

# CREDIT MANAGEMENT

## STUDY TEXT

### **Qualifications and Credit Framework**

**AQ2016**

This Study Text supports study for the following AAT qualifications:

AAT Professional Diploma in Accounting – Level 4

AAT Level 4 Diploma in Business Skills

AAT Professional Diploma in Accounting at SCQF – Level 8

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## STUDY TEXT

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# INTRODUCTION

## HOW TO USE THESE MATERIALS

These Kaplan Publishing learning materials have been carefully designed to make your learning experience as easy as possible and to give you the best chance of success in your AAT assessments.

They contain a number of features to help you in the study process.

The sections on the Unit Guide, the Assessment and Study Skills should be read before you commence your studies.

They are designed to familiarise you with the nature and content of the assessment and to give you tips on how best to approach your studies.

## STUDY TEXT

This study text has been specially prepared for the revised AAT qualification introduced in September 2016.

It is written in a practical and interactive style:

- key terms and concepts are clearly defined
- all topics are illustrated with practical examples with clearly worked solutions based on sample tasks provided by the AAT in the new examining style
- frequent activities throughout the chapters ensure that what you have learnt is regularly reinforced
- 'pitfalls' and 'examination tips' help you avoid commonly made mistakes and help you focus on what is required to perform well in your examination
- 'Test your understanding' activities are included within each chapter to apply your learning and develop your understanding.

## ICONS

The study chapters include the following icons throughout.

They are designed to assist you in your studies by identifying key definitions and the points at which you can test yourself on the knowledge gained.



### Definition

These sections explain important areas of knowledge which must be understood and reproduced in an assessment.



### Example

The illustrative examples can be used to help develop an understanding of topics before attempting the activity exercises.



### Test your understanding

These are exercises which give the opportunity to assess your understanding of all the assessment areas.

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Our Quality Co-ordinator will work with our technical team to verify the error and take action to ensure it is corrected in future editions.

## Progression

There are two elements of progression that we can measure: first how quickly students move through individual topics within a subject; and second how quickly they move from one course to the next. We know that there is an optimum for both, but it can vary from subject to subject and from student to student. However, using data and our experience of student performance over many years, we can make some generalisations.

A fixed period of study set out at the start of a course with key milestones is important. This can be within a subject, for example 'I will finish this topic by 30 June', or for overall achievement, such as 'I want to be qualified by the end of next year'.

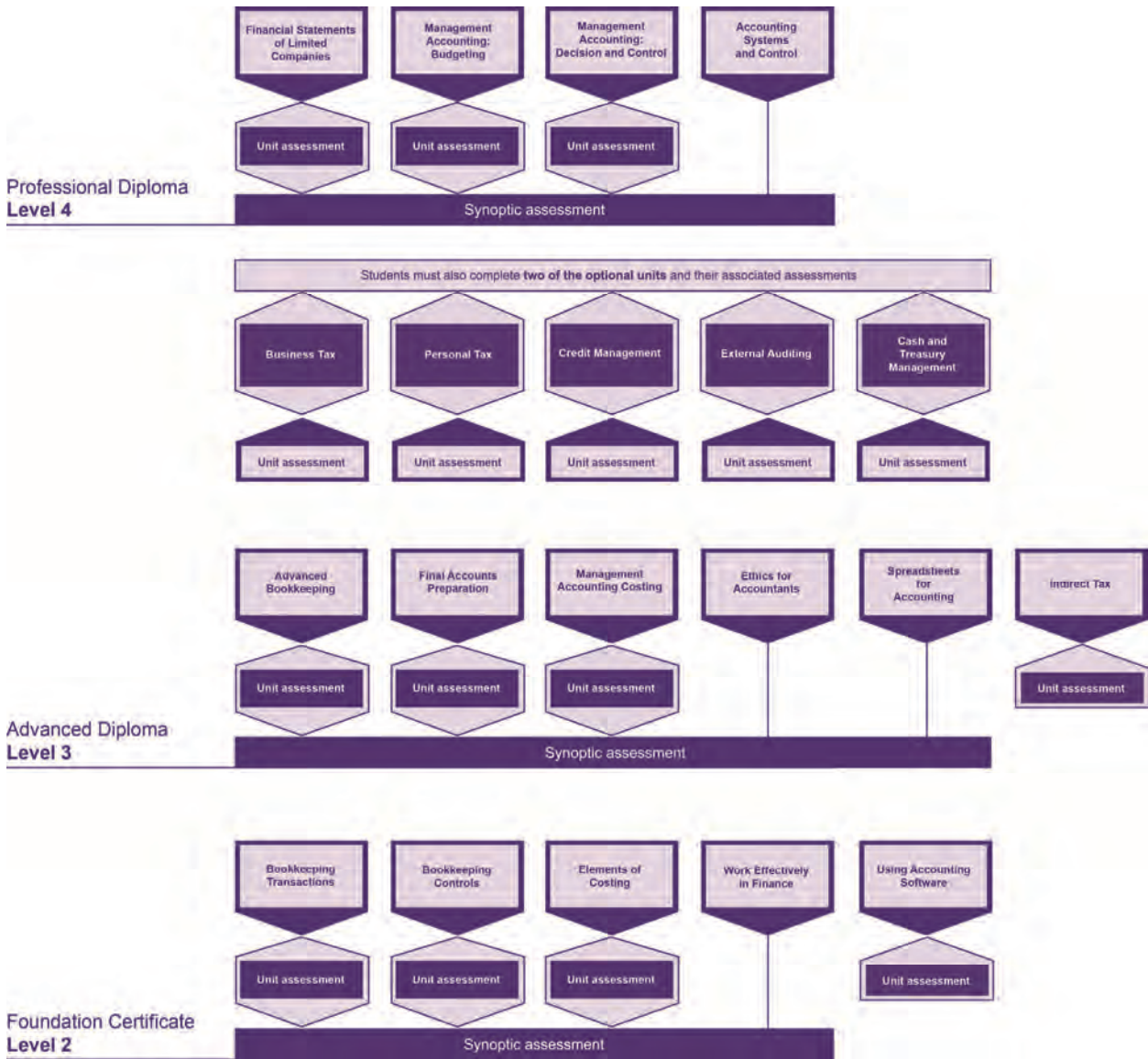
Your qualification is cumulative, as earlier papers provide a foundation for your subsequent studies, so do not allow there to be too big a gap between one subject and another.

