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Review article

NEW EUROPEAN REGIME FOR COMBATTING LATE PAYMENTS IN COMMERCIAL TRANSACTIONS – KEY ELEMENTS OF REVISION AFTER A DECADE

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ABSTRACT

It has been a decade since the Late Payment Directive (2011/7/EU) came into force. At the time of its adoption and implementation into the legislation of Member States marked by the circumstances of a less digital world, it provided legal certainty and protection to small and medium-sized enterprises in case larger or more powerful businesses failed to fulfil their financial obligations on time. Business digitization, geopolitical events, and inflation have influenced entrepreneurs' operations and their decision-making in the allocation of financial resources, indirectly leading to a disruption of payment culture and an increase in the number of unpaid invoices. According to available data from the European Payment Report, late payments affect entrepreneurs in all sectors and all Member States, with small and medium-sized enterprises, the generators of the European Union's gross domestic product, being the most affected. In order to address this growing issue, the European Commission has presented a proposal for revised rules on late payments at the end of 2023. The paper analyses secondary data to answer the question of the effectiveness of existing rules in preventing late payments and highlights the most significant elements of the new Regulation proposal. By comparing existing and revised legal solutions, paper addresses whether the new rules can solve this problem.

Keywords: *Commercial transactions, Competitiveness, Late payments, Regulation*

1. INTRODUCTION

Commercial transaction serves "to transmit economic values such as materials, products, and services from those who want to exchange them for another value, usually money, to those who need them and are willing to pay a countervalue."[1]

[1] Drobnig, U. M. *Encyclopedia Britannica*. 2022. [https://www.britannica.com/topic/commercial-transaction], Accessed 1 March 2024.

The fulfilment of obligatory relations is consistently aimed at achieving them as swiftly as possible. This is because the exchange of goods and the establishment of equilibrium are their underlying purposes. Therefore, the deadline for discharging obligations is a crucial requirement for a lawful fulfilment of duties.[2]

Late payments in commercial transactions represent a significant challenge for businesses, particularly small and medium-sized enterprises (SMEs), by exacerbating liquidity problems, increasing operational costs, and potentially leading to insolvency. The financial crisis of the late 2000s and subsequent economic downturns, including the COVID-19 pandemic, have highlighted the severity of late payments' impact on business stability and growth.[3]

Statistical analyses reveal that a large proportion of businesses across Europe, suffer from late payments, with variations in the intensity and frequency of such occurrences across different EU countries.[4]

Despite legislative measures like Directive 2011/7/EU aimed at reducing late payment durations across the EU, significant disparities remain. Southern European countries typically experience longer delays compared to their Northern counterparts.[5] This indicates a need for a more robust and uniformly enforced regulatory framework.

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2 Gorenc, V. V*rijeme ispunjenja obveze (može li se rastuća nelikvidnost ukloniti donošenjem "novih" propisa o roku plaćanja)*, Računovodstvo, revizija i financije 2009., pp. 171-174.: 171; Gorenc, V. (2011), Rokovi ispunjenja novčanih obveza od 1. siječnja 2012., Računovodstvo, revizija i financije 2011., pp. 140-145; Gongeta, S., *Combating late payments in commercial transactions–the case of Croatia*, *Economic Integrations, Competition and Corporation*, 2014, pp. 116-117; Krahmer, J. *Commercial Transactions,* 38 Sw L.J. 207 (1984), [https://scholar.smu.edu/smulr/vol38/iss1/10].

3 Gołaś, Z.; Gołaś, J. *Late payments in Poland: economic and legal perspectives*. European Research Studies Journal, XXIV (Special Issue 1), 2021. pp. 90-106. [https://doi.org/10.35808/ersj/2031]; McLoughlin, D. Commercial Transactions. Golden Gate University Law Review, vol. 8, no. 1, 1977, pp. 43-54.; Miller, T.; Wongsaro, S. *The Domino Effect: the impact of late payments,* 2017 Plum Consulting London; Nicolas, T. *Short-term financial constraints and SMEs' investment decision: evidence from the working capital channel*, Small Business Economics, 2021.

4 According to the EU Payment Observatory p. 14 „in Poland, almost two thirds of all surveyed enterprises indicate facing issues due to late payments (65 %). The percentage is above 60 % in Cyprus (64 %) and Czechia and Malta (61 %). At the other end of the spectrum, the figure for Bulgaria and the Netherlands is less than half of that (25 %). Austria and Sweden are ranked third in performing better (32 %). Two out of the four big European economies, namely Italy (52 %) and France (47 %) seem to have a higher than European average number of companies suffering from late payments (43 %), while the opposite is true for Spain (36 %) and Germany (33 %). Remarkably, the smallest economies in the European Union occupy the top spots, with Cyprus (64 %), Malta (61 %) and Luxembourg (53 %) all landing among the 6 countries indicating the largest issues with late payments".

5 Maque, I.; San-José, L. *Understanding and solving late payment: the role of organizational routines*. Management International, 2018, Vol. 22, No. 1, pp. 146-156. [https://doi.org/10.7202/1053694ar]; Gołaś, Z.; Gołaś, J. *op cit.* note 3.

Efforts to address late payments require a multifaceted approach, including legislative policies, active enforcement provisions in contracts, and the use of organizational routines to understand and tackle late payment as an organizational phenomenon.[6]

The legislative and policy measures undertaken by the European Union aim to create a more predictable and secure commercial environment conducive to timely payments.[7]

To protect European businesses, particularly SMEs, against late payment, the European Union adopted Directive 2011/7/EU on combating late payment in commercial transactions in February 2011.[8] This Directive, which repealed the earlier Directive 2000/35/EC[9], introduced several key measures, such as payment terms, statutory interest, compensation for recovery costs and unfair contract terms.

Initially, in a comparatively less digital era, it established legal clarity and safeguarded small and medium-sized enterprises (SMEs) against delayed financial commitments from larger or more influential businesses. However, the landscape of business operations and financial decision-making has evolved, influenced by digital transformation, geopolitical shifts, and inflationary pressures. These changes have indirectly disrupted payment practices, leading to a surge in unpaid invoices.[10]

In response to this escalating challenge, in September of 2023, the European Commission proposed a Regulation on combating late payment in commercial transactions[11], an updated regulation on late payments.

