

BAD DEBTS AND HOW TO AVOID THEM!

some helpful tips from



During the current economic slowdown, more and more business clients are conscious of the risk of incurring bad debts with their clients. With this in mind there are a few useful tips that can be adopted by most businesses, which incur little or no cost, that may save the time and expense incurred in respect of a bad debt.

INITIAL STEPS – KNOW YOUR CUSTOMER

It is always important to know who your customer is. For those businesses dealing with Limited Companies, it may be worth undertaking a straight forward search for around £20.00 at Companies House to ascertain the financial viability of your potential customer. Information that can be obtained from Companies House includes the last set of filed accounts and indeed whether or not accounts have been filed at all in relation to the Company. This information will easily allow those accessing this information to ascertain whether or not the Company that they are dealing with is financially viable and can pay your invoices.

PERSONAL GUARANTEES

When entering into large contracts involving Limited Companies, you must also consider obtaining a Personal Guarantee from the Directors of the Company in relation to your invoices. Personal Guarantees by Directors is also something that can be included in your Terms and Conditions of Business. Personal Guarantees can be drafted by MacLachlan Solicitors.

TERMS AND CONDITIONS OF BUSINESS

It is essential that Terms and Conditions are provided to your customers setting out the contractual relationship between you.

These should highlight:

- a) terms of payment
- b) interest rates to be charged in respect of late payment
- c) title to goods delivered
- d) a Directors Guarantee
- e) stage payments
- f) your obligations
- g) your client's obligations

A set of clearly drafted Terms and Conditions of Business, setting out the contract between both parties leaves little scope for a customer to contest an invoice for work undertaken or goods delivered. Professionally drafted Terms and Conditions of Business are not as expensive as you may think ranging from £350.00 to £500.00 from MacLachlan Solicitors.

It should also be remembered that the award of interest on an aged debt by the Court is subject to the Courts discretion, but if the payment of interest is a contractual term contained in Terms and Conditions of Business, the Court is duty bound to award interest on outstanding accounts. Terms and Conditions of Business can be easily drafted and once prepared can be used for all of your businesses dealings with clients and customers with little or no modification for each piece of work that you undertake or for the goods you supply.

SUMS ON ACCOUNT AND STAGE PAYMENTS

Do not be afraid to ask for a sum of money on account of costs, especially in relation to any goods or materials being provided. For large contracts stage payments should be agreed and recorded in writing in either Terms and Conditions of Business or in correspondence with the customer. The failure to pay a stage payment, or the failure to pay for goods or materials in advance, is always an indicator that a client may be facing financial difficulty.

The benefit of using payments in advance and stage payments is that rather than incurring the cost of the entire contract, your losses can be capped at a smaller figure, if it is found that a customer is reluctant or unable to pay in advance or by way of stage payments.

DEBT COLLECTION LETTERS

Once a customer has fallen into arrears, the further provision of goods and services should cease immediately. Many businesses fall into the trap that they continue to provide goods and services to a customer, whilst the client's account with your business is in substantial arrears. Further goods and services are often elicited by the customer by promises of payment.

Invoices must be diarised for payment and a procedure adopted for debt collection as follows:

- a) A reminder letter should be sent reminding the client that their account is in arrears. This can be a gentle reminder informing them that payment is now due.
- b) Shortly thereafter, a second letter should be sent which is slightly stronger in its wording and includes a sum for interest incurred both in total and at a daily rate on the outstanding sum.
- c) Finally, the last letter to be sent is what is termed a "letter before action" which is the threat of Court proceedings.

If these fail to work, depending on the size of the debt, it may be worth the cost of a Solicitor's letter, which often does the trick. MacLachlan charge £85.00 plus V.A.T for a debt collection letter having taken instructions from a client, threatening imminent legal action. Frequently, debtors will pay having received a Solicitors letter.

COURT PROCEEDINGS

a) Small Claims

Small claims for debts of under **£5,000.00**, using the “Claims Online Service” through either the Northampton County Court or your local County Court. Before embarking upon Court proceedings however, it is always worthwhile obtaining some initial legal advice on procedure and your prospects of success. MacLachlan offer a fixed fee interview of up to an hour plus an advice letter for £130.00 plus V.A.T. Also try to ascertain whether the customer is actually “good for the money”. What a business must try to avoid is spending more time and money pursuing Court proceedings in the Small Claims Court when they have little or no prospect of being paid by the customer because it is either a Limited Company with no assets or if dealing with a Partnership or Sole Trader, the individual or Partners concerned in the business have no income or assets and may already be heading towards bankruptcy.

The protocol in relation to the award of costs incurred in Small Claims Proceedings of under £5,000.00 is that a winning party will only obtain reimbursement of the Court fees and out of pocket expenses incurred in attending the Small Claims Hearing. Often it is cheaper and easier to obtain advice from MacLachlan before embarking on a claim.

b) Other claims

The issue of Court proceedings for sums of **more than £5,000.00** can be fraught with danger, in view of the fact that the procedure is more formal and there are costs consequences for the unwary or inexperienced. Should your business be in the unfortunate position that it is owed more than £5,000.00, legal advice should be sought from the outset. This also includes other enforcement action, especially the service of a Statutory Demand on either a company or individual. Significant costs can be incurred by a creditor if the incorrect procedure is embarked upon.

CONCLUSION

The trick from the outset for many businesses is to seek to avoid incurring bad debts. Most of the above outlines reasonably simple and cost effective measures and procedures that can be put in place by businesses to avoid bad debts being incurred and from this aspect prevention rather than cure is the best possible and least costly approach.

For further advice please contact MacLachlan Solicitors - Sherborne 01935 817736 and Gillingham 01747 822103.

Mark Griffin

MacLachlan Solicitors

www.maclachlansolicitors.co.uk