We know that exams encourage techniques that lead to some degree of short term retention, the result being that you will simply forget much of what you have already learned unless it is refreshed (look up Ebbinghaus Forgetting Curve for more details on this). This makes it more difficult as you move from one subject to another: not only will you have to learn the new subject, you will also have to relearn all the underpinning knowledge as well. This is very inefficient and slows down your overall progression which makes it more likely you may not succeed at all.

In addition, delaying your studies slows your path to qualification which can have negative impacts on your career, postponing the opportunity to apply for higher level positions and therefore higher pay.

You can use the following diagram showing the whole structure of your qualification to help you keep track of your progress.

# CREDIT MANAGEMENT



# UNIT GUIDE

## Introduction

This unit is about understanding and applying the principles of effective credit control in an organisation.

Students will require an understanding of the principles of credit control in the context of relevant legislation, contract law, best practice, professional ethics and organisational policies. Students will also be able to describe remedies for breach of contract, as well as the terms and conditions of contracts with customers.

Students will gain knowledge of sources of information and techniques used to assess credit risks in compliance with organisational policies, data protection legislation and professional ethics. Knowledge and application of performance measures relating to liquidity, profitability and gearing will be fundamental to this unit.

Legal procedures and methods for collecting debts, as well as financial techniques used in granting and monitoring credit and debtors, will need to be understood and demonstrated. An understanding of different types of discounts will also be required.

Students will apply their skills to monitoring and evaluating credit control in compliance with organisational policies and, in particular, will learn the importance of liquidity management. Knowledge of bankruptcies and insolvencies will be required, as well as of the mechanisms of invoice discounting, factoring and credit insurance.

Students will be expected to demonstrate their ability to present advice and recommendations in line with organisational policies in a professional manner, including for write-offs and provisions. The financial impact of decisions taken and recommendations given will be essential skills required of the student.

Credit Management is an **optional** unit.



### Learning outcomes

- Analyse relevant legislation and contract law that has an impact on the credit control environment.
- Critically analyse information from a variety of sources to assess credit risk and grant credit in compliance with organisational policies and procedures.
- Evaluate a range of techniques to collect debts.
- Critically evaluate credit control in line with organisational policies and procedures.
- Present advice and recommendations to management on the credit control system.

Delivering this unit

| Unit name                                 | Content links  | Suggested order of delivery   |
|---|--|---|
| Financial Statements of Limited Companies | Credit Management links with Financial Statements of Limited Companies | Ideally, Credit Management should be taken at the same time as or after Financial Statements of Limited Companies |

# THE ASSESSMENT

## Test specifications for this unit assessment

|                                |   |                         |
|--------------------------------|---|-------------------------|
| <b>Assessment type</b>         | <b>Marking type</b>                           | <b>Duration of exam</b> |
| Computer based unit assessment | Partially computer/<br>partially human marked | 2 hours 30 minutes      |

| <b>Learning outcomes</b> |  | <b>Weighting</b> |
|--------------------------|--|------------------|
| 1                        | Analyse relevant legislation and contract law that has an impact on the credit control environment.  | 15%              |
| 2                        | Critically analyse information from a variety of sources to assess credit risk and grant credit in compliance with organisational policies and procedures. | 45%              |
| 3                        | Evaluate a range of techniques to collect debts.   | 15%              |
| 4                        | Critically evaluate credit control in line with organisational policies and procedures.  | 15%              |
| 5                        | Present advice and recommendations to management on the credit control system.   | 10%              |
| Total                    |  | 100%             |

# STUDY SKILLS

## Preparing to study

### Devise a study plan

Determine which times of the week you will study.