The main objectives of the Proposal can be condensed into several policy areas preventing late payment from occurring – equally by introducing stricter enforce-

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6 *Ibid.*

7 Peel, M. *et al.*, L*ate payment and credit management in the small firm sector: some empirical evidence*. International Small Business Journal Researching Entrepreneurship, 2000, Vol. 18, No. 2, pp. 17-37. [https://doi.org/10.1177/0266242600182001].

8 Directive 2011/7/EU of the European Parliament and of the Council of 16 February 2011 on combating late payment in commercial transactions (recast) Text with EEA relevance OJ L 48, 23 February 2011, pp. 1–10.

9 Directive 2000/35/EC of the European Parliament and of the Council of 29 June 2000 on combating late payment in commercial transactions OJ L 200, 8 August 2000, pp. 35–38.; No longer in force, Date of end of validity: 16/03/2013.

10 Huertas, M., The EU's Late Payments Regulation proposal – key points and problems, 2023, https://legal.pwc.de/en/news/articles/the-eu-s-late-payments-regulation-proposal-key-points-and-problems

11 Proposal for a Regulation of The European Parliament and Of The Council on combating late payment in commercial transactions (Text with EEA relevance) Strasbourg, 12 September 2023 COM (2023) 533 final 2023/0323 (COD).

ment measures, facilitating timely payments and strengthening redress mechanisms, ensuring fair payment conditions and empowering companies.[12]

The revision is primarily motivated by the need to address shortcomings in the existing EU legal framework concerning late payments, which significantly affect SMEs due to asymmetries in bargaining power between large clients and smaller suppliers.

These shortcomings include inadequate preventive measures, insufficient deterrents, and ineffective enforcement and redress mechanisms within Directive 2011/7/EU on combating late payments. The ultimate aim is to improve payment discipline across all actors (public authorities, large companies, and SMEs) and protect companies from the negative effects of payment delays in commercial transactions.

2. CONTEMPORARY SMES CHALLENGES WITH LATE PAYMENTS IN THE UNITED KINGDOM AND EUROPEAN UNION – A COMPARISON

Tot[13] and Gongeta[14] highlight that late payments can lead to severe consequences for businesses, including cash flow problems, increased borrowing costs, and even insolvencies. In the construction industry, these issues are particularly acute, prompting the exploration of technological solutions like smart contracts to mitigate such negative outcomes.[15] Elghaish *et al.* further emphasize the importance of addressing late payments to foster business growth and sustainability.

To provide a comprehensive analysis on the impact of late payments on the development and growth of businesses across Europe, including a special focus on the United Kingdom the data from the European Payment Report 2023 are used. This report, yearly published by Intrum UK, is based on insights from over 10.000 C-level executives and explores how businesses are managing liquidity issues amidst economic disruptions and all the statistical data presented in this chapter are based on that report.

The report indicates that UK businesses are particularly pessimistic about inflation, with a higher percentage (68%) finding it difficult to pay suppliers on time

12 Huertas, M., *op. cit.*, note 10.

13 Tot, I. *Late Payment Directive : Recent and Pending Cases at the Court of Justice* // InterEULawEast, 3 (2016), 2; pp. 71-86.

14 Huertas, M., *op. cit.*, note 2.

15 Elghaish, F. *et al.*, *Integrated project delivery with blockchain: an automated financial system*. Automation in Construction, 2020. p. 114, 103182. [https://doi.org/10.1016/j.autcon.2020.103182].

due to inflation, compared to the European average of 56%. This suggests a more acute impact of inflation on UK businesses, likely exacerbated by local economic factors and Brexit implications.

The UK's outlook on inflation stabilization is more pessimistic than the European average. A significant 38% of UK respondents believe it will take more than two years for inflation to stabilize below 2%, compared to 26% on average in Europe. This highlights a more cautious or realistic assessment of economic recovery within the UK.

The concern over late payments is a common theme across Europe, but the UK exhibits particular challenges, with 61% of businesses expecting late payments to increase. The payment gap has widened significantly in the UK, signalling a worsening trend that affects cash flow and financial stability.[16]

Also, the report emphasizes that 65% of UK businesses are taking steps to reduce credit risk, similar to the European trend. The reliance on early arrears and working with debt collection agencies is notably high in the UK, reflecting a proactive approach to mitigating the impact of late payments.

Despite economic pressures, both UK and European businesses are maintaining their commitments to sustainability. However, the UK shows a slightly higher acceleration in sustainability efforts (64% vs. the European average of 58%), possibly driven by stringent regulatory standards and consumer expectations in the UK.[17]

Digital transformation is identified as a strategic priority for UK businesses (77%) more than the European average (67%). This underscores the UK's focus on leveraging technology to navigate economic uncertainties, improve payment practices, and enhance operational efficiency.

Like their European counterparts, UK businesses are prioritizing cost-cutting and improving efficiency. However, the emphasis is stronger in the UK (80% vs. 72% European average), indicating a more intense pressure to optimize operations amidst financial strains.[18]

The UK's approach of sacrificing growth for efficiency reflects broader European trends, where businesses prioritize immediate survival over expansion. The strategic shift towards efficiency, liquidity, and risk management echoes across Europe, albeit more pronounced in the UK due to its unique economic challenges.

16 European Payment Report 2023. p. 12.

17 *Ibid.* p. 16.

18 *Ibid.* p. 18

According to European Payment Report for the 2023, United Kingdom uses various strategies and measures implemented to combat late payments, a pressing issue impacting the cash flow and financial sustainability of businesses. To address this, UK businesses have prioritized cutting costs (80%) and strengthening liquidity (79%) as their top strategies.

The same Report shows that significant 65% of respondents have initiated steps to reduce credit risk and focus on managing late payments, with a particular emphasis on tackling early arrears - 78% of businesses are adopting this approach.

The Report highlights the challenges businesses face due to outdated technology and lack of in-house expertise in managing late payments.

Despite the urgent need to upgrade technology platforms for better debt management, 54% of businesses are hesitant to make such investments in the current uncertain economic climate.

