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## CREDIT MANAGEMENT AND DEBT RECOVERY

Cash flow management has become a grave concern in recent times with credit and debit control a critical part of business. Businesses must now have a competent credit management strategy.

The purpose of this article is to provide an introduction to our corporate recovery practice and how this could assist you in times of economic turmoil.

### The Symptoms of Indebtedness

Watch for symptoms of indebtedness such as:

- the debtor failing to pay by the due date;
- diminishing communication between the debtor and you;
- increasingly implausible excuses;
- proposals for restructuring the debt; and
- signs of poor organisational and/or financial management.

### Bad Debt Prevention

#### **Records**

It is important to keep accurate and detailed records of all your contact with debtors.

#### **Terms and Conditions**

Terms and conditions are seldom given the critical examination that they deserve. Typically, the sale of products and services are accompanied by terms and conditions of sale. As a producer or seller, you must be able to spot issues that may have a detrimental effect on your business.

Warranty exclusions, remedy limitations and indemnification language are only a few possible points of concern. After a contract is formed regardless of whether it's written or oral a "battle of the forms" can ensue when two companies trade purchase orders and sales proposals or confirmations with preprinted terms and conditions. Each company's form will contain terms and conditions, many of which are contradictory to those of the other party.

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Consideration should be given to the inclusion of a Terms of Payment clause in your standard terms and conditions containing the following provisions:

- that prices are as set out in any schedule to a contract;
- that prices can be varied;
- the inclusion of VAT;
- that the term or length of credit can be extended;
- the payment of interest in the event of late payment.



If you are a seller, insist on written agreements, either in the form of a formal contract or a purchase order and use a process that ensures that the other party acknowledges in writing that your terms and conditions supersede their terms and conditions.

If you are the buyer, use a process that ensures that you know what terms and conditions are governing your agreement to buy.

### **Credit Application Form**

A Credit Application Form should be introduced to your business as standard procedure. This should be completed and signed by both parties before credit is extended and include all pertinent information about the customer, as well as the terms and conditions agreed (as above). Information should be assessed to identify whether they are creditworthy.

### **Director Guarantees**

It is becoming common place where goods or services are being provided to a limited liability company that the supplier will insist on a personal guarantee from the director of the company.

### **Mareva Injunction**

If successful, an order can be acquired in relation to specific assets of a debtor and prohibit the debtor from reducing assets below a certain level. This occurs where there is likelihood that a debtor may sell assets in such a way as to defeat any future judgment. This is a complex and expensive process.

## **Pursuit of a Debtor**

### **Solicitors Letter**

Before any legal proceedings are initiated it is important that a demand letter is sent by a solicitor. This will state the amount owing, what it relates to, if the amount continues to accrue, the rate of accrual, payment to be made within a specified time period and that legal proceedings will be initiated if payment is not received within the specified time.

### **Commercial Reality**

Prior to embarking on the full legal process it is prudent to assess the likelihood of success and whether, or not, the case will be contested. These factors will have an impact on the length of time it takes to resolve the matter and more importantly to you, the cost and management time involved.

### **Court Action**

Once the above points have been considered a debt can be collected through the judicial system in Ireland in one of the 3 courts.

## **District Court**

Where the claim does not exceed €6,349.00.

### **Uncontested**

- Civil Summons is served on the debtor;
- An Affidavit of debt is sworn by you the creditor;
- The Affidavit is filed in the Court office;
- Judgment is awarded.



### Contested

- Civil Summons is served on the debtor;
- The debtor files a Notice of Intention to Defend;
- The creditor and debtor put their cases to the judge orally under oath;
- If successful, you the creditor will receive a judgment.

### Circuit Court

Where the claim is above €6,349.00 and does not exceed €38,092.00.

### Uncontested

This is similar to the District Court process, that is, if uncontested, no Court hearing takes place and a judgment issues on receipt of the Affidavit of Debt in the Court office, sworn by you, the creditor.

### Contested

- Civil Bill is served on the debtor;
- An Appearance is submitted by the debtor with a written Defence;
- A Notice of Trial is issued by the Court;
- A Court hearing is conducted.

### High Court

For all other claims other than that of the Commercial Court over €38,092.00. The Commercial Court is for claims over 1 million euro.

### Uncontested

If uncontested, no court hearing takes place and a judgment issues in the same process as with the District and Circuit courts.

### Contested

- A Summary Summons is served on the debtor;
- The debtor responds by entering an appearance;
- The creditor must apply for judgment to the master of the High Court. The creditor and the debtor make their cases by Affidavit and the master may decide in favour of either.

### **Interest**

For business to business contracts entered into after the 8th August, 2002, EU Regulations now allow for interest to be charged on all payments after 30 days have lapsed at a rate of interest linked to the European Central Bank (ECB) base rate.