Split these times into sessions of at least one hour for study of new material. Any shorter periods could be used for revision or practice.

Put the times you plan to study onto a study plan for the weeks from now until the assessment and set yourself targets for each period of study – in your sessions make sure you cover the whole course, activities and the associated questions in the workbook at the back of the manual.

If you are studying more than one unit at a time, try to vary your subjects as this can help to keep you interested and see subjects as part of wider knowledge.

When working through your course, compare your progress with your plan and, if necessary, re-plan your work (perhaps including extra sessions) or, if you are ahead, do some extra revision/practice questions.

## Effective studying

### Active reading

You are not expected to learn the text by rote, rather, you must understand what you are reading and be able to use it to pass the assessment and develop good practice.

A good technique is to use SQ3Rs – Survey, Question, Read, Recall, Review:

#### 1 Survey the chapter

Look at the headings and read the introduction, knowledge, skills and content, so as to get an overview of what the chapter deals with.

#### 2 Question

Whilst undertaking the survey ask yourself the questions you hope the chapter will answer for you.

# Legislation

## Introduction

This chapter covers the legislation that affects granting credit to customers, the characteristics of a contract, remedies for breaches of contract and other relevant legislation.

### ASSESSMENT CRITERIA

Examine how the main features of statute and contract law apply to credit control (1.1)

Discuss remedies for breach of contract and the circumstances in which they can be used effectively (1.2)

Explain the terms and conditions associated with customer contracts (1.3)

Discuss the data protection and ethical considerations associated with credit control activities (1.4)

Evaluate the effectiveness of methods for collection and management of debts (3.2)

### CONTENTS

- 1 Contract law
- 2 Terms and conditions of contracts
- 3 Remedies for breach of contract
- 4 Data Protection Act
- 5 Other legislation

# 1 Contract law

## 1.1 Introduction

Control of the credit given to a customer is important for any organisation. Most organisations therefore appoint a **credit controller** whose responsibility it is to give appropriate credit terms to customers and ensure these terms are kept. **Receivables** are an important part of **working capital** and **careful management** of this asset is required to maintain the company's **liquidity**.

Credit controllers do not need to be qualified lawyers but it is important to understand the legal background to contracts and credit arrangements.

## 1.2 Nature of a contract

The sale of goods and services is a type of contract and therefore the credit controller must ensure that each party abides by this contract.



### Definition

A **contract** is a legally binding agreement between two parties.



### Definition

The **offeror** is the party making the offer.



### Definition

The **offeree** is the party accepting the offer.

The **law of contract** is the branch of the civil law which determines whether or not a promise is legally binding (i.e. enforceable by a court of law).

### 1.3 The essential characteristics of a contract

There are certain requirements if a contract is to be valid:

- **offer and acceptance** (i.e. an agreement)
- the **intention to create legal relations** (i.e. the parties must be willing to submit to the authority of the law and be bound by their contracts)
- **consideration**, in that both parties must do, or promise to do, something as their side of the contract
- the parties must have the **capacity**, or ability, **to contract and submit** themselves to the authority of the law (children and mentally disordered people are restricted)
- the parties must genuinely **consent to the terms** of the contract in that they must not have been mistaken by the contract terms, or lied to in negotiations – there must be **certainty of terms**
- the contract itself must be both **legal** and **possible**
- **written formalities** may be observed in **some** situations.

The key factors are a basic understanding of offer, acceptance, intention, consideration and capacity which will be detailed below.

### 1.4 Offer and acceptance

It is important to distinguish between an **offer** and an **invitation to treat**.



#### Definition

An **offer** is a definite and unequivocal statement of willingness to be bound on specified terms without further negotiations.

If you make an 'offer' it means that you are stating that you are willing to be bound to a contract in its current form with no changes required.

An offer can be in any form – oral, written or by conduct. However, it is not effective until it has been communicated to the offeree. For example, if a reward is offered for the return of a lost item, it cannot be claimed by someone who did not know of the reward before they returned the item.



### Definition

An **invitation to treat** is not an offer. An invitation to treat means an invitation to the other party to make an offer.

