisions for gross advances are classified into three categories i.e. specific impairment, portfolio specific impairment, and incurred but not reported (IBNR) provisions. The specific impairment provision of R1 397 million (September 2018: R1 439 million) is in respect of the non-performing (on balance sheet) loan book. The portfolio specific impairment provision of R5.4 million (September 2018: R6.5 million) and the IBNR provision of R3 million (September 2018: R5 million) is in respect of the performing loan book.

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	March 2019		
	Rm		
	Loan	Credit card	Total
Financial assets that are neither past due nor specifically impaired			
CD 0	34	-	34
Financial assets that are past due and specifically impaired			
CD 1 to 3	13	1	14
CD 4 and higher	1 616	84	1 700
Total credit exposure	1 663	85	1 748
Total impairments	(1 350)	(55)	(1 405)
Incurring but not yet reported (IBNR)	(3)	-	(3)
Portfolio specific impairment	(4)	(1)	(5)
Specific impairment	(1 343)	(54)	(1 397)
Deferred administration fees	-	-	-
Net advances	313	30	343

The gross value of the written off book at 31 March 2019 was R10.4 billion (September 2018: R12.2 billion).

	September 2018		
	Rm		
	Loan	Credit card	Total
Financial assets that are neither past due nor specifically impaired			
CD 0	65	1	66
Financial assets that are past due and specifically impaired			
CD 1 to 3	29	1	30
CD 4 and higher	1 807	83	1 890
Total credit exposure	1 901	85	1 986
Total impairments	(1 402)	(49)	(1 451)
Incurring but not yet reported (IBNR)	(5)	-	(5)
Portfolio specific impairment	(6)	(1)	(7)
Specific impairment	(1 391)	(48)	(1 439)
Deferred administration fees	(7)	-	(7)
Net advances	492	36	528

	Unaudited March 2019 Rm	Audited September 2018 Rm
5. Stub instruments		
Senior unsecured stub instrument	(4 322)	(4 743)
Subordinated unsecured stub instrument	(5 185)	(4 886)
	(9 507)	(9 629)

Stub instruments:

- are unsecured unlisted claims against the Company;
- the senior unsecured stub instrument is subordinated in favour of SARB and shall only be repayable once all operational and run-off expenses have been paid or provided for in full, and the Indemnity Reserve has been established or released and will rank pari passu with the other unsecured unsubordinated creditors of the Company; and has no fixed maturity or interest payment date. Subordinated unsecured stub instrument is subordinated in favour of all of the above, including the senior unsecured stub instrument.

6. Fair value of stub instruments

As part of the restructure and exchange offer, the Company extinguished its existing funding liabilities and simultaneously recognised a new funding liability – namely the stub instruments.

In line with the Company's accounting policy the stub instruments were initially recognised at their face value and subsequently measured at amortised cost of the contractual cashflows.

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In estimating fair value of liabilities, the Company made a number of assumptions that gave rise to a range of projected outcomes. In practice, it is possible that a combination of outcomes would materialise and that these potential outcomes may fall anywhere within the ranges projected.

The expected future cash flows have been modelled based on the various possible outcomes mentioned above. A discounted cash flow valuation technique has been applied to estimate the projected outcome under each of these outcomes.

The projected outcomes under each of the scenarios described have been classified as Level 3 for purposes of determining their fair value in terms of IFRS 13 – Fair value measurement.

Given that there is no active or directly observable market for the stub instruments on which a fair value, using level 1 or level 2 inputs could be derived, the fair value of the new stub instruments as at 31 March 2019 requires a level 3 input valuation technique to be performed in order to arrive at an appropriate fair value at the reporting date, in terms of IFRS 13. An appropriate valuation technique includes a discounted cash flow valuation using expected future cash flows.

