



7 September 2009

PROPOSAL FOR A DIRECTIVE OF THE COUNCIL AND THE EUROPEAN PARLIAMENT ON COMBATING LATE PAYMENT IN COMMERCIAL TRANSACTIONS (RECAST OF DIRECTIVE 2000/35/EC)

EXECUTIVE SUMMARY

- Late payments inflict severe damage on companies – in particular SMEs. They reduce available working capital and pose a threat to the survival of otherwise viable businesses. The current financial and economic crisis exacerbates this situation.
- Payment delays vary between member states and the type of transaction, i.e. business-to-business and business-to-public authorities. For example, the average payment delay of public authorities exceeds 260 days in Italy compared with two to three weeks in Sweden.
- According to the Commission's impact assessment, businesses would receive additional liquidity of almost 180bn euros if public authorities paid outstanding bills within a period of 30 days. For comparison: In economic recovery plans, the EU and member states made 200bn euros available to fight the economic impact of the crisis.
- In Intrum Justitia's European Payment Index it is estimated that in 2009, companies will need to write off 270 billion euros of receivables– equal to 2.4% of EU GDP.
- On 8 April 2009 the European Commission presented a proposal for a directive to combat late payment in commercial transactions, recasting directive 2000/35/EC, the effectiveness of which was limited and which did not address late payment by public authorities.
- BUSINESSEUROPE welcomes the Commission's proposal. But we encourage policy-makers to implement key principles of the new directive without delay in order to provide effective relief for companies in the current crisis. A coordinated, European approach is essential to avoid threats to the internal market.
- BUSINESSEUROPE appreciates in particular, that transactions between businesses and public authorities should be paid within 30 days. Public authorities at all levels should lead by example.
- BUSINESSEUROPE appreciates that the principle of contractual freedom is upheld for business-to-business transactions. Of course, it is a sign of responsible business behaviour that agreements are respected and that they do not result from an abuse of a dominant negotiation position.
- The assumption that especially smaller suppliers take legal recourse in case of late payments seems unrealistic out of fear of losing future contracts. In the absence of an efficient and independent framework for enforcement, sanctions to be applied by the supplier might not be effective. Incentives for payment on time might therefore be more promising.



LATE PAYMENTS – A REAL THREAT TO COMPANIES

Late payments inflict severe damage on companies' – in particular SMEs' – liquidity positions. Clients' delayed or non-payment of invoices reduces cash flows and thus available working capital. This poses a direct threat to the survival of otherwise viable companies. In the current financial and economic crisis, which has triggered a substantial tightening of banks' credit conditions and hence reduced access to external finance severely, the impact of late payments for companies is even amplified.

Payment delays vary significantly between member states, with a clear north-south divide. The payment behaviour between business-to-business transactions also differs from payment delays by public authorities at national, regional or local level. Whereas the European average for public authorities' payment delays is 67 days – compared with 57 for the private sector –, the average delay even exceeds 130 days in Spain or 260 days in Italy.

Based on data published in a recent study by Intrum Justitia¹, we estimate that the total amount of late payments in member states representing 80% of EU27 GDP, i.e. payments occurring after 30 days, was close to 800 billion euros in 2007. In the context of the current crisis, this amount is likely to have increased substantially.

In the same study, Intrum Justitia estimates that due to bad payment behaviour, companies will need to write off 270 billion euros of receivables in 2009 alone. This represents 2.4% of EU GDP – compared to the EU economic recovery plan of 1.5% of EU GDP. In addition, companies are expected to spend 25 billion euros on recovery proceedings.

Because of the impact of the financial crisis, it has become increasingly difficult for companies to insure against late payment or to cover delays by short-term bank loans. Public guarantee schemes and EIB loan facilities might not be sufficient and the situation has taken life-threatening proportions in Ireland or Portugal.

MEMBER STATES' MEASURES TO FIGHT LATE PAYMENTS

Some governments have taken action to fight late payments and limit their impact:

- **United Kingdom**

BUSINESSEUROPE's British member federation, CBI, has long been active in promoting prompt payment at national level and the UK is now already comparatively ahead of the measures put forward by the Commission. Conscious of the importance of good customer/supplier relationships, CBI members are today encouraged to consider signing up to the voluntary "Prompt Payment Code²", which focuses on a commitment to pay suppliers on time, clear guidance and encouraging good payment practice.