Examples of an **invitation to treat** is an advertisement, price ticket, goods on display in a shop or a trade price list where a written order from a customer is then the **offer**.

Once an offer has been made the next stage is for the contract to be accepted.



### Definition

**Acceptance** is the unqualified and unconditional agreement to all the terms of the offer.

To be effective, the acceptance must be made while the offer is still in force; it must be **absolute**, **unqualified** and **communicated** to the offeror by word or action.

**Offer and acceptance constitute agreement.**



### Example

Joseph has a sign in his car stating 'For sale, £1,200'.

Benjamin sees the invitation to treat and offers £800 to Joseph.

Joseph does not accept but responds to Benjamin that the lowest he would accept is £1,000.

Benjamin accepts so long as the car has a valid MOT certificate.

This is still not an agreement as Benjamin's response has a criterion that must be met.

Once Joseph proves he has a valid MOT and Benjamin accepts this certificate there has been:

- an invitation to treat (sign in the car)
- an offer (to buy/sell the car) and
- acceptance (Benjamin approves of the certificate).

Therefore an agreement has been formed.



**Termination of an offer**

An offer can be terminated by:

- **Revocation** – an offer can be revoked by the offeror at any time before acceptance, even if the offeror has agreed to keep the offer open. The revocation must be communicated to the offeree, i.e. it must be brought to his actual notice. The revocation can be communicated by the offeror or a reliable third party. There are two exceptions to the above rules on revocation:
  - If the offeree pays the offeror to keep the offer open, any revocation will amount to a breach of that contract. The offeree could claim damages for the loss of the opportunity to accept the offer, although he could not accept the offer itself.
  - The offeror cannot revoke his offer once the offeree has begun to perform the acts which would amount to acceptance, for example if part payment has been made.
- **Rejection** – the offeree may reject the offer outright or may make a counter offer. A counter offer is an offer made in response to an offer. A request for further details does not constitute a counteroffer.
- **Lapse** – an offer will lapse on:
  - the death of the offeror (unless the offeree accepts in ignorance of the death)
  - the death of the offeree
  - after the expiry of a fixed time (if any) or after a reasonable time. What is a reasonable time may depend on the subject matter of the contract; if the goods are perishable the time for lapse will be very short.

Once an offer has been terminated, it cannot be accepted.

**1.5 Consideration**

Before a simple binding contract exists, both parties must have **agreed to provide something of value to the other**. The price which each has to pay is termed the consideration and converts the mere promises of the parties into bargains **enforceable by the courts**.



**Definition**

**Consideration** can be defined as ‘some right, interest, profit or benefit accruing to one party, or some forbearance, detriment, loss or responsibility given, suffered or undertaken by the other’.



### Example

Joseph is selling his car and has agreed to sell it for £1,000 to Benjamin.

Joseph will be suffering the loss of his car but the benefit of gaining £1,000.

Benjamin will be suffering the loss of £1,000 but the benefit of gaining the car.

When deciding on what the consideration will be, the following should be observed:

- **Sufficient** – it must be of some value (an item or service), even if it is minimal value (**peppercorn**). The consideration is usually of monetary value. Another legal term used here is '**adequate**', this means fair price. Consideration does not need to be adequate, but needs to be **sufficient** to form a contract.
- **Legal** – i.e. not against the law.
- **Should not be a duty which exists currently** – for example 'I will pay you £50 for not breaking the speed limit'. The speed limit is a legal requirement and is therefore a duty that already exists.

Consideration must be **executory** or **executed**, but **not past**:

- **Executory** – a promise to do something in the future is given in exchange for another promise to be done in the future. (I will pay you £10 if you get an A grade in your exam).
- **Executed** – a promise is actually executed, in exchange for another promise to be executed in the future. (I will pay you £5 now for you to wash my car at the weekend).



### Example

If Z promises to paint B's house, in return for B's promise to pay Z £500, there is a valid contract between them, with both parties having obligations to perform in the future. The consideration is executory. Once Z has painted B's house, he is said to have provided executed consideration for Z's promise to pay him £500.

- **Past** – a promise has been given or executed before and independently of the other promise.



### Example

Joseph offers to sell his car to Benjamin for £1,000. Benjamin agrees to pay £1,000 for Joseph's car. There has been offer and acceptance and consideration – a simple contract has been formed.

However if Joseph had given the car to Benjamin as a gift, then at a later date Benjamin felt like he owed Joseph something for the car so told him that he would give him £1,000 next week, this would not constitute a contract since Joseph had already given the car to Benjamin (past consideration).

## 1.6 Intention to create legal relations

If an offer is accepted, then an agreement is created, but this agreement does not automatically become a contract. If one of the parties wishes to invoke the aid of the law in enforcing the terms of the agreement against the other party, he must show that there had been an intention by both parties that the agreement was to create legal relations.