The key assumptions the Company has made in deriving the expected cash flows in this scenario are as follows:

- The expected cash flows derived from the remaining advances is projected for a 60 month period from the date of the valuation;
- Using the expected cash flows derived from the remaining advances, the Distribution Waterfall is applied to the free cash flows;
- The Indemnity Reserve has been built up and it is assumed that 100% (R3 billion) thereof will be called upon by African Bank Limited and accordingly be paid out over a three year period;
- As the cash of R3 billion has built up to satisfy any potential indemnity reserve claim as detailed above, it is assumed that all surplus cash in excess of the R500 million operational float is then paid to senior unsecured stub instrument holders (every 6 months).
- The model assumes that subordinated unsecured stub instrument holders will not receive any cash until the senior unsecured stub instrument holders are not repaid in full.
- Payments to senior unsecured stub instrument holders commenced in January 2018, and occurred every 6 months as envisaged above and are assumed to take place (based on forecasted surplus cash balances at the applicable points in time) until the end of the 60 months period mentioned above.
- An additional cash outflow totalling R200 million has been incorporated for potential future closure and associated costs.
- The discount rate used to present value the expected future cash flows is 14.0%, which represents a modified weighted average cost of capital (“WACC”) for the Company.

Sensitivity - change in WACC

In determining the fair value of the stub instruments, if the discount rate was increased and decreased by 1% the fair value as at 31 March 2019 would change as detailed below:

	31 March 2019			30 September 2018		
	Fair value – using 14.0% NACM Rm	Fair value – using 15.0% NACM Rm	Fair value – using 13.0% NACM Rm	Fair value – using 14.0% NACM Rm	Fair value – using 15.0% NACM Rm	Fair value – using 13.0% NACM Rm
Senior stub unsecured instrument	2 219	2 173	2 267	2 472	2 421	2 525
Subordinated stub instrument	Nil	Nil	Nil	Nil	Nil	Nil

Sensitivity- change in assumption relating to the claim on the indemnity reserve

An additional sensitivity analysis has been performed where it is assumed that none of the indemnity reserve is claimed for the duration of the indemnity period, and thus the full R3 billion is paid to senior unsecure stub instrument holders at the end of the indemnity period, being April 2024.

In addition, the discount rate used to present value the expected future cash flows is 14.0% (which represents a modified weighted average cost of capital (WACC) for the Company). However, the R3.5 billion cash flow mentioned above is not discounted using the WACC of 14.0%, but is discounted using the 5 year risk free rate as at 31 March 2019 of 7.487% (September 2018 : 8.116%) NACQ. This is considered more appropriate as the full R3.5 billion has been collected to date and held on deposit with major South African banks.

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The table below illustrates the stub instrument's fair values under this scenario as at 31 March 2019, together with the sensitivity if the discount rate increases, or decreases by an additional 1%.

	31 March 2019			30 September 2018		
	Fair value – using 14.0%* Rm	Fair value – using 15.0%* Rm	Fair value – using 13.0%* Rm	Fair value – using 14.0% Rm	Fair value – using 15.0% Rm	Fair value – using 13.0%* Rm
Senior unsecured stub instrument	4 374	4 327	4 422	4 823	4 768	4 880
Subordinated unsecured stub instrument	324	308	340	98	93	103

* - All cash flows discounted at a NACM WACC of 14%, 15% or 13% as indicated, except for the R3.5 billion (indemnity reserve and operational float balance) which is assumed to be paid in April 2024 and is discounted at the risk free rate at 31 March 2019 of 7.487% NACQ.

Sensitivity- change in assumption relating to regulatory and industry developments

Separate to the above indicative impacts of the sensitivity of the valuation of the stub instruments to a change in the WACC and changes in the assumption relating to a claim on the indemnity reserve, there are specific regulatory and industry developments, including the potential impact of the National Credit Amendment Bill, and the potential impact of the proposed changes to the debit order collections regime which may also impact the valuation of the stub instruments.

