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Planning, Information Gathering, and Assessment

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I. Overview

§2.1 Filing a lawsuit against a worthless defendant when there is no chance of recovery is a substantial waste of time, money, and energy. To save headaches and client disappointment, check out the defendant before instituting a suit. Besides reviewing such basic items as a corporation's annual reports and conducting a Uniform Commercial Code (UCC) search for secured creditors and tax liens, searching the Internet, through services such as Accurint (<http://www accurint.com>) and AutoTrackXP (<http://www autotrack.com>), is a convenient and reasonably priced way to collect a considerable amount of useful information about debtors.

At an early stage the collector must consider such concerns as the statute of limitations, the legal composition of the debtor, what court to file suit in, what parties to sue, and potential fraudulent transfers. The creditor should take full advantage of the information that is contained in credit applications. Finally, the collector's staff should be trained to make full and effective use of the telephone to collect debts.

Exhibits 2.1 and 2.2 (flowchart and explanatory text) describe the litigation process of a collection lawsuit to a client.

II. What Nonlawyer Clients Need to Know About Contract Law

A. In General

§2.2 A working knowledge of fundamental contract law principles is essential in collecting debts. Credit professionals should be aware of just how important contract law is in terms of enforcing creditor claims. A review of the following sections plus the contract defenses discussed in chapter 5 should give the nonlawyer some background and "ammunition" to deal with various debtor claims or defenses that might arise in the course of debt collection. *See also Michigan Contract Law* (John R. Trentacosta ed, ICLE 2d ed).

B. Fundamental Principles and Documents

§2.3 A contract generally consists of an offer, acceptance, and consideration. In business, the offer typically consists of a purchase order, and the acceptance is the shipping of the goods or the providing of services named in the purchase order. The consideration is the purchase price. Offer, acceptance, and consideration can be implied depending on the circumstances.

With some important exceptions (such as sales of real property), contracts do not have to be in writing. Although the UCC provides that all contracts over

\$1,000 should be in writing, UCC 2-201(1), MCL 440.2201(1), there is a notable exception to this rule. Where a seller of goods ships to a buyer and the buyer receives and retains those goods, there is an implication that a contract exists. If the buyer fails to timely return the goods, no writing is needed to imply that the buyer intended to contract for the purchase price of the goods. UCC 2-201(3)(c), MCL 440.2201(3)(c). The UCC also provides for substitutes for a writing or exceptions to the writing requirement where there is a written confirmation between merchants, UCC 2-201(2), MCL 440.2201(2); specially manufactured goods, UCC 2-201(3)(a), MCL 440.2201(3)(a); an agreement admitted in court, UCC 2-201(3)(b), MCL 440.2201(3)(b); and partially performed agreements, UCC 2-201(3)(c), MCL 440.2201(3)(c).

The UCC does not require price terms, delivery terms, or other details for the sale of goods. Past experience of the parties and other statutory default provisions will help to determine most of the terms of a contract, including a purchase price. Therefore, it is fairly easy under the UCC to establish the existence of a contract without having to prove specifically the elements of offer, acceptance, and consideration.

The contract has to be entered into before the goods are delivered or services are provided. For that reason, the purchase order and the documentation before the sale, including the credit application, become the contract between the parties. The credit application is an often overlooked but important document. Credit applications often set forth extremely important terms such as interest rates to be paid should the account become delinquent, personal guaranties to be invoked if the account becomes delinquent, the parties' agreement concerning full settlement checks, etc. For a sample credit application, see form 2.1.

A common misconception among business people is that an invoice is a contract. An invoice may contain a description of the goods, shipping dates, and price terms, but it is not a contract. The invoice is prepared and mailed out after the goods are shipped and after the contract is entered into. For this reason, the terms printed on the back of invoices (most companies insist on filling up the back of their invoices with various terms in small print: immediate inspection, immediate return of any defective goods, a return authorization number on any defective goods, and so forth) are generally not enforceable. See *Power Press Sales Co v MSI Battle Creek Stamping*, 238 Mich App 173, 183, 604 NW2d 772 (1999). Thus, for example, if a customer voluntarily agrees to pay interest on a delinquent account based on the terms set forth in the invoice, that is all well and good, but if the customer later decides not to pay the interest, it is likely that a court will not enforce the interest terms if they are only in the invoice.

The courts will generally enforce contracts that are within the parties' expectations. If there is a one-sided (unilateral) mistake, the contract is enforceable. However, if there is a mutual mistake, the court will generally not enforce it. For example, if both parties thought that the steel was Grade A worth \$57.00 per pound and it turned out, by mistake of both parties, that the steel was Grade B, then the court will not enforce the contract.