There is a presumption in social or domestic agreements that legal relations are not intended. But in **commercial agreements**, it is generally **assumed that relations** are intended unless there is a clause in the agreement to the contrary.

## 1.7 Capacity

Each party must have the legal power to bind itself contractually. For example persons under the age of eighteen (minors) and persons of unsound mind or under the influence of alcohol have limitations on their power to contract.



### Test your understanding 1

Which of the following are features of a simple contract:

- (i) Offer
  - (ii) Consideration
  - (iii) Relations
  - (iv) Acceptance
  - (v) Invitation
  - (vi) Certainty of terms
  - (vii) Intention to create legal relations
- A All of them
- B (i), (ii), (iii), (v), (vi) only
- C (i), (ii), (iii), (iv) only
- D (i), (ii), (iv), (vi) and (vii)



### Test your understanding 2

Raphael has a notice in his shop window saying that the books he has for sale are half price. This is an example of:

- A Offer
- B Acceptance
- C Invitation to treat
- D Consideration



### Test your understanding 3

Barry is ordering an Indian takeaway on the telephone and says he will pay when he picks up the order. Which of the following would constitute consideration?

- A Placing the order
- B Paying for the order
- C Saying he will pay for the order
- D Picking up the order



#### Test your understanding 4

Betty is the owner of a haberdashery and put a notice in the window of her shop advertising that all fabric has 20% off. This is:

- A A completed contract
- B An acceptance of an offer
- C A contractual offer
- D An invitation to treat



#### Test your understanding 5

If you are shopping in a supermarket a contract is formed?

- A When you put your goods in the trolley
- B When you take items off the shelves
- C When the checkout assistant takes your goods
- D When you pay for the goods



#### Test your understanding 6

Steph has asked Callum for a price to paint her bedroom. Callum has said he can do it for £300 and Steph has agreed. Nearing the end of the job Callum asks Steph for £50 more as he has underestimated the work.

Does Steph have to pay Callum the extra £50?

Yes/No?



#### Test your understanding 7

Tina orders a Chinese takeaway over the telephone and says she will pay on delivery. Which of the following would constitute consideration?

- A Handing over the money to the delivery driver
- B Promising to pay for the takeaway
- C Accepting delivery of the takeaway
- D Calling the Chinese takeaway

# 2

## Terms and conditions of contracts

### 2.1 Types of contracts

A **void** contract is one that **cannot be enforced by law**. An agreement to carry out an illegal act or an agreement that is impossible to carry out are examples of void contracts.

A **voidable** contract is a valid contract that **can be nullified** (to make legally null and void) – one party is bound to a contract but the other party is not, so can withdraw from the contract. If this happens then the contract becomes void. A contract between an adult and a minor is an example of a voidable contract as the adult is bound by the contract but the minor is not as they are not of legal age.

An **unenforceable contract** is one that is **valid** (i.e. meets all the requirements previously defined) but **if one party withdraws** from the contract the **courts of law will not enforce** them to meet the requirements of the contract.

A **frustrated contract** occurs if an unforeseen event either renders contractual obligations impossible, or radically changes the party's principal purpose for entering into the contract.

Frustrated contracts could occur in the following circumstances:

- An item or building essential to the contract is destroyed, through no fault of either party.
- A law is passed subsequent to the formation of the contract, which makes the contract illegal.
- A person or group under contract becomes unavailable through death, illness or unavailability (generally only applies for the performance of personal services and not for generic commercial services such as building work, which could be performed by numerous individuals).

An important limitation is that economic hardship, or a 'bad bargain', will not render a contract frustrated.

**Test your understanding 8**

A void contract is a contract that:

- A Is valid
- B Can be enforced by the law
- C Can be nullified
- D Cannot be enforced by the law

## 2.2 Contractual terms

A statement, written or oral, made during the negotiations leading to a contract, may be a **term** of the contract or merely a **representation** inducing the contract.

A **representation** is something that is said by the offeror in order to persuade the offeree to enter into the contract. It may or may not become a term of that contract.

The distinction between terms and representations is important because, if a statement is untrue, the remedies available to the innocent party differ:

- if the representation becomes a term of the contract, the innocent party has remedies for breach of the term as well as for misrepresentation
- if, however, the representation does not become a term of the contract, the innocent party will have remedies only for misrepresentation which are based on equitable remedies.

## 2.3 Sources of terms

Terms may be **express** or **implied**.

**Express** terms are those specifically inserted into the contract by one or both of the parties. They must be clear for them to be enforceable.

**Implied** terms are not expressly included in the contract, but they are nevertheless still part of the contract. They may be implied by statute or by the courts.