Given the uncertainties pertaining to these developments, it is not possible to accurately estimate the impact on the valuation of the stub instruments. Assuming that the impact results in a 10% reduction on the future cash flows derived from advances to customers, the fair value of the subordinated unsecured stub instrument will decrease by R103 million from R324 million to R221 million (using a WACC of 14%).

7. Financial results

The table below demonstrates changes in the financial performance of the Company for the current reporting period and for comparative reporting periods:

Rmillion	Unaudited Six months ended 31 March 2019	Unaudited Six months ended 30 September 2018	Unaudited Six months ended 31 March 2018	Audited Year ended 30 September 2018
Interest income on advances	16	49	38	87
Credit impairment reversal	477	589	604	1 193
Risk adjusted income from operations	493	638	642	1 280
Other interest income	153	156	152	308
Other income	13	9	6	15
Interest expense	(533)	(529)	(530)	(1 059)
Operating costs	(221)	(273)	(311)	(584)
Indirect taxation: VAT	(21)	(22)	(35)	(57)
Loss from operations	(116)	(21)	(76)	(97)
Capital items	-	50	49	99
(Loss)/profit before taxation	(116)	(29)	(27)	2
Direct taxation: current and deferred	-	2	-	2
(Loss)/profit for the period	(116)	31	(27)	4

8. Events after the reporting period

The Curator is not aware of any material events occurring between the reporting date and the date of authorisation of these condensed interim financial statements.

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9. Fair value disclosures

Valuation models

The fair value of financial assets and financial liabilities that are traded in active markets are based on quoted market prices or dealer price quotations. For all other financial instruments, the Company determines fair values using other valuation techniques.

The Company measures fair value using the following fair value hierarchy; which reflects the significance of the inputs used in making the measurement.

- Level 1 fair value measurements are those derived from quoted market prices (unadjusted) in active markets for identical assets or liabilities.
- Level 2 fair value measurements are those derived from inputs other than quoted market prices included within Level 1 that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices).
- Level 3 fair value measurements are those derived from valuation techniques that include inputs for the asset or liability that are not based on observable market data (unobservable inputs).

Valuation techniques include net present value and discounted cash flow models, comparison with similar instruments for which market observable prices exist and other valuation models. Assumptions and inputs used in valuation techniques include risk free and benchmark interest rates, credit spreads and other factors used in estimating discounting rates, foreign currency exchange rates, bond and equity prices, equity and equity index prices and expected price volatilities and correlations.

The objective of valuation techniques is to arrive at a fair value measurement that reflects the price that would be received to sell the asset or paid to transfer the liability in an orderly transaction between market participants at the measurement date.

The Company uses widely recognised valuation models for determining the fair value of common and more simple financial instruments, such as interest rate and currency swaps that use only market data and require little management judgement and estimation. Observable prices or model inputs are usually available in the market for listed debt and equity securities, exchange traded derivatives and simple over-the-counter derivatives such as swaps. Availability of observable market prices and model inputs reduces the need for management judgement and estimation and also reduces the uncertainty associated with determining fair values. Availability of observable market prices and inputs varies depending on the products and markets and is prone to changes based on specific events and general conditions in the financial markets.

For more complex instruments, the Company uses its own valuation models; which are usually developed from recognised valuation models. Some or all of the significant inputs into these models may not be observable in the market, and are derived from market prices or rates or are estimated based on assumptions. Examples of instruments involving significant unobservable inputs include advances and certain loans and securities for which there is no active market. Valuation models that employ significant unobservable inputs require a higher degree of management judgement and estimation in the determination of fair value. Management judgement and estimation are usually required for selection of the appropriate valuation model to be used, determination of expected future cash flows on the financial instrument being valued, determination of the probability of counterparty default and selection of appropriate discount rate.

Fair value estimates obtained from models reflect the credit risk of the instrument and include adjustments to take account of the credit risk of the Company and the counterparty where appropriate.

Model inputs and values are calibrated against historical data and published forecasts and, where possible, against current or recent observed transactions and experiences. This calibration process is inherently subjective and it yields ranges of possible inputs and estimates of fair values, and management judgement is required to select the most appropriate point in the range.