Similarly, 55% of respondents expressed a desire to improve their late payment management practices but found it difficult due to a lack of resources and expertise.

Businesses are also leveraging the European Late Payment Directive, with 50% using its provisions to charge fees and interest for late payments, an increase from 46% in the previous year. This reflects the growing issue of payment delays that companies are facing.

Businesses report dedicating significant time and resources to chasing late payments, with UK companies spending an average of 71 days a year on such activities.

In combating late payments, the Report suggests that businesses are stuck between the necessity to cut costs and the need to invest in improving payment processes. While many focus on early arrears to mitigate larger losses, the lack of proper systems and expertise remains a substantial barrier.

Despite these challenges, there's a noticeable effort among businesses to maintain ethical standards and prompt payment cultures, with 35% having a code of ethics in place to encourage timely payments.[19]

Presented data from the European Payment Report 2023 underscores the critical need for effective measures to address late payments. These data suggest that while existing rules like the European Late Payment Directive are utilized, their effectiveness in preventing late payments is limited. The continued high incidence of

[19] *Ibid.*

late payments, significant time spent chasing payments, and reliance on reactive measures (early arrears, debt collection) point to the need for more robust and preventive regulations. The adoption of digital invoicing solutions and technological advancements can significantly improve payment practices, enhancing the financial stability and growth of SMEs across Europe.

3. THE EVOLUTION OF THE EU'S LATE PAYMENTS LEGISLATIVE POLICY

SMEs are often described as the backbone of the European economy, providing a substantial portion of jobs and significantly contributing to innovation and economic growth.[20] However, their size and negotiating power can put them at a disadvantage in commercial transactions, especially when dealing with larger companies or public authorities. Late payments can strain their liquidity, limit their ability to invest and grow, and in severe cases, lead to insolvency.

The issue of late payments exacerbates the risk aversion of SMEs, making them more reluctant to engage in cross-border transactions due to concerns over payment reliability in different jurisdictions. This hesitancy undermines the European Union's efforts to encourage a more integrated and competitive single market.[21]

Latest researches show a significant discrepancy between the expressed opinions on the need for timely payments and the actual payment behaviours of the surveyed micro-enterprises. Late payments are perceived as unethical by a vast majority of respondents, who also agree that such practices tarnish the debtor enterprise's image, undermine trust with business partners, and deteriorate the quality of relationships with suppliers. The majority of micro-enterprises acknowledge the necessity of making timely payments to suppliers, though nearly half believe that delaying payments can be justified under certain circumstances.[22]

Recognizing the gravity of this issue, the European Union has sought to address it through legislative measures, notably with the Directive 2011/7/EU on combating late payment in commercial transactions.

The theme of payment behaviour attracted considerable attention from European decision-makers. In its Resolution of 17 January 2019 on the implementation of

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20 Proposal for a Regulation of The European Parliament and Of the Council on combating late payment in commercial transactions (Text with EEA relevance) Strasbourg, 12 September 2023 COM (2023) 533 final 2023/0323 (COD).

21 *Ibid*.

22 Ziętek-Kwaśniewska K., *The problem of late payments in the opinion of micro-enterprises*. Prace Naukowe Uniwersytetu Ekonomicznego We Wrocławiu 2017(478): pp. 463-471. [https://doi.org/10.15611/].

the Directive 2011/7/EU, the European Parliament had called on the Commission and the Member States to foster "a decisive shift towards a culture of prompt payment." The theme also featured prominently in the SME Strategy adopted by the Commission in 2020, which noted the need for "a decisive shift towards a new business culture in which prompt payment is the norm." Accordingly, the Commission committed to supporting the implementation of the Late Payment Directive by equipping it with strong monitoring and enforcement tools.[23]

The Study on building a responsible payment culture in the EU – Improving the effectiveness of the Late Payment Directive, aimed to collect evidence and provide inputs on a series of possible actions to foster the effectiveness of the Directive 2011/7/EU.

The work was articulated in 6 thematic areas, dealing with identifying the conditions for creating an EU observatory on payment behaviour[24]; facilitating the uptake of financial tools[25] addressing the issues originated by poor payment behaviour and fostering the use of e-invoicing; facilitating access to credit information on prospective clients[26]; implementing synergies between public procurement and prompt payment objectives[27]; fostering the use of Alternative Dispute Resolution tools to settle payment delays disputes[28]; and enhancing SMEs' credit management capabilities.[29]

In light of the inadequacies of the 2011 Directive on combating late payments, the European Commission's thorough assessments and consultations have highlighted the need for a regulatory overhaul. The existing framework's shortcomings, notably its failure to introduce effective preventive, enforcement, and redress measures, have prompted the Commission to propose a new Regulation aimed at instilling fairness and enhancing the resilience of SMEs and the supply chain at large.[30]

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23 European Commission, Directorate-General for Internal Market, Industry, Entrepreneurship and SMEs, Study on building a responsible payment culture in the EU – Improving the effectiveness of the Late Payment Directive (2011/7/EU), Publications Office of the European Union, 2022, [https://data.europa.eu/doi/10.2873/34185].

24 This would monitor and analyse payment practices across member states, providing a clear picture of compliance and areas needing improvement.

25 Addressing issues caused by poor payment behaviour through financial tools and fostering the use of e-invoicing.

26 Making credit information on prospective clients more accessible to SMEs.

27 Ensuring that public procurement policies support prompt payment objectives.

28 Promoting the use of these tools to settle payment delay disputes efficiently.

29 Providing training and resources to improve internal credit management practices.

30 European Commission, *op. cit.,* note 23.

The European Commission has taken a decisive step to tackle the chronic issue of late payments in commercial transactions, a problem that significantly impacts the financial health and survival of SMEs across the European Union.

With late payments being a contributing factor to one in four bankruptcies, the power imbalance between large corporations and their smaller counterparts has led to a culture of delayed payments, forcing many SMEs into precarious financial positions.