Interest is charged on the gross amount of the debt including VAT. The ECB base rate is applied plus 7%. The ECB rates in force on January 1<sup>st</sup> and July 1<sup>st</sup> apply for the following 6 months in each year. From the 1<sup>st</sup> January 2009, the late payment interest rate is 9.5% per annum (that is based on the ECB rate of 2.5% plus the margin of 7%). That rate equates to a daily rate of 0.026%. Penalty interest due for late payments should be calculated on a daily basis. The ECB rate fell to 1.25% in April 2009, however, the late payment interest rate will not change until 1<sup>st</sup> July 2009.

In addition to interest, suppliers may claim compensation for the recovery costs of the debt if such costs arise.



The Regulations will not apply:

- where the regulations are excluded specifically and in a fair manner;
- where a consumer is a party to the transaction;
- where debt is subject to statutory proceedings;
- where there has been incomplete performance or a breach of contract by the supplier.

## Enforcement

The obtaining of a judgment does not guarantee the collection of the debt and you may have to follow this with an enforcement action such as:

### (i) *Against Companies:*

**Registration:** Judgments of the High Court, Circuit Court and the District Court can be registered in the Judgments Office of the High Court. The main consequence of registration of a judgment is publicity, as once registered, judgments are published in the Experian, All Ireland Gazette, Stubbs Gazette and various commercial databases.

**The Sheriff:** A judgment can be sent to the county sheriff with a request that he attend at the defendant's premises and either collect the debt or remove and dispose of sufficient assets to discharge the debt.

**Garnishee Orders:** Where a judgment creditor knows that a third party owes his judgment debtor monies the creditor can apply to the court for an order that the third party pay the creditor the monies due.

**Equitable Execution:** This is a similar process to the Garnishee Order, except the ultimate objective is for the creditor to receive the net sale proceeds of an asset belonging to the debtor.

**Judgment Mortgage:** Once the judgment has been obtained, the creditor can apply in Court to have a Judgment Mortgage registered against the debtor's property. This registration creates a statutory mortgage against the lands of the judgment debtor but is subject to the rules on priorities. If the bank or another third party has a charge over the lands then there may not be much point in pursuing this option.

**Liquidations:** To pursue the repayment of a debt from a limited company one of the options open to the creditor is to wind-up the company. This must involve debts over €1,269.74 unsecured and not disputed. To avoid spurious defences and the disapproval of the High Court, it is advisable to obtain a judgment beforehand, or at the very least, a written confirmation from the debtor company admitting the debt. There are a number of grounds set out in section 213 Companies Act, 1963 upon which the High Court may wind up a company, however, the ground most frequently relied upon is "*the company is unable to pay its debts*". This may seem a simple procedure, however, the courts do not grant such petitions lightly and frown upon this procedure being used as a debt collection tool. If such a petition is granted and the court appoints an official liquidator, the assets are distributed as follows:

- (i) Preferential creditors;
- (ii) Floating chargers;
- (iii) Unsecured creditors;
- (iv) Members.

This is a very expensive process and unfortunately, in the majority of liquidations, there are little or no funds left to satisfy the claims of unsecured creditors. Quite often the liquidation process might only end up paying the liquidator fees.



*(ii) Against Individuals:*

**Examination Order:** The debtor may be required to attend in court and be cross examined as to his financial circumstances.

**A Committal Order:** If the debtor defaults in making payments as directed by the court then the creditor can apply for a committal order to have the defendant committed to prison for non payment.

**Bankruptcy:** Bankruptcy proceedings may only be brought in the High Court and must involve debts over €1,905.00 unsecured and not disputed. To avoid a debtor or indeed a judge questioning a debt it is advisable to first obtain a judgment against the debtor. Once adjudicated a bankrupt, the affairs and property of the bankrupt are transferred to an official assignee. It is possible for a creditor to appoint their own trustee in bankruptcy following the appropriate court application and procedure. Again this is a very expensive and time consuming process.

**Legal Costs**

Costs awarded to creditors are generally low, unless the case is defended. This will also vary depending on the amount due and the Court.

As the recession takes hold there is an ever increasing likelihood that your company and indeed individuals will be involved in disputes, whether this is in the pursuit of money from a struggling debtor or simply unwarranted claims from creditors.

**Conclusion**

For any business a key element in the profitability equation is the prompt collection of cash due. We recommend to our business clients that they proactively manage and monitor their business debtors, making sure their paperwork is in good order so as to avoid having to become involved in unnecessary legal proceedings.

If you have any questions in relation to the above or would like advice on a related matter please contact Julian Cunningham or any member of the firm.