Valuation framework

The Company has an established control framework with respect to the measurement of fair values. This framework includes formalised policies and the approval and review process.

When third party information is used to measure fair value the following procedures are performed in order to ensure that valuations meet the requirements of the framework:

- verifying that the third party is approved for use in pricing the relevant type of financial instrument; and
- understanding how the fair value has been arrived at and the extent to which it represents actual market transactions.

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Fair value measurements recognised in the statement of financial position

The Company did not measure any of its assets and liabilities, in the statement of financial position, at fair value at the end of the period 31 March 2019.

Assets and liabilities for which fair value is disclosed

31 March 2019

Rmillion	Level 1	Level 2	Level 3	Total
Financial assets				
Net advances*	-	-	1 585	1 585
Total	-	-	1 585	1 585
Financial liabilities				
Stub instruments	-	-	**	-
Total	-	-	-	-

30 September 2018

Rmillion	Level 1	Level 2	Level 3	Total
Financial assets				
Net advances*	-	-	1 855	1 855
Total	-	-	1 855	1 855
Financial liabilities				
Stub instruments	-	-	**	-
Total	-	-	-	-

*Included in the net advances fair value is the fair value of the written off book of R1billion (September 2018: R1.1billion).

** Please refer above for disclosure on the fair value of the stub instruments.

10. Other matters

Current Tax Asset

The Company has open tax matters with the South African Revenue Services (SARS) relating to the deductibility of impairment provisions on the Company's advances book and the application of SARS's directive regarding the treatment of doubtful debts by banks.

The Company is of the view that a tax asset cannot be recognised because of the uncertainty around the resolution of this matter as negotiations with SARS remain ongoing and have advanced to an appeal stage with the courts. This dispute is with respect of amounts already paid to SARS. The Company continues to pursue this matter, however, the ultimate conclusion of this matter could vary as it is dependent upon the outcome of the negotiations with SARS. During this dispute process, SARS reduced its initial assessment issued by the penalties and interest. This receivable was recognised as it is not dependent on the outcome of the court case. Aside from legal costs payable to legal advisors, there are no payments expected to be made to SARS by the Company.

Due to the losses in the prior financial years and the expectation that these losses will persist for the near future, the Company deemed it improbable that sufficient taxable profit will be available against which the deferred tax asset will be recoverable. Therefore, the Company has not recognised a deferred tax asset because of the losses incurred during the previous financial periods.

Given the uncertainty for the basis on which to claim an allowance for doubtful debt and the fact that this basis will only be determined by the outcome of the engagement with SARS, the IT14 income tax returns for preceding years of assessment have not been submitted. All provisional IRP6 income tax returns due have however been submitted, notifying SARS of the taxable loss position. The late submission of the IT14 income tax returns may give rise to penalties and or interest to be raised by SARS, however SARS have not raised such penalties or interest at the date of these financial statements.

SARB Indemnity Guarantee

As at 31 March 2019, the indemnity reserve fund of R3 billion remains fully funded, as well as the additional R500 million operational float. The Curator has been making 6-monthly distributions of the surplus funds collected by the Company to the holders of the stub instruments in accordance with the terms of such instruments.

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Gilt Edged Management Services Pty Limited (“GEMS”) contingent liability

The Company has a contingent liability to clients, as a result of a court order issued in 2004, to pay reparations to clients who might have been prejudiced by actions of Gilt Edged Management Services Pty Limited (“GEMS”), a related party of the old African Bank Limited, between 1999 and 2002. The terms of the court order require each client to sign an acceptance and waiver form before the settlement can be made. In terms of the court order the maximum amount of potential reparations was R60.1 million, of which in excess of R40.0 million was paid by the end of September 2006. Subsequent to September 2006, a marginal amount of R0.2 million of reparations was paid to GEMS clients. The Company has a remaining contingent liability of R20 million (2018: R20 million) for these reparations.