Express terms will generally override implied terms. However, some statutory terms cannot be overridden by express agreement (for example, terms inserted by the Consumer Rights Act).

There are three types of terms:

- A **condition** – is an important term going to the root of the contract. Breach can result in damages or discharge or both. Discharge entitles the innocent party to reject the contract and claim damages.
- A **warranty** – is a less important term, which is incidental to the main purpose of the contract. Breach of warranty results in damages only.
- An **innominate** or indeterminate term – is neither a condition nor a warranty. The remedy depends on the effects of the breach:
  - if trivial then damages only i.e. term is treated as if it were a warranty.
  - if serious then damages, discharge or both i.e. term is treated as if it were a condition.

## 3

### Remedies for breach of contract

#### 3.1 Introduction

Legal action can be taken to enforce a contract or to act as a remedy if a contract is breached. There are different types of **breach of contract**:

- **Actual breach** – when one party refuses or fails to complete the contract by the due date.
- **Fundamental breach** – is a breach of contract where the offending party fails to complete a contractual term that was so fundamental (hence the name of the breach) to the contract that another party was prevented from fulfilling their own responsibilities. This type of breach is not a subtle one, and it often is grounds for the aggrieved party to cancel the contract entirely. It is sometimes known as a **repudiatory** breach.
- **Anticipatory breach** – when one party informs the other party prior to the due date that the contract will not be completed. Compensation can be sought as soon as the innocent party is aware of the breach. Anticipatory breach is often referred to as **renunciation**.



Anticipatory breach may be express or implied:

- **Express** anticipatory breach occurs where one of the parties declares, before the due date for performance, that they have no intention of carrying out their contractual obligations.
- **Implied** anticipatory breach occurs where one of the parties does something which makes subsequent performance of their contractual undertaking impossible.

This section examines the legal remedies that may be available to any injured party as a result of a breach of contract.

### 3.2 Damages

The innocent party can claim damages from the guilty party. He may recover **damages** for any loss suffered as a result of the breach by bringing an **action for damages** for breach of contract. The objective of damages is to put the innocent person into the same financial position he would have been in if the contract had been completed correctly. The amount of damages awarded should compensate the innocent party but should not punish the guilty party.

If the breach consists of the other party's failure to pay a debt (i.e. the contractually agreed price or other remuneration due under the contract), the appropriate course for the injured party is to bring an action for the **agreed sum** to recover that amount, this is an **action for price**.

If one party has already performed part of his obligations and the other party then repudiates the contract the course of action would be the remedy of **Quantum Meruit**. Under this remedy, the value of the contractual work which has already been performed is measured.

### 3.3 Equitable remedies

If damages are not sufficient then equitable remedies, such as *specific performance*, *injunctions* or *rescission*, may be awarded.

**Specific performance** – This is a court order to force the guilty party to positively complete his contractual obligations.

**Injunction** – This is a court order to force the guilty party to perform a negative obligation i.e. to cease doing something or to remove something that is in breach of contract.

**Rescission** – Restores the parties to their exact pre-contractual position.

### 3.4 Retention of title

The seller can add to the contract that the '**goods remain the property of the seller until payment has been received**'. This means that if there is non-payment that the seller retains the ownership of the goods. This is particularly useful if the receivable becomes insolvent as the seller maintains priority over the goods when monies are being paid.

For a retention of title claim to be successfully enforced:

- the goods need to be clearly identifiable
- the goods must not have been processed or improved in a manufacturing process.



#### Test your understanding 9

The normal remedy for breach of contract due to non-payment of the debt is:

- A Action for remedy
- B Action for the goods
- C Action for specific performance
- D Action for price



#### Test your understanding 10

Retention of title is:

- A The right of the seller to retain ownership of the goods until payment is made
- B The right of the purchaser to retain ownership of the goods received
- C The right of the purchaser to expect that title is retained by the seller even when payment has been received
- D The right of the seller to retain ownership of the goods until a cheque has been posted

### 3.5 Late Payment of Commercial Debts (Interest) Act 1998

The late payment act allows businesses to **charge other business customers interest on overdue amounts** and allows businesses to cover late payments of bank borrowings. Interest can be charged:

- 30 days after the goods are supplied or the service is completed.
- 30 days after receipt of invoice (or the customer is told the amount due is payable).
- The agreed date for payment.

The interest rate is 8% above the Bank of England base rate for the period the debt is late. The interest is based on the **VAT inclusive** amount and calculated as a simple interest rate.



#### Example

A debt of £3,000 exclusive of VAT has been outstanding for 60 days. The Bank of England base rate is 0.5%. The late payment charge is:  
 $3,000 \times 1.2 \times 0.085 \times 60/365 = \text{£}50.30$

It is also possible to charge a business a fixed sum for the cost of recovering a late commercial payment (sometimes called a **compensation entitlement**) on top of claiming interest from it.