Sometimes contracts are purely unilateral. In other words, acceptance of the contract occurs through performance. For example, if someone offers to pay \$500 if the contracting party drives a car to California, acceptance occurs when the car is driven to California.

Consideration is difficult to measure and courts often will not bother to measure it at all. If there is the existence of any legal consideration, the contract will most likely be enforced. Thus, if the buyer overpays for a product, a court will not question the overpayment unless there was actual fraud or a mutual mistake.

C. Ratification

§2.4 Ratification is an overlooked principle in the enforcement of contracts. Sometimes the parties have dealings with each other but no valid contract exists. This might occur when one of the parties was represented by an agent who had no authority to act on the principal's behalf (see §2.18). If a seller ships to a buyer who did not authorize the shipment, the buyer is still obligated to pay for the goods if the goods are received and accepted. The acceptance of goods under the UCC creates an absolute obligation to pay for them. UCC 2-607, MCL 440.2607. This is the concept of ratification. For an example of how this might occur, consider a printing company that receives an order for 5,000 sheets of letterhead. It is more efficient for the printer to run 10,000 sheets at a time. Therefore, the printer prepares an order of 10,000 sheets and ships the entire 10,000 to the buyer. If the buyer receives the 10,000 sheets at the delivery dock, signs for them, and then fails to timely reject them, the buyer is now obligated to pay for 10,000 sheets of letterhead even though 5,000 was the original order quantity. Thus, ratification can create a contract (or different terms) where none originally existed.

III. The Importance of Credit Applications

A. In General

§2.5 The credit application is frequently one of the more powerful documents in a credit manager's file. In many instances, the credit application is literally the only contract between the parties that specifies conditions other than those contained in purchase orders. Shipments of goods on open accounts often are devoid of any contractual terms, and credit people look to their own invoices to establish the contractual basis for their dealings with their customer. However, the invoice is not a contract. It is sent out after the making of the order. It is not designed or intended to be a contract between a buyer and a seller; it is only a confirmation of specific terms such as price, dates, place of delivery, quantity of goods, and so forth. Even the interest provisions that often appear on invoices are generally not enforceable if a debtor chooses to ignore them.

Although the courts have not definitively ruled on jurisdiction and venue for businesses with websites, many courts are allowing cases to be heard in venues where a website is accessible, particularly if the site is more than just informational (passive). See also §2.11. A website's posting of a credit application that would form the basis of doing business with a customer could easily be considered active.

Furthermore, it is good practice to set forth a forum for dispute resolution, and it is becoming increasingly common to insert some specific means of dispute resolution, such as binding arbitration clauses, in a contract. Keep in mind that these clauses should be regularly reviewed by an attorney because the law in this entire area is unsettled and constantly changing. Finally, electronic signatures are enforceable as original signatures, although as of yet no cases have decided that this also applies to personal guaranties. *See* 15 USC 7001 et seq. (Electronic Signatures in Global and National Commerce (E-SIGN) Act), MCL 450.831 et seq. (Uniform Electronic Transaction Act [UETA]).

Thus, at the beginning of the open account, a credit application is the key document. A well-written credit application can head off a number of problems between the parties that may arise as their business relationship develops. See also the discussion of UCC searches in §2.33.

B. Information Requests and Policy Statements

§2.6 An effective credit application contains provisions asking for the following information or stating the following:

1. The correct and full legal name of the applicant, the physical address (not merely a post office box), and the position of the individual who is applying (treasurer, president, etc.). To make sure that the customer clearly specifies the type of business entity, provide check-off boxes for proprietorship, corporation, limited liability company (LLC), and partnership. Requiring a tax I.D. number for a corporation and social security number for a proprietorship is also a good idea.
2. Any trade names the company operates under. For example, if the Brake Shop is a division of Win Management Corporation, the application should require that both names be listed along with the relationship between the two.
3. Names, addresses, and telephone numbers of any authorized purchasers at any branches.
4. Names, addresses, telephone numbers, and social security numbers of partners and officers.
5. Name, address, and telephone number of the bank where the company maintains its accounts.
6. Names, addresses, and telephone numbers of several trade references.
7. Type of product(s) sold.
8. Year the business was formed.
9. A statement similar to the following: “A signature on this document provides permission to pull a credit bureau report on any individual who may be liable under this agreement (such as a personal guarantor, proprietor, general partner, or similar person).”
10. Financial statements.