If we analyse the legislative framework for combating late payments in European member states, the measures established through legal acts can be classified into several main categories: Preventative measures[31], remedial measures[32], initiatives contributing to changing business culture[33], supportive measures in changing business culture[34] and other measures.[35]

For example, Austria in its Late Payment Act[36] included stricter payment terms, contract management, unfair contractual terms and the role of business organisations as part of regulatory framework. Also, in its Initiative named Payin7Days Petition, Austria provided something like an open letter, which launches a petition to reduce late payments. According to the letter, Austrian states (Land) and the federal government is lagging behind with on time payments. The petition aims to achieve better payment morale from the public sector towards businesses, especially SMEs.[37]

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31 Main preventative measures are stricter payment terms, transparency of payment practices, invoice management measures, e-Procurement, financial mechanisms, measures creating rights for suppliers, stricter payment terms in contracts between larger companies and SMEs, obligations for larger companies and public authorities, Restriction of access to public funds, introduction of specific criteria in public tender assessment, obligations for larger companies when conducting business with SMEs and provisions applicable to contracts where one party is a third country.

32 Main remedial measures are Alternative Dispute Resolution System, administrative sanctions, administrative sanctions protecting suppliers and measures creating rights for suppliers.

33 Main initiatives contributing to changing business culture include prompt payment codes, corporate social responsibility, credit ratings, credit management education and contract management.

34 Supportive measures in changing business culture are defining unfair contractual terms and the role of business organisations, awareness raising activities, labels and prizes, working groups, wording in soft law measures, endorsement of soft law measures, assessment criteria and disclosure commitments.

35 Compensation for recovery costs proportional to the size of the debt, legal provisions on the retention of title, tax regulations and assessment criteria can be classified as other measures.

36 Late payment Act, [https://www.ris.bka.gv.at/eli/bgbl/I/2013/50].

37 [https://www.ots.at/presseaussendung/OTS_20210425_OTS0019/offener-brief-republik-muss-den-zahlungsmoral-turbo-zuenden], Accessed 12 February 2024; EU Payment Observatory Repository: [https://single-market-economy.ec.europa.eu/smes/sme-strategy/late-payment-directive/eu-payment-observatory/observatory-documentation_en], Accessed 12 February 2024.

Belgium has adopted a strengthened Late Payment in Commercial Transactions Act starting Feb. 1, 2022[38]. It includes transparency of payment practices, stricter payment terms in contracts between larger companies and SMEs and contract management.

It is interesting that when speaking about combating late payments in commercial transactions, Bulgarian Law on Obligations and Contracts[39] with its preventive and "other measures" states "Albeit outside the time scopes of analysis, nevertheless a measure that is always relevant is the provision of the Law on Obligations and Contracts, stating that in case of non-fulfilment of a monetary obligation, the debtor owes compensation in the amount of the legal interest from the day of the delay". In Bulgarian Commercial Act which is in force since 20th of February 2013 it is stated that "parties to commercial contracts may agree on a term for payments in period of no more than 60 days unless the nature of the goods of services require a longer period. When a government entity is party to a commercial contract, this period is of a duration of no more than 30 days. If no payment term has been agreed upon, the monetary obligation must be fulfilled within 14 days of receipt of an invoice or other request for payment. A compensation in amount of 40 EUR is due for the costs of collection to the creditor who has fulfilled his obligations."[40]

Croatia has enacted a whole range of laws, mechanisms, and instruments for the purpose of enforcing the adherence to payment deadlines in commercial transactions.[41] The Law on Financial Operations and Pre-Bankruptcy Settlement[42] is the main piece of legislation transposing the Late Payment Directive. The Law changes the provisions related to the Kuna for the purpose of introducing the Euro. Also, regarding the reference rate that serves as the basis for determining interest on late payment, it is stipulated that the reference rate will be the interest

38 Act amending the Act of August 2, 2002 on combating late payment in commercial transactions [https://etaamb.openjustice.be/nl/wet-van-14-augustus-2021_n2021032597.html], Accessed 10 February 2024.

39 It is adopted and in force since 1991. [https://lex.bg/laws/ldoc/2121934337], Accessed 10 February 2024.

40 [https://lex.bg/laws/ldoc/-14917630], Accessed 10 February 2024.

41 For example Law on Electronic Invoicing in Public Procurement, Law on factoring, Documentation of the PD model and methodology for calculating the credit rating of entrepreneurs using machine learning applications (ML.PD), Guidelines for encouraging the participation of SMEs in the public procurement market, Law on public procurement, Preliminary assessment form for the Draft Law on deadlines for the fulfilment of financial obligations, Law prohibiting unfair trade practices in the food supply chain, Law on Obligations (including provisions on payments for contractual obligations), the National Insolvency Register as a publicly available electronic register which seeks to improve the provision of information to relevant creditors and courts about insolvency proceedings.

42 Official Gazette 108/12, 144/12, 81/13, 112/13, 71/15, 78/15, 114/22.

rate applied by the European Central Bank to its last main refinancing operations or the marginal interest rate resulting from tender procedures for a variable rate for the last major refinancing operations of the European Central Bank.[43]

In Denmark, key measures are stated in Act on Interest and Other Conditions in the event of Late Payment (Interest Act) introducing stricter payment term for G2B transactions[44][45] and Public Procurement Act introducing "dynamic purchasing systems".

3.1. Overview of the Directive 2011/7/EU

To protect European businesses, particularly SMEs, against late payment, the EU adopted Directive 2011/7/EU on combating late payment in commercial transactions in February 2011. and was due to be integrated into national law by EU

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43 EU Payment Observatory Repository: [https://single-market-economy.ec.europa.eu/smes/sme-strategy/late-payment-directive/eu-payment-observatory/observatory-documentation_en], Accessed 12 February 2024.

44 „The amendments to the Interest Act transpose the provisions of the Late Payments Directive into Danish national law. The Act sets out a stricter payment term for G2B transactions, by stipulating that the agreed payment period in an agreement where the debtor is a public authority cannot be more than 30 days (§3b(1)). Only one exception from this rule is allowed: according to §3b(2), "The Minister for Justice may, after consultation with the Minister for Business and Growth, lay down rules stipulating that the payment period referred to in paragraph 1 may be up to 60 days for public authorities carrying out economic activities of an industrial and commercial nature by offering goods or services on the market, where the authority as a public undertaking falls within the definition in Article 2(b) Directive 2006/111/EC on the transparency of financial relations between Member States and public undertakings and on financial transparency within certain undertakings." EU Payment Observatory Repository: [https://single-market-economy.ec.europa.eu/smes/sme-strategy/late-payment-directive/eu-payment-observatory/observatory-documentation_en], Accessed 12 February 2024.