Public sector organisations have committed to settle bills within 10 days. Legislation to allow businesses to claim interest on the late payment of commercial debt was introduced in 1998, but statistics show that this facility is underused.

¹ Intrum Justitia, "European Payment Index 2009"

² <http://www.promptpaymentcode.org.uk>



- Belgium
The federal government has committed to pay invoices to federal authorities more rapidly. Furthermore, the federal government has created a special and new "bridge credit" under a federal investment fund to finance payment delays by all public authorities, not only at federal level.
- Spain
For 2009, the Instituto de Crédito Oficial (ICO) has created a liquidity facility of 10 billion euros for preferential loans to enable SMEs and self-employed workers to meet their liquidity needs. These funds are subject to co-financing rules, i.e. 50% are covered by the ICO and 50% by credit institutions.
Furthermore, the "Local Corporation Advance Payment Facility" guarantees the collection of invoices endorsed by enterprises and the self-employed for works and services supplied to local corporations.

The problem of late payments is less urgent in Nordic member states, where suppliers can rely on clients' very good payment morale. According to Intrum Justitia¹, average business-to-business payment delays in Finland (7 days) or Sweden (8 days) are less than two weeks, bringing the overall payment duration in both countries very close to the payment period of 30 days aimed at in the proposed directive. Furthermore, interest for late payment can be charged automatically, without involving court rulings.

In other member states, governments have committed to reduce payment delays notably by public authorities. This is the case in the Czech Republic – although in contrast to the private sector, payment times remain above EU average in the public sector –, Ireland, Poland, Portugal or the United Kingdom. However, the effectiveness of such measures often remains limited. In particular provisions that allow companies to claim interest on late payments are rarely invoked for fear of upsetting relationships with public or private clients

In the light of this disparate picture, a number of BUSINESSEUROPE member federations esteem that further legislative action is needed, especially regarding the payment behaviour of public authorities. However, this needs to be done on a European basis in order to prevent distortions to the internal market.

As regards business-to-business transactions, legislative measures should not impede contractual freedom but bring transparency into the payment relations between companies and reduce administrative burden connected to their legal enforcement.

BUSINESSEUROPE ASSESSMENT OF THE COMMISSION PROPOSAL

The European Commission has presented on 8 April 2009 a proposal for a directive to combat late payment in commercial transactions ("late payments directive"), recasting the earlier directive 2000/35/EC.

Assessments have shown that the existing directive has not been effective in reducing late payments in business-to-business transactions. The aspect of late payment by public authorities was not included in the directive at all.

Therefore, BUSINESSEUROPE welcomes the Commission's proposal to recast the existing directive. Yet, in view of the time needed to adopt the proposal under the "co-decision" procedure, the business community strongly encourages European and



national policy-makers to implement key principles of the new directive already, in order to provide effective relief to companies in the current crisis.

Payment by public authorities

We appreciate in particular, that the issue of late payments in commercial transactions between businesses and public authorities is addressed with the imposition of stringent sanctions in case the payment is not made within 30 days. Indeed, business considers that public authorities at all levels should lead by example in their payment behaviour.

We also appreciate the proposals to reduce the administrative burden for companies that experience late payments by entitling the creditor to interest for late payment without the necessity of a reminder.

Terms in business-to-business transactions

As regards payment terms in business-to-business transactions, BUSINESSEUROPE stresses the need to uphold contractual freedom so that conditions of payment terms can be negotiated freely. Of course, it is a sign of responsible business behaviour that these terms are respected. But since late payment is a symptom of liquidity problems rather than unwillingness to pay, the increase in sanctions is unlikely to affect clients' readiness to pay. When funds are available, normally payment is effected promptly. But national bodies should nevertheless monitor and publish clients' payment periods in those sectors where the risk is highest that small suppliers suffer from the abuse of larger clients' market power.

Legal recourse in case of late payments

The assumption that weaker parties take legal recourse in case of late payments themselves seems unrealistic. Companies are rarely keen to take judicial recourse against customers through fear of losing future contracts. Hence, widening the choice of punitive measures and increasing fines might not be effective in the absence of an efficient and independent framework for enforcement.