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Addendum A

Significant accounting policies

Financial instruments

The Company recognises financial assets and liabilities when it becomes a party to the terms of the contract, which is the trade date or the settlement date.

The Company has financial assets classified into the following categories:

- loans and receivables

The Company has financial liabilities classified into the following categories:

- financial liabilities at amortised cost.

The classification of financial assets and financial liabilities depends on the nature and purpose of the financial instrument and is determined at the time of initial recognition.

Initial measurement

All financial instruments are measured initially at fair value plus transaction costs, except for stub instruments. Financial liabilities arising from the issue of stub instruments are recognised at their face value upon initial recognition.

Subsequent measurement

Subsequent to initial measurement, financial instruments are measured at amortised cost.

- Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market.

The Company's advances are included in the loans and receivable category.

These advances arise when the Company provides money, goods or services directly to a debtor with no intention to trade the receivable. Loans and advances originated by the Company are in the form of personal unsecured loans and are either paid back in fixed equal instalments or, in the case of credit cards, are revolving credit facilities.

Advances are classified as loans and receivables and are measured at amortised cost using the effective interest rate method, less any impairment losses through the use of an allowance account whereby the amount of the losses are recognised in profit or loss. Origination fees and monthly service fees that are integral to the effective interest rate are capitalised to the value of the loan and amortised to profit or loss over the contractual life of the loan using the effective interest rate method.

- Financial liabilities at amortised cost

All financial liabilities are measured at amortised cost.

Effective interest method

The effective interest method is a method of calculating the amortised cost of a financial asset or liability and of allocating interest income or expense over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash receipts/payments (including all fees that form an integral part of the effective interest rate) through the expected life of the financial asset/liability or, where appropriate, a shorter period. Where a change in estimation of expected future cash flows occurs on fixed rate instruments, the change in estimate calculated is recognised as part of interest income/expense.

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Impairment of financial instruments

Assets carried at amortised cost

The Company assesses at each reporting date whether there is objective evidence that an asset or group of assets is impaired.

The Company reviews the carrying amounts of its loans and advances to determine whether there is any indication that those loans and advances have become impaired using objective evidence at a loan level. A loan or receivable is impaired and impairment losses are incurred if, and only if, there is objective evidence of impairment as a result of one or more events that occurred after the initial recognition of the asset (a “loss event”) and that loss event(s) has an adverse impact on the estimated future cash flows of the financial asset or group of financial assets that can be reliably estimated. Losses expected as a result of future events, no matter how likely, are not recognised. Objective evidence that a financial asset or group of assets is impaired includes observable data that comes to the attention of the holder of the asset about the following loss events:

- significant financial difficulty of the issuer or debtor;
- a breach of contract, such as a default or delinquency in the payment of interest or principal;
- the lender, for economic or legal reasons relating to the borrower’s financial difficulty, granting to the borrower a concession that the lender would not otherwise consider;
- it becoming probable that the borrower is over-indebted;
- indication that there is a measurable decrease in the estimated future cash flows from a group of financial assets since the initial recognition of those assets, although the decrease cannot yet be identified with the individual financial assets in the group, including:
 - adverse changes in the payment status of borrowers in the group (e.g. an increased number of delayed payments or an increased number of credit card borrowers who have reached their credit limit and are paying less than the minimum monthly amount); or
 - national or local economic conditions that correlate with defaults on the assets in the group (e.g. an increase in the unemployment rate in the geographical area of the borrowers or adverse changes in industry conditions that affect the borrowers in the group).

If there is objective evidence that an impairment loss has been incurred, the amount of the loss is measured as the difference between the financial assets’ carrying amount and the recoverable amount.

The recoverable amount is the sum of the estimated future cash flows, discounted to their present value using a discount rate that reflects the portfolio of advance’s original effective interest rate. The effective interest method is a method of calculating the amortised cost and of allocating interest income over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash receipts (including loan origination fees and monthly service fees) through the expected life of the loan, or, where appropriate, a shorter period, to the net carrying amount on initial recognition.