45 "The Public Procurement Act deals with public procurement and tender procedures. While it does not mention the issue of late payments, it sets out the general framework of public procurement in the country, as well as establishes an e-procurement system. Particularly, §78(3) stipulates that "A contracting authority must arrange for the payment of remuneration in appropriate installments to the participating partners.""In addition, in §101-108 the Act establishes the concept of ""dynamic purchasing system"" (dynamiske indkøbssystemer), which are an electronic procurement process. This is applicable in the procurement of services that are generally available on the market and meet the requirements of the contracting entity. Moreover, the Act foresees that anyone who meets the minimum eligibility requirements and is not covered by the grounds for exclusion, must be included in the dynamic purchasing system. The contracting public authority is additionally obliged to continuously admit new participants to the system and cannot limit the number of participants. Finally, §109-115 cover ""electronic auctions"" and §116-118 deal with ""electronic auctions." EU Payment Observatory Repository: [https://single-market-economy.ec.europa.eu/smes/sme-strategy/late-payment-directive/eu-payment-observatory/observatory-documentation_en], Accessed 12 February 2024.

countries by 16 March 2013 at the latest.[46] The Directive established a culture of prompt payment within the EU, setting maximum payment periods and enforcing interest for late payments to deter the practice. It also allows for the recovery of reasonable recovery costs incurred through the pursuit of late payments, thus attempting to level the playing field for SMEs.

The directive applies to commercial transactions between undertakings, or between undertakings and public authorities, excluding transactions with consumers, payments under cheque and bill of exchange laws, and compensation for damages. It defines terms such as commercial transactions, public authority, undertaking, late payment, and "statutory interest for late payment".

The Late Payment Directive defines commercial transactions as "transactions between undertakings or between undertakings and public authorities which lead to the delivery of goods or the provision of services for remuneration."[47] Late payment is defined as "payment not made within the contractual or statutory period of payment".[48]

Undertakings are entitled to statutory interest for late payment if they have fulfilled their contractual and legal obligations and have not received payment within the agreed timeframe.[49]

Public authorities must pay their invoices within 30 calendar days (extendable under certain conditions to 60 days), ensuring quick compensation for creditors.[50]

Creditors are entitled to a minimum of EUR 40 as compensation for recovery costs, in addition to interest for late payment. They may also claim reasonable compensation for any recovery costs exceeding this fixed sum.[51]

Contractual terms or practices that grossly deviate from good commercial practice, contrary to good faith and fair dealing, or exclude the right to charge interest for late payment or compensation for recovery costs are deemed grossly unfair to the creditor.[52]

Member States must ensure transparency regarding the rights and obligations stemming from the directive and encourage awareness among undertakings about the remedies available for late payment.[53]

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[46] Maque; San-José, op. *cit.,* note 6.

[47] Art. 2. p. 1. Directive 2011/7/EU.

[48] Art. 2. p. 4. Directive 2011/7/EU.

[49] Art. 3. Directive 2011/7/EU.

[50] Art. 4. Directive 2011/7/EU.

[51] Art. 6. Directive 2011/7/EU.

[52] Art. 7. Directive 2011/7/EU.

[53] Art. 8. Directive 2011/7/EU.

Sellers can retain title to goods until full payment if expressly agreed upon, providing security in transactions.[54]

An enforceable title for unchallenged claims related to late payment must be obtainable within 90 calendar days, facilitating swift and effective redress for creditors.[55]

Recent data indicates an improvement; the 2021 Survey on the Access to Finance of Enterprises (SAFE) showed that 42% of EU businesses encountered payment delays, a decrease from 49% in 2019. Despite these improvements, over 50% of businesses in 8 Member States continue to report late payment issues.

Despite its well-intentioned provisions, the Directive faced criticism for its limited effectiveness in addressing the root causes of late payments. Critics argue that while the Directive provided a legal framework, it did not sufficiently address the power imbalances between SMEs and larger corporations, which often led to SMEs hesitating to enforce their rights due to fear of damaging business relationships.[56] Furthermore, the lack of robust enforcement mechanisms meant that many businesses, especially in certain EU countries, continued to experience significant payment delays.

Recognizing the significance of payment practices, the European Parliament and the European Commission have emphasized the need for a culture of prompt payment and enhanced enforcement of the Directive 2011/7/EU through various strategies and resolutions.[57]

3.2. Reasons and Key Elements of the Revision

The European Union internal market is characterized by a vast volume of commercial transactions, with an estimated 18 billion invoices issued annually.[58] This immense flow of transactions underpins the European economy, where the smooth

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54 Art. 9. Directive 2011/7/EU.

55 Art. 10. Directive 2011/7/EU.

56 Conti, M. *et al. Government late payments and firm's survival. Evidence from the EU*. Journal of law and economics, 64 (3), 2021, p. 603-627, DOI: 10.13140/RG.2.2.34292.68480; Drobnig, U. M. Encyclopedia Britannica. 2022. [https://www.britannica.com/topic/commercial-transaction], Accessed 1 March 2024.

57 European Commission, Directorate-General for Internal Market, Industry, Entrepreneurship and SMEs, Study on building a responsible payment culture in the EU – Improving the effectiveness of the Late Payment Directive (2011/7/EU), Publications Office of the European Union, 2022, [https://data.europa.eu/doi/10.2873/34185].

58 European Commission (2019). Study on the evaluation of invoicing rules of Directive 2006/112/EC. Final Report.

operation and competitiveness of enterprises, especially small and medium-sized enterprises (SMEs), are critically dependent on reliable payment streams.