Instead, policy makers should reflect in how far efficient, market-based structures that publicly state companies' average payment delays could create necessary incentives and encourage better payment behaviour without creating undue additional costs.

In this respect, the UK's "Prompt Payment Code" and the respective website might serve as one example of an efficient, market based instrument to improve payment behaviour.

In addition to the general reflections, BUSINESSEUROPE has the following comments on several articles of the proposal.

Article 2: Definitions

- Article 2.2: "Public authorities" are defined by referring to Directive 2004/18/EC, which also defines the meaning of "contracting authorities" and "bodies governed by public law".

It would be helpful to clarify, if the above-mentioned entities comprise companies that, although they are governed by private law, are "financed, for the most part, by the state, regional or local authorities, or other bodies governed by public law; or subject to management supervision by those bodies, or having an administrative, managerial or supervisory board, more than half of



whose members are appointed by the State, regional or local authorities or by other bodies governed by public law” as in Article 1.9 of Directive 2008/18/EEC.

- It would also be useful to define the concept of “debt” as referred to in Article 4.1 in order to clarify if it comprises just the amount of the product or service inserted in the invoice, or if that amount includes the VAT or even other costs (e.g. transportation).

Article 3: Interest in the case of late payment

Articles 3.2 b and 5.2 b: In the absence of an agreement on the date or a period for payment, the date determining if interest can be charged depends on the receipt of the invoice or of some other request for payment, which should be clearly defined. If the contractual partner denies having received the invoice, it will be extremely difficult for the supplier to prove receipt of the invoice or of the request for payment, which could only be solved with expensive certified mails or the implementation of electronic invoices.

Hence, the starting point for the 30-day period should be the day when the creditor has sent his invoice or other request for payment as this can be proven more easily.

Article 4: Compensation for recovery costs

Although providing for reasonable compensation of recovery costs due to late payment is welcomed in principle, this article has been received with caution. Claiming further compensation arising from late payment recovery costs is already possible under several national laws. provisions as in Article 4 are not needed for all 27 member states. However, harmonisation of existing national laws should be accelerated.

Fixing at EU level the amount of recovery costs, which can be claimed in addition to overdue interest and without any proof, creates grave concerns.

Furthermore, costs and administrative efforts of recovery do not necessarily increase with the size of the unpaid claim and certain amounts in this article appear disproportionate.

BUSINESSEUROPE therefore suggests revising this article. It would make more sense to stipulate a compensation entitlement only for verifiable recovery costs in the case of wrongful late payment. .

Article 5: Payment by public authorities

Explicitly including public authorities in the scope of the directive is a step in the right direction. But to really be effective, it is essential to provide for an independent sanction mechanism for public authorities that pay late. Companies, and in particular SMEs, will find it almost impossible to charge interest on big public clients.

Article 5 envisages a lump sum compensation of 5% of the amount due in the case of late payment by public authorities as soon as interest for late payment can be claimed. This compensation is intended to be paid in addition to the interest for late payment. However, it is not clear if further compensation over and above the flat rate of 5% is possible, provided the claim can be verified.

Article 6: Grossly unfair contractual clauses and practices



Article 6 tightens the rules on grossly unfair contract clauses and these are welcomed in general. However the question of enforceability on private transactions remains.

As regards the definition, of unfair clauses, courts should assess each case individually and on the basis of the criteria laid down in Article 6.1. A legal definition of when a clause can be deemed grossly unfair is not desirable.

The provision of empowering associations on the basis of national law to take action in the courts or vis-à-vis authorities so that grossly unfair clauses are no longer used should be removed. In our view, the claims can be enforced by individual lawsuits and EU regulation does not seem necessary.

Article 8: Retention of title

Retention of title has very much proved its worth as a means whereby suppliers can safeguard credit. In practice it would be beneficial if its character as a safeguarding instrument were to be emphasised as a reservation by the supplier regarding transfer of ownership. The reference here to a clause expressly agreed before supply of the goods makes the handling of this instrument difficult. A simplification could be brought about by adding wording at the end of Article 8 section 1 along the following lines: "... if the seller has clearly reserved the transfer of ownership of the goods supplied vis-à-vis the buyer."