LEGISLATIVE INTEREST ON LATE PAYMENT

1. BACKGROUND

Since 2002, all businesses, including public sector organisations have been entitled to claim interest and compensation on late payments under non-consumer contracts. On 16 March 2013, new rules were introduced. A party to a commercial contract can claim (a) compensation, (b) interest and (c) reasonable costs of recovery.

2. HOW DOES THE ACT WORK?

If a non-consumer contract does not comply with the minimum requirements of the Act, the default system in the Regulations apply.

The definition of a late payment according to the Act is,

"where the agreed credit period given by the supplier to the purchaser has expired"

3. WHEN DOES INTEREST RUN FROM

If the exact period has not been mentioned in the contract, the Act applies a default period of 30 days after which interest will accumulate.

The 30-day period runs from either:

1. The delivery of the goods or the performance of the service
   If a contract between the parties specifies that there is no credit period, the main debt will be due as soon as the goods are delivered or the service has been performed.
2. The day the purchaser receives notice of the debt
   If there is no payment period after invoice the debt is due immediately.

In cases, where the goods or services are being delivered in advance, the interest will apply from when part of the goods or services were delivered or performed.

In a commercial construction contract, the Construction Act will usually apply and the relevant final date for payment will be the date on which payment should be made and interest will be payable if payment is not made.[1]

[1] The Construction Act Scheme applies to non-compliant contracts or the parts of contracts that do not comply. Under the scheme the contracts must provide for: Payment Due Date and Final Date for payment (S110), Payment Notice or Pay-less Notice (S110(A)(B) and S111). Accordingly, where contract does not specify the interest to be paid after the final date for payment, statutory interest will apply at 8% on top of the outstanding balance.

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4. WHAT IS THE MAXIMUM PERIOD FOR DELAYING PAYMENT?

Public sector contracts now have a maximum 30-day period for payment from invoice, and other non-public sector contracts, a 60-day period[2]. The Regulations describe acceptable periods for delayed payment in public sector supply chains. Parties can agree longer periods for payment so long as the period is not 'grossly unfair' – what is considered 'grossly unfair' has to date not been defined. The new payment commitments apply to all parties on central Government contracts, whether they are signatories to the Payment Charter[3] or not, as a result of the Public Contracts Regulations 2015.

5. INTEREST

The rate of interest that can be charged on late payments is to be agreed, but it must be a 'substantial remedy' – if no rate is agreed the Regulations import a default rate of 8% above the Bank of England base rate for business to business transactions.[4]

BASE RATE	6 MONTH PERIOD
The Bank of England base rate on 31 December will be the 'reference rate' for	1 January to 30 June
The Bank of England base rate on 30 June will be the 'reference rate' for	1 July to 31 December

It is common in construction contracts to see this rate reduced to 5%, but we would argue that nothing less should be acceptable.

The interest is simple, i.e. not compounded when calculated, e.g.:

Debt x interest rate x the number of days late 365

[2] Payment of undisputed invoices within 30 days by contracting authorities, contractors and sub-contractors under Regulation 113 Public Contracts Regulations 2015. In the event of an undue delay (i.e. not confirming an invoice as valid and undisputed within the suggested 7 calendar days), the invoice shall be regarded as valid and undisputed. The Regulations can be found here: **http://www.legislation.gov.uk/uksi/2015/102/regulation/113/made**

[3] The construction supply chain payment charter guide can be found here: **Charter guide**

[4] More on Late Payments can be found here: **Claiming Interest**

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6. COMPENSATION & COSTS OF RECOVERY

The creditor is entitled to a fixed penalty charge from the debtor and has up to 6 years to claim, depending on the sum owed, plus additional reasonable costs incurred, ('reasonable costs' may include the costs of legal advice and debt recovery).

SIZE OF THE UNPAID DEBT	THE COMPENSATION
Debt owed up to £999.99	£40
Debt owed £1000 - £9,999	£70
Debt owed £10,000 or more	£100

7. PERIOD FOR CLAIMING

You have up to 6 years in which to make a claim for the late payment compensation, interest and costs of recovery. The interest can be claimed on invoices that were not paid within the credit period but have since been paid. The interest can be claimed for the period starting with the day the invoice should have been paid and ending with the date it was paid.

8. SUMMARY – NEGOTIATING STRATEGY

Essentially, the right to (a) compensation, (b) interest and (c) reasonable costs of recovery, is a deterrent to debtors from failing to pay creditors on time as debtors will face residual liability for debt, compensation, interest, and recovery costs.

It therefore affords the creditor commercial leverage to get paid on time. The debtor when entering the contract should not seek to argue to reduce the interest rate as to do so would be to indicate at the pre-contract stage that it might be likely to breach its payment obligations under the contract – further, it cannot contract out of the legislation. In reality, the bigger the interest rate the bigger the warning to the debtor that failure to pay will result in adverse commercial consequences.

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