

December 8th 2009

AmCham EU Concerned Over Ambiguities in Late Payments Directive Proposal

AmCham EU acknowledges the importance of ensuring the fairness of commercial transactions and timely payments and fully supports the European Commission (**Commission**) in the important objective of improving the effectiveness of remedies for breach of contractual obligations relating to late payment through its Proposal for a Directive of the European Parliament and of the Council on combating late payment in commercial transactions (Recast) implementing the Small Business Act (the **Proposed Directive**).

Many payments in commercial transactions are often executed later than agreed. Unfortunately, this is particularly the case in transactions between businesses and public authorities, as correctly identified in the Commission's Explanatory Memorandum to the Proposed Directive. Late payments affect the competitiveness of companies operating in Europe and these negative effects are far worse in the current challenging economic environment.

Many parts of the Proposed Directive are likely to further the objectives of improving liquidity, facilitating companies' financial management and increasing their competitiveness and viability as well as improving the opportunities for intra-Community commercial transactions.

However, AmCham EU cautions the European Parliament and the Council of Ministers in relation to certain aspects of the Proposed Directive, in relation to which suppliers and customers alike could face serious difficulties in their commercial activities. AmCham EU therefore calls on the EU institutions to assess these issues with due care, as set out below and in the annexed Information Paper, to ensure that the Proposed Directive will not lead to unforeseen and unintended consequences.

Although the fundamental principle on contract freedom is laid out in numerous places in the Proposed Directive, there are unfortunately contradictory and unclear provisions found elsewhere. These provisions put the effectiveness of the Directive as a whole in question and will be felt most directly by the SME's that form the core of the European supplier base. The Directive effectively eradicates the contractual freedom it sets itself out to ensure, in particular:

- **The concept of "grossly unfair terms" is vague and could easily lead to misinterpretations and abuse.** The concept should be clarified and a provision should be added establishing a presumption in favour of the

fairness of mutually agreed terms that could be overcome only on a showing of egregious conduct outside the norm of commercial behaviour;

- **The notion of providing for “representative organisations”** to conduct litigation is inappropriate and should be reconsidered;
- **The seller’s ability to compete against firms from other jurisdictions not subject to such a provision will be hampered** if the buyer’s ability to accept payment terms is called into question by operation of legislation under the Proposed Directive;
- **Payment terms are a very direct form of price competition**, and extended payment often is desired by buyers in lieu of other price concessions in order to meet the varying needs of the enterprise – for example, for cash management or other measures imposed upon it internally or by external market conditions.

For more information and a detailed explanation of these points, please refer to the attached Information Paper.

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AmCham EU speaks for American companies committed to Europe on trade, investment and competitiveness issues. It aims to ensure a growth-orientated business and investment climate in Europe. AmCham EU facilitates the resolution of transatlantic issues that impact business and plays a role in creating better understanding of EU and US positions on business matters. Aggregate US investment in Europe totalled €1.2 trillion in 2008 and currently supports 4.8 million direct jobs in Europe.

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Explaining AmCham EU's position on the Late Payments Directive

INFORMATION PAPER

December 8th 2009

The following information paper contains a more detailed explanation of the recommendations made in AmCham EU's position statement on the Proposal for a Directive of the European Parliament and of the Council on combating late payment in commercial transactions (Recast) implementing the Small Business Act (the **Proposed Directive**).

Freedom to contract is an essential provision of the Proposed Directive

Maintaining freedom to contract is an essential feature of the Proposed Directive and the European Commission (**Commission**) has considered it important to stress "*the fundamental principle of freedom of contract between economic operators*".

Indeed, the Commission's Impact Assessment notes (page 6) the undesirable nature of harmonising payment periods between businesses as "*loss of contractual freedom by removing the ability of companies to compete through payment periods offered to clients.*"

Provisions on "grossly unfair terms" and "representative organisations" cause concern

Even though the fundamental principle on contract freedom is laid out in numerous places in the Proposed Directive, there are unfortunately contradictory and unclear provisions found elsewhere.

Specifically, **paragraph 6 of the Proposed Directive** prohibits "*abuse of freedom of contract to the disadvantage of the creditor*":

1. Member States shall provide that a clause in a contract on relating to the date for payment, the rate of interest for late payment or recovery costs shall either be unenforceable or shall give rise to a claim for damages if it is grossly unfair to the creditor. In determining whether a clause is grossly unfair to the creditor, all circumstances of the case shall be considered, including good commercial practice and the nature of the product or the service. Account shall also be taken of whether the debtor has any objective reason to deviate from the statutory rate of interest or from Article 3(2)(b), Article 4(1) or Article 5(2)(b).

For the purpose of the first subparagraph, a clause which excludes interest for late payment shall always be considered as grossly unfair.