The carrying amount of the financial asset due to the impairment calculated is reduced through the use of an allowance account and the amount of the loss is recognised in the credit impairment charge line of the statement of total comprehensive income.

Where an impairment loss subsequently reverses, the carrying amount of the advance is increased to the revised estimate of its recoverable amount, but so that the increased carrying amount does not exceed the carrying amount that would have been determined had no impairment loss been recognised for the advance in prior years. A reversal of an impairment loss is immediately recognised in profit or loss.

Currently, all advances are assessed for impairment on a portfolio basis due to the large number of insignificant balances within the portfolio.

The Company estimates the recoverable amount on a portfolio basis using portfolio statistics derived from past performance of similar financial assets, taking into account any changes to collection procedures and projected future market conditions.

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For portfolio (collective) assessment of impairment, financial assets are grouped on the basis of similar credit characteristics which indicate the borrower's ability to pay in accordance with the contractually agreed terms. For the purposes of portfolio impairment assessment, the impairment provisioning is divided into the following categories:

- Provision for IBNR (incurred but not yet reported);
- Portfolio specific impairments;
- Specific impairments; and
- Written off portfolio.

Provision for IBNR

In order to provide for the latent losses in a group of loans that have not yet been identified as specifically impaired, an impairment for incurred but not yet reported ("IBNR") losses is recognised on historical loss patterns and estimated emergence periods. Loans and receivables that are neither past due nor impaired are collectively assessed for the IBNR impairment provision. Neither past due nor impaired is defined by the Company as loans and receivables that are contractually up to date with all payments due.

Portfolio specific impairments

Loans and receivables that have missed up to 3 payments contractually are assessed collectively for portfolio specific impairment provisioning. These loans are still considered to be part of the performing loan portfolio.

Specific impairments

Loans and receivables that have missed 4 or more instalments are assessed for specific impairments. These loans form the non-performing loan portfolio.

Written off portfolio

A write off is effected against the allowance account (effectively derecognised) when the debtor is deemed to be impaired and not recoverable. Any cash subsequently recovered from the debtor is recorded as bad debt recovered and included in the credit impairment charge in the statement of total comprehensive income.

Derecognition of financial instruments

Financial assets

The Company derecognises a financial asset (or group of financial assets) or a part of a financial asset (or part of a group of financial assets) when the contractual rights to the cash flows arising from the financial asset have expired or the Company transfers the financial asset and the transfer qualifies for de-recognition.

A transfer of the financial assets requires that the Company either transfers the contractual rights to receive the cash flows of the financial asset or retains the contractual rights to receive the cash flows of the financial asset, but assumes a corresponding contractual obligation to pay the cash flows to one or more recipients, and consequently transfers substantially all the risks and benefits associated with the asset.

On derecognition of a financial asset in its entirety, the difference between the asset's carrying amount and the sum of the consideration received and receivable and the cumulative gain or loss that had been recognised in other comprehensive income and accumulated in equity is recognised in profit or loss.

On derecognition of a financial asset other than in its entirety (e.g. when the Company retains an option to repurchase part of a transferred asset), the Company allocates the previous carrying amount of the financial asset between the part it continues to recognise under continuing involvement, and the part it no longer recognises on the basis of the relative fair values of those parts on the date of the transfer. The difference between the carrying amount allocated to the part that is no longer recognised and the sum of the consideration received for the part no longer recognised and any cumulative gain or loss allocated to it that had been recognised in other comprehensive income is recognised in profit or loss. A cumulative gain or loss that had been recognised in other comprehensive income is allocated between the part that continues to be recognised and the part that is no longer recognised on the basis of the relative fair values of those parts.