Deferred payments, where goods or services are supplied before payment, necessitate a framework that ensures these payments are made promptly. Yet, late payments are a widespread issue, affecting businesses across all sectors and Member States, with a particularly severe impact on SMEs.[59]

Core Challenges for SMEs are asymmetry in bargaining power, inadequacy of current legal frameworks.[60]

A significant cause of late payments is the imbalance of power between large clients and their smaller suppliers. This asymmetry often forces suppliers to accept unfavourable payment terms and conditions, putting them at a financial disadvantage. For large clients, late payments serve as an attractive, cost-free financing option, imposing undue financial strain on the creditors.[61]

In 2022. Altares Dun & Bradstreet[62] conducted research on business payments in 14 European countries, focused specifically on the Netherlands. The study found that over a quarter (25.8 percent) of Dutch business invoices are not paid on time, based on research among more than 300,000 companies in the Netherlands. This issue is most prevalent among large companies, with only 36 percent of the largest companies paying on time, compared to 78 percent of the smallest organizations.

The practice of employing acceptance or verification procedures to confirm that goods or services meet contractual requirements, alongside the verification of invoice accuracy and compliance, is frequently leveraged to intentionally prolong the payment timeframe. Therefore, the incorporation of such procedures into a contract should be objectively warranted by the specific nature or distinct characteristics of the contract in question.[63]

The existing EU legal framework, specifically Directive 2011/7/EU, has been identified as lacking in several areas. It does not offer sufficient preventive measures against late payments nor does it provide adequate deterrents. Furthermore, the mechanisms for enforcement and seeking redress under the Directive 2011/7/

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59 Nicolas, T., *Short-term financial constraints and SMEs' investment decision: evidence from the working capital channel*, Small Business Economics (2021). European Payment Report 2022. Intrum

60 Directive 2000/35/EC *op. cit.*, note 9.

61 Huertas, M., *op. cit.*, note 10.

62 Altares Dun & Bradstreet, *Payment Study North Europe*, 2022. Rotterdam: [https://altares87872.activehosted.com/content/pyND2/2023/11/03/082cf7f2-8c0f-4d1b-b578-945b96dad7cc.pdf].

63 Judgment of 20 October 2022, *BFF Finance Iberia SAU v Gerencia Regional de Salud de la Junta de Castilla y León*, OJ C 53, 15 February 2021, p. 19, C585/20, EU: C: 2022:806, paragraph 53.

EU are considered insufficient, failing to protect businesses effectively from the repercussions of late payments.[64]

In response to these challenges, the proposal for a new regulation seeks to overhaul the current system by introducing measures designed to improve payment discipline across all actors in the commercial landscape, including public authorities, large corporations, and SMEs; provide robust protection for businesses from the adverse effects of delayed payments in commercial transactions; enhance the resilience and competitiveness of the European economy by ensuring that businesses, especially SMEs, can rely on timely payments for their goods and services.[65]

The initiative is part of the European Commission's 2023 work program under the objective "A Europe Fit for the Digital Age," reflecting the priority given to adapting EU policies to the contemporary economic environment and the challenges of digitalization.

The proposal is consistent with key EU policy provisions, including the Commission Communications on updating the New Industrial Strategy and the SME Strategy for a sustainable and digital Europe. It also addresses recommendations from the Fit for Future Platform and resolutions from the European Parliament calling for improved payment practices.

By targeting the revision of the Late Payment Directive, the proposal aims to address identified shortcomings and ensure that EU businesses operate in a more favourable and fairer commercial environment.

The proposed regulation finds its legal foundation in Article 114 of the Treaty on the Functioning of the European Union (TFEU)[66]. This article is a critical piece of the EU legislative framework, providing a basis for the harmonization of laws and regulations within Member States to ensure the functioning of the internal market. Article 114 TFEU supports measures aimed at removing obstacles to the internal market or preventing potential distortions of competition within it, making it a fitting legal basis for the proposed regulation aimed at combating late payment in commercial transactions.

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64 *Ibid.*

65 Commission Staff Working Document Executive Summary of The Impact Assessment Report Accompanying the Document Proposal for A Regulation of The European Parliament And Of The Council On Combating Late Payment In Commercial Transactions Strasbourg, 12 September 2023 SWD (2023) 313 final.

66 Consolidated version of the Treaty on the Functioning of the European Union, OJ C 326, 26 August 2012, pp. 47–390.

The necessity for revising the Late Payment Directive was significantly informed by comprehensive ex-post evaluations. These evaluations scrutinized the Directive's effectiveness, relevance, efficiency, and coherence, alongside its EU added value.

Ex-post evaluation of Late Payment Directive[67] showed that nearly two-thirds of companies are familiar with the rules governing late payments, and 86% are aware of their entitlement to claim compensation and, or interest for late payments. Still, this knowledge doesn't necessarily prevent late payments and 80% of companies that faced late payments in the past three years knew they could claim compensation or interest. Awareness of the regulations is linked to a smaller likelihood of worsening payment delays over three years compared to unaware firms.[68]

Despite the awareness, the Late Payment Directive's provisions are underutilized, with 60% of respondents never claiming their rights to interest and/or compensation. SMEs, in particular, are less likely to assert their rights compared to larger companies.

The Directive seems more effective in countries with shorter average payment times, where companies are more inclined to enforce their rights.[69]

The main deterrent against claiming rights under the Directive is the fear of harming business relationships, along with the absence of efficient remedies.

Payment durations have slightly decreased in recent years across the EU, but substantial disparities persist among Member States. For Business to Business (B2B) transactions, the average payment duration has decreased from 56 days in 2011 to 47 days in 2014, with a minimal reduction in payment delays. 90% of companies adhere to the Directive's mandate for payment terms of 60 days or less, with 70% not exceeding 30 days. However, sector and country affiliations significantly influence payment terms more than company size or rule awareness, with manufacturing and construction sectors experiencing longer payment terms than others.[70]

For transactions between public authorities and businesses (PA2B), average payment duration decreased from 65 days in 2011 to 58 days in 2014, though it still exceeds Directive stipulations, with some Member States seeing increased delays.

67 European Commission, Directorate-General for Internal Market, Industry, Entrepreneurship and SMEs, Lofstrom, F., Rivoire, L., Gallo, C. *et al.*, Ex-post evaluation of Late Payment Directive, Publications Office, 2015, [https://data.europa.eu/doi/10.2873/016503], p. 6-7.

68 *Ibid.*

69 *Ibid.*, p. 8.

70 *Ibid.*

Firms working mainly with public authorities are less likely to report worsened payment delays than those dealing primarily with other businesses.

