DISPUTE RESOLUTION FOR BUSINESSES

Debt recovery – late payment of commercial debts

Businesses depend on cashflow in order to make them successful and allow them to continue to run. Being paid on time by customers is key to businesses, as this allows them to pay suppliers and their staff.

Most businesses will have terms and conditions with their customers detailing the time in which invoices should be paid. But what remedies are available to you when a customer continually pays invoices late?

If a customer continually pays invoices late, then the business may, as well as being able to bring proceedings for payment of the invoice itself, also be able to bring a claim for interest and compensation pursuant to the Late Payment of Commercial Debts (Interest) Act 1998 (as amended) ('the Act').

Under the Act, a business can recover interest and compensation for each invoice that is paid late and outside of any agreed payment terms. As the interest and compensation are payable per invoice, this can add to up quite large additional sums of money, especially in cases where there are a large number of invoices which have not been paid, or have been paid late, but outside of the agreed payment terms.

HOW MUCH INTEREST AND COMPENSATION CAN I RECOVER?

Interest is payable at a fixed rate and is simple interest, not compound. The rate is set twice a year and is based on 8% above the Bank of England's base rate as at 30 June and 31 December. For example, for invoices where interest starts to run between 1 January and 30 June, the rate will be based on 8% above the base rate as at 31 December the previous year.

As soon as interest begins to run, a fixed sum is also payable in addition to the interest on the debt. The amount of the fixed sum compensation depends on the value of invoice that is outstanding or that was paid late:

- £40 fixed sum for invoices under £1,000
- £70 fixed sum for invoices of at least £1,000 but under £10,000
- £100 fixed sum for invoices of £10,000 or more

As you can see from the above, if you have a large number of invoices that have not been paid, or have been paid late (and outside of agreed payment terms), the compensation element could be substantial. Indeed, it does not even matter if the value of the invoice is below £40, you are still entitled to recover the minimum fixed sum of £40 for each invoice that has been paid late. For example, if a food supplier provided food supplies to a restaurant and invoiced them ten separate invoices for £25 each, and those invoices were paid late, the supplier would be entitled to compensation of £400 (as well as interest), even though the total value of the invoices was only £250. If, however, the supplier invoiced all the products on one single invoice for £250, then the compensation payable would only be £40.

SHOULD I BRING A CLAIM FOR A LATE PAYMENT COMPENSATION AND INTEREST?

Even though it is your statutory entitlement to recover interest and compensation for each invoice that is paid late, suppliers may wish to consider whether they wish to pursue a claim, especially in cases where invoices have been paid, albeit late and outside of agreed terms. Even if an invoice is paid only a couple of days late by a customer, the supplier is still entitled to interest and compensation on that invoice. However, suppliers need to consider whether proceeding with such a claim will affect any ongoing relationship they have with that customer, who may decide, after being presented with a claim, to take their business elsewhere.

If you are no longer conducting business with that customer (due to the fact they were continually bad payers), then there appears to be fewer reasons as to why you would not bring a claim, although you may wish to consider whether that customer would then tell other customers in the same marketplace, which could reduce your business reputation.

Notwithstanding the above, the threat of bringing claims for late payment interest and compensation can be used as a good tool for securing payment of invoices that have not been paid. You may wish to tell a customer that unless they pay the unpaid invoice(s) by a certain date, you will issue a claim against them, not only for the unpaid invoice(s) but also to recover late payment interest and compensation. As set out above, where there are a number of low value invoices, all of which remain unpaid, the amount of interest and compensation due could be at a similar level to the value of the invoice(s) or in some cases, exceed the value of the invoice(s).

DOES THE ACT APPLY TO ME?

The Act only applies to business-to-business contracts for the supply of goods and services. As such, there has to be a contract between the parties. This need not be in writing, but can be based on oral agreements or conduct.

However, both parties need to be acting in the course of their business for the Act to apply. Consumer Credit Agreements are excluded.

There are a number of excluded contracts, such as employment contracts or security contracts (such as mortgages and charges), and there has to be monetary consideration for the supply of goods or services. The Act only applies to contracts in England, Wales, Scotland and Northern Ireland. The Act does not apply to contracts made before 1 November 1998. For contracts between 1 November 1998 and 1 November 2002, the Act may apply depending on the size of the businesses. However, for contracts after 1 November 2002, the Act applies.