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Financial liabilities

The Company derecognises a financial liability when the obligation specified in the contract is discharged, cancelled or expired. A substantial modification to the terms and conditions of an existing financial liability or part of an existing financial liability is accounted for as an extinguishment of the original financial liability and recognition of a new financial liability. A substantial modification to the terms occurs where the discounted present value of the cash flows under the new terms, including any fees paid net of any fees received and discounted using the original effective interest rate, is at least 10 percent different from the discounted present value of the remaining cash flows of the original financial liability.

Where the Company purchases its own debt, the debt is derecognised from the statement of financial position and any difference between the carrying amount of the liability and the consideration paid is included in gains or losses on bond buy backs in the statement of total comprehensive income.

Offsetting

Financial assets and liabilities are offset and the net amount reported only when a legally enforceable right to set off the recognised amount exists and there is an intention to either settle on a net basis, or to realise the asset and settle the liability simultaneously. Income and expense items are offset only to the extent that their related instruments have been offset in the statement of financial position.

Cash and cash equivalents

Short-term deposits and cash comprise fixed and notice deposits as well as call and current accounts with financial institutions that have a maturity of less than three months from date of acquisition.

For the purposes of the statement of cash flows, cash and cash equivalents comprise short-term deposits and cash, net of bank overdrafts.

Provisions

Provisions represent liabilities of uncertain timing or amount and are measured at the expenditure or cash outflow required to settle the present obligation.

Provisions are recognised when the Company has a present legal or constructive obligation, as a result of past events, for which it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate can be made for the amount of the obligation.

Equity

Equity is the residual interest in the assets of the Company after deducting all liabilities of the Company.

All transactions relating to the acquisition and sale or issue of shares in the Company, together with their associated costs, are accounted for in equity.

Share capital and share premium

Shares issued by the Company are recorded at the value of the proceeds received less the external costs directly attributable to the issue of the shares.

Dividends

Dividends to equity holders are recognised as a liability in the period in which they are declared and are accounted for as a movement in reserves in the statement of changes in equity. Dividends declared after the statement of financial position date are not recognised.

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Revenue

Revenue comprises income from interest income and non-interest income.

Interest income

Interest income is accrued on a yield to maturity basis by reference to the principal outstanding and the interest rate applicable.

- Origination fees on loans granted

Origination fees on loans granted are charged upfront and capitalised into the loan. These fees are primarily based on the cost of granting the loan to the individual. These origination fees are considered an integral part of the loan agreement and are therefore recognised as an integral part of the effective interest rate and are accounted for over the shorter of the original contractual term and the actual term of the loan using the effective interest rate method. The deferred portion of the fees is recorded in the statement of financial position as a provision for deferred administration fees.

- Monthly service fee

Monthly service fees are the fees which form an integral part of the effective interest rate and are charged to the customers on a monthly basis. These fees are recognised as part of the effective interest rate over the shorter of the original contractual term and the actual term of the loans and receivables. Beyond the original contractual term of the loan, the fee is recognised in profit or loss as it is charged to the customer on a monthly basis.

Non-interest income

- Rendering of services

When the transaction involves the rendering of services and the outcome can be estimated reliably, revenue associated with the transaction is recognised by reference to the stage of completion of the transaction at the reporting date. The outcome of a transaction can be estimated reliably when all the following conditions are satisfied:

- the amount of revenue can be measured reliably;
- it is probable that the economic benefits associated with the transaction will flow to the entity;
- the stage of completion of the transaction at the reporting date can be measured reliably; and
- the costs incurred for the transaction and the costs to complete the transaction can be measured reliably.

- Other income

Other income consists primarily of administration fees on loans and advances, commission charged as well as any other sundry income.

Taxation

Indirect taxation

Indirect taxation in the form of non-claimable value-added tax (VAT) on expenses is disclosed as indirect taxation in profit or loss and not as part of the taxation charge. The net amount of VAT recoverable from, or payable to, the taxation authority is included as part of the receivables or payables in the statement of financial position.