The amount you are allowed to charge depends on the amount of debt:

| Amount of debt      | Charge |
|---------------------|--------|
| Up to £999.99       | £40    |
| £1,000 to £9,999.99 | £70    |
| £10,000 or more     | £100   |

# 4 Data Protection Act

## 4.1 Introduction

Due to the growth in the use of computer technology the Data Protection Act 1998 was introduced to make **certain restrictions** on the use of data about **individuals** and the **use of personal data**. It is likely that your organisation will hold computer data about credit customers and therefore you need to be aware of the broad outlines of the Act.

However it is important to realise that the Act relates to data **held about individuals not about organisations** so will only be relevant to non-corporate customers or to data about individuals who belong to a customer organisation.

The Data Protection Act gives individuals the right to know what information is held about them. It provides a framework to ensure that personal information is handled properly.

The Act works in two ways.

- Firstly, it gives rules and principles concerning the use of data.
- Secondly, it provides individuals with important rights concerning data held about them.

There are, however, exemptions to the Data Protection Act. For example:

- Any personal data that is held by MI5 and MI6 for a national security reason is not covered.
- Personal data held for domestic purposes only at home does not have to keep to the rules – e.g. a list of your friends' addresses.

## 4.2 Definitions

**Personal data** is information held about an individual, not only factual information but also expressions of opinion about that individual.

**Data users** are individuals or organisations who use personal data.

A **computer bureau** is an individual or organisation which processes personal data for data users, or allows data users to process personal data on its equipment.

### 4.3 The key principles of the Act

- Data may only be used for the **specific purposes** for which it was collected.
- Data **must not be disclosed** to other parties without the consent of the individual whom it is about, unless there is legislation or other overriding legitimate reason to share the information (for example, the prevention or detection of crime). It is an offence for other parties to obtain this personal data without authorisation.
- **Individuals have a right of access to the information held about them**, subject to certain exceptions (for example, information held for the prevention or detection of crime).
- Personal information may be **kept for no longer than is necessary** and must be kept up to date.
- Personal information **may not be sent outside the European Economic Area** unless the individual whom it is about has consented or adequate protection is in place, for example, by the use of a prescribed form of contract to govern the transmission of the data.
- Subject to some exceptions for organisations that only do very simple processing, and for domestic use, all entities that process personal information must **register with the Information Commissioner's Office**.
- Entities holding personal information are required to have adequate **security measures in place**. Those include technical measures (such as firewalls) and organisational measures (such as staff training).
- Subjects have the right to have **factually incorrect information corrected** (note: this does not extend to matters of opinion).
- All data users and computer bureaux have to **register with the Data Protection Registrar** – the data user must then only hold data and use data for the purposes which are registered.
- Processing of personal data is forbidden except in the following circumstances:
  - with the consent of the individual
  - due to a legal obligation
  - due to a contractual obligation
  - due to a contractual arrangement
  - in the public interest
  - to protect the vital interests of the individual.

- If data is obtained from a third party the data subject must be given:
  - the identity of the controller of the data
  - the purposes for which the data is being processed
  - the data that will be disclosed and to whom.
- Data subjects have the right to a copy of the data held, the right to know why the data is being processed and the logic behind the processing. Data subjects may seek compensation through the courts for damage or distress caused by the loss, destruction, inaccuracy or unauthorised disclosure of personal data.
- Data subjects can apply to the courts or Registrar for inaccurate data to be corrected or removed from the data user's files.



### Test your understanding 11

The Data Protection Act applies to (pick as many as appropriate):

- A Data about individuals, companies and government departments
- B Data about individuals only
- C Data about companies only
- D Data about companies and individuals only
- E Only manual records
- F Only computer records
- G All records held by the company
- H Only records of opinions

## 5 Other legislation

### 5.1 Trade Descriptions Act

The Trade Descriptions Act states that manufacturers, retailers and the service industry must **correctly describe what they are selling**. It is a **criminal offence to make a false or misleading statement** about the goods or services being provided i.e. **misrepresented** in any way.

From May 2008, the **Consumer Protection from Unfair Trading Regulations 2008** replaced most of the Trade Descriptions Act 1968.

