



Dishonoured Cheques and Direct Debits

With the introduction of the trial of the new debit card for transactions under £10 which do not require a pin number and the explosion in the use of credit and debit cards in the past few years, the humble cheque is being accepted by less and less retail outlets as a means of payment. The cheque still remains a popular method for business transactions and looks almost certain to remain so for the foreseeable future.

The law relating to cheques has remained in force and relatively unchanged since the passing of the Bills of Exchange Act 1882. The Cheques Act 1957 and 1992 have slightly amended the Bills of Exchange Act 1882 which remains otherwise fully intact. The introduction of the 1882 Act set out the law that had previously been developed by the Courts of Exchequer in over 2500 cases since the Industrial Revolution.

In this article, we look closely at exactly what a cheque is and how it may be of benefit to your business.

A cheque is a promise of payment by a specified bank for a particular sum on a particular date. If the cheque is not honoured upon presentation, for whatever reason, the debt will be honoured if it is not discharged. Therefore, once you have a cheque received, the chances of having a claim defended can only be defended in a few limited ways. These are:

1. **Duress:** The person signing the cheque would be made to do so because of unlawful pressure brought to bear against him. The law relating to duress, which has developed largely through the courts on a case by case basis, makes the burden of proof very difficult for the person alleging duress and it is quite rare for this to succeed unless good cause can be shown.
2. **Fraud:** The person who signed the cheque was not the signatory or the person purported to be. Again, the person who wishes to rely on the defence faces a difficult task in proving their claim as the evidential burden is again high.
3. **Failure of consideration:** This is that no bargain is given in return for the cheque. Providing there is some (however small) consideration then this defence will fail as the courts are not there to determine whether or not you've got a good deal but just to determine whether or not there was sufficient consideration.

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4. **In respect of an illegal contract**, which is a contract which is illegal to enter into and therefore unenforceable, therefore once you have received the cheque the chances of not receiving payment are relatively small as this is an unequivocal promise to pay.

A further problem for the party who dishonours is when they dishonour a cheque for over £750 where the cheque is marked "refer to drawer" as there are insufficient funds in the account. This therefore gives the creditor (person to whom the cheque is made payable) the legal right to present a winding-up petition (if against the company) or a bankruptcy petition (if against an individual or sole trader) as they have an inability to pay their debts as set out in Section 123 of the Insolvency Act 1986. The cheque must be for more than £750 to enable a bankruptcy or winding-up petition to be presented. If the cheque is for under £750 this does give you the right to present a statutory demand which is a formal demand for payment but this gives the debtor three weeks in which to pay. The debtor has to owe more than £750 to present a bankruptcy or winding up petition but creditors can join their debts together to reach this sum. Where the cheque is over £750 the need for a statutory demand is extinguished.

Interestingly, the law relating to dishonoured cheques now applies to dishonoured direct debits and therefore providing a direct debit is a promise to pay in the same way that a cheque is. This was confirmed by the Court of Appeal in the case of *Esso Petroleum Co. Limited v. Milton* 1997.

Nowadays, it is also common practice to have a cheque supported by a cheque guarantee card. This can also strengthen your position as the bank is obliged to honour the cheque up to the value of the cheque guarantee card whatever happens. The bank is only obliged to pay you once you have complied with the following conditions:

1. that the cheque was from a pre-printed chequebook;
2. that the cheque was signed in your presence;
3. the transaction occurred before expiry of the cheque guarantee card;
4. the details of the card, card number, expiry date, etc, must be written on the back of the cheque; and
5. the amount of the cheque must not exceed the total of the cheque guarantee card.

Where you have, say, a £100 cheque guarantee card limit and you have a transaction worth £200, multiple cheques cannot be guaranteed by the bank in the same transaction and therefore you are only protected up to the value of the first cheque as the bank is not obliged to pay beyond this value. You should therefore be careful to ensure that you check carefully the level of the cheque guarantee card.

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The use of cheques and direct debits therefore offer the seller greater protection if they are used in the appropriate way.

What should you do once a cheque has been dishonoured?

Immediately upon receiving the notification from your bank of a dishonoured cheque, you should provide the provider of the bounced cheque with notice of dishonour pursuant to Section 48 of the Bills of Exchange Act 1882. Once notice of dishonour has been provided and a reasonable time has elapsed you then have the option of whether to issue County Court or High Court proceedings followed by an application for summary judgment. Legal costs are only recoverable (save for fixed legal costs as specified by the court) where the sum outstanding is £5,000 or more. You are only able to issue in the High Court with claims over £15,000 in value. A statutory demand can also be used by we usually advise to obtain a County Court Judgment first. If the debt is over £750 a bankruptcy or winding-up petition can be sought.

Furley Page Debt Recovery and Insolvency Services

Furley Page Debt Recovery and Insolvency Team has vast experience of dealing with dishonoured cheques and direct debits and operate debt recovery matters on a percentage recovery fee, where largely we only charge commission where we are successful. This information sheet has been prepared to highlight some of the key issues relating to the dishonouring of cheque payments and direct debits and the possible avenues available to you. It is intended for general guidance only and is no substitute for specific legal advice. It is based on our understanding of the current legal position and is, of course, subject to changes in the law after August 2008.

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