Factors like national business culture, economic conditions, and power imbalances play more critical roles in determining payment behaviours than legislation alone. Currently, there's no clear evidence that the Directive has significantly impacted cross-border transaction uncertainty reduction. While the Directive was recognized for its relevance and efficiency, a critical finding was its limited effectiveness in fully addressing the fear and reluctance among creditors, especially SMEs, to assert their rights against late payments. This hesitancy is attributed to concerns about harming commercial relationships.

The evaluations pointed to a need for stronger preventive measures, more substantial deterrents, and enhanced enforcement mechanisms to protect businesses from the adverse impacts of late payments effectively.

Also, analysing the persistent challenges highlighted by the European Payment Report 2023 indicate that the existing rules have had some impact, but further changes and enhancements are necessary to effectively prevent late payments and support business growth and stability.

The rigorous ex-post evaluations, extensive stakeholder consultations, and thorough impact assessments collectively underscore the necessity for and potential benefits of the proposed Regulation on Combating Late Payment in Commercial Transactions. By addressing the limitations of the existing framework and incorporating stakeholder feedback, the proposal aims to introduce a more robust, effective, and equitable regime for managing commercial payments across the EU, with particular emphasis on safeguarding the interests and sustainability of SMEs.

4. MAIN DIFFERENCES AND IMPROVEMENTS OF THE LATE PAYMENT REGULATION PROPOSAL

The European Commission has decided to revise the current Late Payment Directive due to identified inadequacies in tackling the late payment problem in commercial transactions. Since 2015, various studies, assessments, and resolutions, including the 2019 European Parliament Resolution[71] and the 2021 Opinion of the Fit for Future Platform, highlighted the directive's main shortcomings. These include a lack of preventive measures, effective enforcement, accessible redress

[71] European Parliament resolution of 19 September 2019 on the importance of European remembrance for the future of Europe (2019/2819(RSP)) OJ C 171, 6 May 2021, pp. 25–29.

mechanisms for SMEs, unclear concepts, and the absence of a maximum payment term in Business-to-Business (B2B) transactions.

To address these issues and enhance the framework for combating late payments, the Commission proposed a new Regulation on late Payments. The proposed Late Payment Regulation introduces several significant changes compared to the existing directive: direct applicability and uniform provisions, stricter payment terms, automatic interest and compensation fees, enforcement and redress measures, protection of subcontractors, verification procedures limit.

According to Article 1, Regulation covers payments in business transactions, including those between businesses and public authorities, involving the delivery of goods or services, as well as public works and engineering projects. It excludes transactions with consumers, damage compensations, and payments within the scope of insolvency or restructuring proceedings. Except for a specific provision, it does not alter existing regulations established by Directive (EU) 2019/633.[72]

Under the Proposal of Regulation, the terms are defined as follows: "undertaking" is any organization conducting economic or professional activities independently. A "public authority" refers to a contracting authority as detailed in specific EU Directives. "Late payment" is a payment not made within the defined contractual or statutory period. The "amount due" includes the sum owed within the payment period plus applicable taxes and charges. An "enforceable title" is any legal document that allows for the forced collection of a debt. "Retention of title" is an agreement where the seller retains ownership of goods until full payment. "Procedure of acceptance or verification" checks the conformity of goods or services with contract requirements. A "debtor" is anyone owing payment for goods or services. A "creditor" is anyone who has provided goods or services and is owed payment.[73]

Regarding payment periods in commercial transactions, the payment period is capped at 30 calendar days from when the debtor receives the invoice or equivalent request for payment, assuming the goods or services have been received. This applies to both Business to Business and Business to Public Authority Transactions, including for regular and non-regular supplies of non-perishable agricultural and food products, unless a shorter period is specified by national law.

72 Directive (EU) 2019/1023 of the European Parliament and of the Council of 20 June 2019 on preventive restructuring frameworks, on discharge of debt and disqualifications, and on measures to increase the efficiency of procedures concerning restructuring, insolvency and discharge of debt, and amending Directive (EU) 2017/1132, OJ L 172, 26 June 2019, p. 18.

73 Art. 2. Proposal for a Regulation.

Additionally, a contract may specify a procedure of acceptance or verification of goods or services, strictly when necessary, with details including its duration. Such a procedure must not extend beyond 30 calendar days from receipt of the goods or services, with the total payment period not exceeding 30 calendar days post-procedure, irrespective of any shorter periods set by national laws.[74]

For public works contracts under EU Directives 2014/23/EU[75], 2014/24/EU[76], 2014/25/EU[77], and 2009/81/EC[78], contractors must prove to contracting authorities that they have paid their direct subcontractors on time as per this Regulation.

This evidence, likely a written declaration, should accompany any payment request. If the contracting authority lacks such proof or knows of late payments to subcontractors, it must promptly inform its Member State's enforcement authority.[79]

If a payment is late, the debtor must pay interest unless not responsible for the delay. This interest is automatically owed without needing a reminder if the creditor has met its contractual and legal duties, the debtor received the invoice or payment request, and payment wasn't made within the specified period.

Creditors cannot waive their right to late payment interest. The invoice receipt date cannot be contractually altered by the parties. The debtor must ensure the invoice or payment request is promptly processed upon receipt. Interest accrues from the latest of either the invoice's receipt or the goods or services' receipt and continues until full payment is made.[80]

The interest rate for late payment will be the reference rate plus 8 percentage points. For Eurozone countries, the reference rate is either the European Central Bank's main refinancing operations rate or the marginal interest rate from its latest

74 Art. 3. Proposal for a Regulation.

75 Directive 2014/23/EU of the European Parliament and of the Council of 26 February 2014 on the award of concession contracts Text with EEA relevance OJ L 94, 28 March 2014, pp. 1–64.

76 Directive 2014/24/EU of the European Parliament and of the Council of 26 February 2014 on public procurement and repealing Directive 2004/18/EC Text with EEA relevance OJ L 94, 28.3.2014, pp. 65–242

77 Directive 2014/25/EU of the European Parliament and of the Council of 26 February 2014 on procurement by entities operating in the water, energy, transport and postal services sectors and repealing Directive 2004/17/EC Text with EEA relevance OJ L 94, 28 March 2014, pp. 243–374.

