



Interest on Commercial Debts

The Late Payment of Commercial Debts (Interest) Act 1998 provides that interest is automatically payable on late payments under most commercial contracts. Before that Act, there was no automatic right to interest on the late payment of a debt.

What contracts are covered?

All contracts for the supply of goods or services where both parties are acting in the course of business. Employment contracts are not covered by this definition, and certain other contracts such as mortgage contracts are excluded. "Business" includes government departments and local and public authorities.

What statutory rights does the supplier have?

If payment is late, the supplier can claim:

- interest on late payment; and
- debt recovery costs.

When is payment late?

Payment is late if the debt has not been paid by the agreed date for payment or, if no payment date has been agreed, 30 days after the goods or services are supplied and an invoice has been rendered.

How is the interest calculated?

Simple interest accrues on the gross debt (i.e. including VAT) from the date it becomes late, calculated on a daily basis until the debt is paid.

The statutory rate of interest is 8% above base, fixed for six-month blocks each year as follows:

- the rate on 31 December applies for the following January to June; and
- the rate on 30 June applies for the following July to December.

What can be claimed for debt recovery costs?

Amount of Debt	Recovery Costs
less than £1,000	£40
£1,000 to £9,999.99	£70
over £10,000	£100

Can statutory interest and debt recovery costs be avoided?

The principal aim of the Act is to protect small businesses from suffering at the hands of larger businesses who abuse their position by paying their bills late. The Act therefore contains extensive provisions designed to prevent businesses contracting out of the statutory provisions.

Businesses can agree alternative penalties for late payment with each other, but these will only exclude the right to statutory interest and recovery costs if they are realistic penalties, and not if they are merely artificial provisions designed to frustrate the supplier's statutory rights.

Note however that the Act gives businesses rights to claim statutory interest and recovery costs. Businesses are not obliged to exercise those rights.

What action should be taken?

All businesses should review their standard terms of business in light of the Act, with particular attention to credit periods and penalties for late payment.

This is a general guidance note giving a brief overview of the Act only and detailed advice is recommended before relying on its terms. For further advice please contact Derek McCulloch or Chris Smith in our Corporate Department on 0131 225 1677.