There are three main sections in the "Regulations". These are as follows:

- A general ban on unfair commercial practices. A commercial practice is 'unfair' if it fits both of the following requirements:
  - 1 It falls below the good-faith standards of skill and care that a trader in that industry would be expected to exercise towards customers.
  - 2 It affects, or is likely to affect, consumers' ability to make an informed decision about whether to purchase a particular product.
- A ban on misleading and aggressive practices which are assessed in light of the effect they have, or are likely to have, on the average consumer. A commercial practice is considered aggressive if, by means of harassment, coercion or undue influence, it significantly impairs (or is likely to significantly impair) the average consumer's freedom of choice or conduct, which then leads the consumer to take a decision that they would otherwise not have made.
- The 'blacklist' of commercial practices which will always be unfair and so are banned outright. There are a number of banned practices they include:
  - 1 Limited offers – falsely stating that a product will only be available for a very limited time.
  - 2 False free offers – describing a product as free or without charge if the consumer has to pay anything other than the unavoidable cost of responding to the offer and collecting or paying for delivery of the item.
  - 3 Pressure selling – creating the impression that the consumer cannot leave the premises until a contract is formed.

## 5.2 Unfair Contract Terms Act

Contracts must be written in **language that is understandable** and any part of the contract that acts more favourably for the vendor than the consumer is unfair and not binding.

This is the most important statute affecting exclusion clauses and is largely restricted to business liability i.e. liability arising during business or from occupation of premises for business purposes. It is not possible to exclude liability for death or personal injury and all other losses are subject to a test of reasonableness.

## 5.3 Consumer Rights Act 2015

The Consumer Rights Act 2015 became law on 01 October 2015, replacing three major pieces of consumer legislation – the Sale of Goods Act 1994, Unfair Terms in Consumer Contracts Regulations and the Supply of Goods and Services Act.

The Consumer Rights Act **applies when the title of the goods has passed from the vendor to the buyer** and states that as a buyer you have three statutory rights:

- 1 Goods should be of '**satisfactory quality**', they shouldn't be faulty or damaged when you receive them.
- 2 That the goods should be **fit for the purpose** they are supplied for.
- 3 Goods supplied must match any description given to you; they should be '**as described**'.

The rules also includes digital content in this definition.

The Consumer Rights Act also covers providing services, for example work carried out by accountants, solicitors, builders. The Act means that all contracts for services must do the following:

- The trader must perform the service with reasonable care and skill.
- Information that is spoken or written is binding where the consumer relies on it.
- Where the price is not agreed beforehand, the service must be provided for a reasonable price.
- Unless a particular timescale for performing the service is set out or agreed, the service must be carried out in a reasonable time.



If the service does not satisfy these criteria, you are entitled to the following remedies:

- The trader should either redo the element that is inadequate, or perform the whole service again at no extra cost to you, within a reasonable time and without causing you significant inconvenience.
- If repeat performance is not possible, you can claim a price reduction. Depending on how severe the failings are, this could be up to 100% of the cost, and the trader should refund you within 14 days of agreeing that you're entitled to a refund.

### 5.4 Consumer Credit Act 1974 and 2006

The Consumer Credit Act 1974 and 2006 requires:

- Businesses that offer goods or services on credit or lend money to individuals to be **licensed** by the **Financial Conduct Authority (FCA)**. Trading without a licensing arrangement is a criminal offence and can result in a fine and/or imprisonment.
- That the borrower can settle a regulated consumer credit agreement early by giving notice to the lender and paying the amount due less a rebate. The borrower is also entitled to information about the amount needed to settle.
- The seller lays down rules requiring information to be given to borrowers or hirers before entry into a consumer credit or hire agreement.



### Test your understanding 12

Calvin is sold some lime cordial by Hobbs but when Calvin opens the bottle it is actually lemonade. Calvin can claim for breach of contract due to:

- A Fiduciary misconduct
- B Misrepresentation
- C Misuse of Sales Act
- D Unfair Contract Terms Act

### **5.5 Professional ethics in the context of credit control**

Finance professionals can help in creating and promoting an ethics-based culture that discourages unethical or illegal practices, including money laundering, terrorist financing, fraud, theft, bribery, non-compliance with applicable regulations, bullying and short-term decision-making.

## **6 Summary**

This chapter has covered the legislation that affects granting credit to customers, the characteristics of a contract, remedies for breaches of contract and other relevant legislation.

The sale of goods on credit to a customer is a contract and therefore you need to be aware of the legal background in terms of the general nature of contract law. You must also be aware of the basic provisions of the Data Protection Act and other legal terms and conditions in relation to a contract.

Test your understanding answers



Test your understanding 1

Answer D



Test your understanding 2

Answer C



Test your understanding 3

Answer C



Test your understanding 4

Answer D



Test your understanding 5

Answer C



Test your understanding 6

No – the additional amount does not have to be paid as the agreement was for £300.



**Test your understanding 7**

Answer B



**Test your understanding 8**

Answer D



**Test your understanding 9**

Answer D



**Test your understanding 10**

Answer A



**Test your understanding 11**

Answers B and G



**Test your understanding 12**

Answer B