Direct taxation

Direct taxation in profit or loss consists of South African jurisdiction corporate income tax, inclusive of capital gains tax (CGT) (currently payable, prior year adjustments and deferred).

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Current taxation

Current taxation is the expected taxation payable based on the taxable income, inclusive of capital gains tax, for the year, using taxation rates enacted or substantially enacted at the statement of financial position date, and any adjustment to taxation payable in respect of previous years. Taxable income is determined by adjusting the profit before taxation for items which are non-taxable or disallowed in terms of tax legislation. Current tax is charged or credited to profit or loss, except to the extent that it relates to items charged or credited directly to the statement of changes in equity, in which case the tax is also dealt with in equity.

Deferred taxation

Deferred taxation is provided on temporary differences using the balance sheet liability method. Temporary differences are differences between the carrying amounts of assets and liabilities for financial reporting purposes and their taxation base. However, deferred taxation is not accounted for if it arises from initial recognition of an asset or liability in a transaction other than a business combination that at the time of the transaction affects neither accounting profit or loss nor taxable income. Deferred tax assets and liabilities are measured at the tax rates that are expected to apply to the period when the asset is realised or the liability is settled, based on tax rates (and tax laws) that have been enacted or substantively enacted by the end of the reporting period.

Deferred taxation is charged or credited in profit or loss, except to the extent that it relates to items charged or credited directly to the statement of changes in equity, in which case the deferred taxation is also dealt with in equity.

The effect on deferred taxation of any changes in taxation rates is recognised in profit or loss, except to the extent that it relates to items previously charged or credited directly to equity.

The deferred taxation related to the fair value re-measurement of available-for-sale investments and cash flow hedges, which are charged or credited to other comprehensive income, and accumulated in equity is also credited or charged to other comprehensive income and is subsequently recognised in profit or loss together with the deferred gain or loss.

Deferred tax assets are recognised on the tax effects of income tax losses available for carry-forward, if the Company considers it probable that future taxable income will be available against which the unused tax losses can be utilised. The carrying amount of deferred tax assets is reviewed at each statement of financial position date and reduced to the extent that it is no longer probable that sufficient taxable profit will be available to allow all or part of the deferred tax asset to be recovered. Unrecognised deferred tax assets are reassessed at each reporting date and are recognised to the extent that it has become probable that future taxable profit will allow the deferred tax asset to be recovered.

Deferred tax liabilities are recognised for all taxable temporary differences. Deferred income tax assets and deferred income tax liabilities are offset, if a legally enforceable right exists to set off current income tax assets against current income tax liabilities and the deferred income taxes relate to the same taxable entity and the same taxation authority.

Contingent liabilities and commitments

Contingent liabilities

A contingent liability is disclosed when:

- a possible obligation arising from past events, the existence of which will be confirmed only by the occurrence or non-occurrence of one or more uncertain future events that are not wholly within the control of the Company; or
- the Company has a present obligation that arises from past events but it is not recognised because it is not probable that an outflow of resources will be required to settle such obligation or the amount of the obligation cannot be measured with sufficient reliability.

Commitments

Items are classified as commitments where the Company has committed itself at the reporting date to future significant transactions or the acquisition of assets for material amounts.

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Comparative figures

Where necessary, comparative figures within notes have been reclassified to conform to changes in presentation in the current year and to enhance disclosure of certain items. Any reclassifications have been further explained or detailed in the interim financial statements (including the notes thereto as applicable).

Forthcoming accounting standards

To achieve fair presentation as envisaged in the Framework, the curator will endeavour to align accounting standards adopted in the industry in the future to the financial reporting of Residual Debt Services Limited (under curatorship).

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CORPORATE INFORMATION

Company Secretary

Maliga Chetty

Residual Debt Services Limited

Incorporated in the Republic of South Africa

Registration number 1975/002526/06

NCR Registration number: NCRCP5

Residual Debt Services Limited (under curatorship) is an Authorised Financial Services and Registered Credit Provider

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