The right to interest and compensation will only apply where the contract between the parties does not provide for any contractual right to interest/compensation or the right to interest under the contract is not considered to be a 'substantial remedy' (see further below). If there is however a clause that relates to late payment in the contract, then the parties will usually be obliged to follow such provisions unless it is not a substantial remedy. For example, there may be a clause in the contract which states that in the event of late payment, the supplier can charge 8% interest on any late paid invoices. If this is the case, then the parties must follow the agreed clause rather than adopt the Act, which means that the supplier would be able to recover some interest, but would lose out on the right to claim the fixed sum compensation for each invoice.

What constitutes a 'substantial remedy' will be based on the time the contract was made and whether the sums provided were sufficient and fair to compensate the supplier for the late payment. A Court may also look at the payment terms, the bargaining strength of the parties, whether one party imposed the term on the other, and the base rate at the time the contract was agreed. It will therefore depend on the individual circumstances of each matter as to whether the contract contains a substantial remedy or whether the supplier can instead rely on the provisions of the Act.

There have been some cases where 'substantial remedy' has been considered. The case law seems to suggest a rate of somewhere between 3 - 5% above base rate could be a substantial remedy, despite it being lower than the sums that a supplier is entitled to under the Act. However, as set out above, it all depends on the individual cases and the circumstances under which the contract was negotiated.

WHEN MIGHT A COURT REDUCE THE AMOUNT OF INTEREST DUE?

Customers will often argue that the reason they have not paid an invoice or paid invoices late was due to the conduct of the supplier. For example, they may say the supplier did not provide invoices on the same day as they are dated, or did not provide any additional information requested to allow the customer to properly reconcile those invoices.

If this is the case, the Courts have the power to review the conduct of the supplier and can reduce the amount of interest paid on each invoice, even down to zero, if they believe the supplier's conduct is the reason behind the late payment. Again, each case will be determined on its own individual circumstances.

The Court does not have the power however to reduce the fixed compensation sum, namely the £40, £70 or £100 fixed sum.

WHEN DOES INTEREST START FROM?

This depends on whether the contract provides for an actual agreed payment date (i.e. 30 days after the date of the invoice) or when there is no agreed payment date in the contract.

Where there is an agreed payment date, the interest starts to run on the day after that payment date has passed. If for example, the payment date is the end of the month, interest can start to accrue on any invoices that have not been paid from the first day of the following month.

Where the contract does not provide for an agreed payment date, then the Act implies a 30-day payment period from the latest date of delivery of the goods/services, the invoice or any acceptance procedure (such as time allowed to check the quality of the goods). Interest starts to run after the expiry of this 30-day period. For example, if a supplier supplies goods and then invoices for those goods a week later, the 30-day period for payment will only start after the invoices have been provided to the customer.

It is possible for businesses to agree a later payment date than provided for by the Act, such as 60 days from the date of the invoice, before interest starts to accrue. However, if too long a payment date is set out in the contract, a Court may deem the same to be grossly unfair and therefore invalid. In such cases, the Court will then apply the 30-day payment period. Again, the Court will consider the circumstances of each case and the relative bargaining/negotiating positions of each party and what may be the commercially acceptable standard for that industry before determining if the payment terms are grossly unfair.

WHEN DOES INTEREST END?

Interest will stop accruing when the principal debt (or invoice) is paid. As set out above, the Act applies to not only unpaid invoices, but also to invoices that have been paid, but paid late and outside of any agreed payment terms. As such, interest and compensation due under the Act can still be claimed even if the invoice itself has been paid, as long as the invoice was paid late. Businesses can go back six years to pursue late paid invoices. However, the supplier will need to consider if it is in the interests of their business as to whether they want to pursue an existing customer for old late paid invoices under the Act.

GET IN TOUCH

Mark Ovenell
PARTNER
Dispute Resolution
E: mark.ovenell@bindmans.com
T: +44 20 7833 4433

> The lawyers have incomparable client service skills. They are very clear and always make sure they understand the picture, even if it is a complicated one.

CHAMBERS AND PARTNERS 2022

BINDMANS LLP
236 Gray’s Inn Road | London | WC1X 8HB
T: +44 20 7833 4433 | E: info@bindmans.com | W: bindmans.com

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