78 Directive 2009/81/EC of the European Parliament and of the Council of 13 July 2009 on the coordination of procedures for the award of certain works contracts, supply contracts and service contracts by contracting authorities or entities in the fields of defence and security, and amending Directives 2004/17/EC and 2004/18/EC.

79 Art. 4. Proposal for a Regulation.

80 Art. 5. Proposal for a Regulation.

variable-rate tender operations. Non-Eurozone Member States will use the rate set by their national central bank. Reference rates for the first and second semesters are set on 1 January and 1 July of each year.[81]

When payments are scheduled in instalments and any instalment is overdue, interest for late payment will be calculated on the unpaid amount, with compensation also provided as per Article 8.[82]

When interest for late payment is due as per Article 5 of Proposal, debtors must automatically pay a flat fee of EUR 50 for recovery costs per commercial transaction, without requiring a reminder. Creditors cannot waive this right. Besides the flat fee, creditors can also seek reasonable compensation for recovery costs exceeding this amount caused by late payment. This does not affect creditors' rights to other forms of compensation.[83]

Contractual terms and practices that violate specific regulations will be considered null and void, including: (a) setting payment periods against Article 3's guidelines; (b) denying creditors' rights to interest for late payment or compensation for recovery costs as in Articles 5 and 8; (c) extending verification or acceptance procedures beyond Article 3(3)'s limits; (d) intentionally delaying invoice issuance.

Proposal defines obligation for Member States that they must provide effective means to address these issues, including legal or administrative action by organizations representing creditors or businesses.[84]

Also, Member States must promote transparency about the rights and obligations under this Regulation, including publicizing the applicable late payment interest rates. The Commission will also make these rates available online.

Creditors should receive an enforceable title within 90 days of action, excluding document service periods and creditor-caused delays, without affecting Regulation (EC) 1896/2006's[85] provisions. Member States will designate enforcement authorities to ensure payment deadlines are met, facilitate cross-border cooperation, and coordinate with other regulatory bodies, including sharing information.

81 Art. 6. Proposal for a Regulation.

82 Art. 7. Proposal for a Regulation.

83 Art. 8. Proposal for a Regulation.

84 Art. 9. Proposal for a Regulation.

85 Regulation (EC) No 1896/2006 of the European Parliament and of the Council of 12 December 2006 creating a European order for payment procedure OJ L 399, 30 December 2006, pp. 1–32.

Complaints about late payments in the agricultural and food sector will be directed to the appropriate authorities under Directive (EU) 2019/633[86]. [87]

The future outlook for SMEs under the new Regulation is cautiously optimistic. By addressing the root causes of late payments and enhancing the regulatory framework, the EU aims to create a fairer and more resilient business environment. This will not only support the financial stability of SMEs but also promote a more integrated and competitive single market

While the Directive 2011/7/EU laid the groundwork for addressing late payments, its limited effectiveness necessitated a comprehensive review and overhaul. The proposed new Regulation represents a significant step forward in ensuring timely payments, fostering a culture of prompt payment, and enhancing the overall resilience of the EU economy.

5. CONCLUSION

In the broader context of the European Union's ongoing battle against late payments, the progression from Directive 2011/7/EU to the proposed Regulation represents a significant shift in strategy, emphasizing the EU's commitment to enhancing the efficiency and uniformity of its approach to this pervasive issue.

The Directive, while a landmark step, laid the groundwork by setting clear expectations for payment terms, introducing automatic entitlements to statutory interest for late payments, and empowering creditors with the ability to claim compensation for recovery costs. Furthermore, it tackled the challenge of unfair contract terms, granting member states the authority to address grossly unfair contractual deviations.

Still, the complexity of economic interactions within the single market, compounded by the unique challenges faced by SMEs, necessitates a more uniform and directly enforceable set of rules across the EU.

The European Payment Report 2023 highlights that, despite the Directive's intentions, late payments remain a significant obstacle, with inflation and other economic factors exacerbating the situation. This is not just an issue of financial logistics but one that deeply affects the sustainability and growth potential of businesses, especially SMEs, which are often at a disadvantage in their bargaining positions.

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86 Directive (EU) 2019/633 of the European Parliament and of the Council of 17 April 2019 on unfair trading practices in business-to-business relationships in the agricultural and food supply chain PE/4/2019/REV/2 OJ L 111, 25 April 2019, pp. 59–72.

87 Art. 11. – 13. Proposal for a Regulation.

Recognizing these challenges, the Commission's proposal to replace the Directive with a Regulation is a strategic pivot designed to streamline and strengthen the EU's approach. Unlike a Directive, which requires individual member states to enact national legislation, a Regulation is directly applicable, ensuring that the rules are uniformly applied across all member states without additional national legislative measures. This shift is particularly advantageous for businesses engaged in cross-border trade within the EU, offering them a clearer, more predictable legal framework.

The proposed Regulation not only maintains the core achievements of the Directive, such as specified payment terms, statutory interest for late payments, and mechanisms for recovering costs but also introduces nuanced flexibilities. It recognizes the diverse economic landscapes of member states by allowing them the leeway to establish enforcement bodies and implement Alternative Dispute Resolution (ADR) mechanisms tailored to their specific contexts. Furthermore, it acknowledges the importance of education and training in credit management and financial digital literacy, underscoring the need for a holistic approach to fostering a responsible payment culture.

By focusing on direct applicability and uniform enforcement, the proposed Regulation aims to reduce the administrative burden on businesses, simplify cross-border transactions, and ultimately create a more conducive environment for economic growth and stability in the European single market. This forward-looking approach illustrates the European Union's adaptability and responsiveness to the needs of its economic ecosystem, particularly in supporting SMEs and facilitating a smoother integration of digital and sustainable business practices.

The transition from Directive 2011/7/EU to the proposed Regulation represents a significant shift in the EU's strategy to combat late payments. By addressing the identified shortcomings and incorporating stakeholder feedback, the new regulation has the potential to provide a more effective and equitable framework for managing commercial payments. The new legal framework will certainly serve as a basis for future research on its effectiveness, with a particular emphasis on the development of digital technologies that will undoubtedly impact possible payment methods."

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