2. Member States shall ensure that, in the interests of creditors and competitors, adequate and effective means exist to prevent the continued use of clauses which are grossly unfair to the creditor within the meaning of paragraph 1.

3. The means referred to in paragraph 2 shall include provisions whereby representative organisations may take action according to the national law concerned before the courts or before competent administrative bodies on the grounds that clauses are grossly unfair, so that they can apply appropriate and effective means to prevent their continued use.

- **“Grossly unfair terms”**

The concept of “grossly unfair terms” is vague and could easily lead to misinterpretations and abuse.

It is helpful that the Commission has not attempted to set down specific examples of unfair terms, which could create a straightjacket for business. However, the factors that the Proposed Directive sets out for consideration – “all circumstances of the case [...], including good commercial practice and the nature of the product or the service”— are vague and subject to interpretations that would unduly restrict the freedom of contract. In order to give appropriate dignity to the concept of freedom of contract, the Proposed Directive should, at a minimum, establish a strong presumption that an agreement on payment terms freely entered into by two commercial actors is fair. A party should be able to overcome the presumption only on a showing of unusual circumstances wholly outside the norm of commercial behaviour.

Moreover, the suggestion that account should be taken of whether the debtor has any “objective reason” to deviate from the statutory rate of interest, or from Article 3(2)(b) and 5(2)(b) - which set down time limits for payment - or Article 4(1) - which sets down compensation for recovery costs, not only limits the contractual freedom the Proposed Directive sets out to ensure, but eradicates that freedom, causing great uncertainty for business. Rather than give respect to the freedom of contract of the parties by establishing a presumption that their commercial decision is fair, this provision establishes the opposite presumption and requires an affirmative showing to demonstrate that their freely-made agreement is reasonable. Under a strict reading of the proposed Article 6, parties would be unwilling to deviate from the statutory rate of interest or from Article 3(2)(b), Article 4(1) or Article 5(2)(b), with the debtor having the burden of proof to show “objective reasons” for the relevant terms and conditions used. Such a situation is unsatisfactory and AmCham EU asks the European Parliament (**Parliament**) and Council of Ministers (**Council**) to ensure that the wording is improved.

RECOMMENDATION: AmCham EU proposes to delete from Article 6(1) the sentence “Account shall also be taken of whether the debtor has any objective reason to deviate from the statutory rate of interest or from Article 3(2)(b), Article 4(1) or Article 5(2)(b)”, and to add a provision



establishing a presumption in favour of the fairness of mutually agreed terms that could be overcome only on a showing of egregious conduct outside the norm of commercial behaviour.

- ***"Representative organisations"***

Articles 6(2) and 6(3) set out that Member States shall ensure that “adequate and effective means” exist to prevent the continued use of grossly unfair clauses. These means include “representative organisations” which may take legal action before the courts or before competent administrative bodies of the Member States.

In considering whether to maintain and expand this provision, the Parliament and Council should take into account whether it is needed to accomplish the objectives of the Proposed Directive and whether it may have unintended consequences that could be to the detriment of commercial operators in the EU and, in particular, SMEs.

Firstly, it is not clear that such a provision will be needed to protect the rights of creditors. Other provisions of the Proposed Directive provide robust access for individual firms to seek redress for late payment. In the absence of experience with these provisions, it is premature to expand upon a procedure that could, as discussed below, have unintended negative consequences.

Secondly, the Commission has not in its Impact Assessment accounted for how the existing Directive (2000/35/EC) was transposed into national legislation and which “representative organisations” have to date taken on the role foreseen. Needless to say, representative organisations is a very vague term and it cannot be excluded – in particular given the precarious language used to define “grossly unfair terms” - that this could fuel unmeritorious and abusive “class action”-style litigation by plaintiff law firms and litigious companies before the courts of the Member States.

Importantly, collective litigation should only be used where there is a high degree of similarity between the claimants and the nature of their claims, something unlikely to be the case in individually negotiated and concluded agreements for a wide range of products and services in a myriad of different commercial considerations. It needs to be recognised that, by their nature, certain actions should normally be dealt with on an individual basis.

Moreover, a wide-ranging clause which would allow "representative organisations" to take action, and for courts to look at contract clauses in isolation - without the ability to give full consideration to the entire agreements and their wider context - would indubitably lead to undesired outcomes. Through this provision businesses, small and large alike, could have their contractual freedom seriously curtailed by decisions that would affect their ability to negotiate and conclude favourable contracts that in certain aspects would deviate from such court decisions. As a result, this could lead to effects that would impair a significant number of market participants.

The focus should instead be on strengthening the rules relating to late payment - as otherwise foreseen in the Proposed Directive - and thereby strengthening the position of a contractual party who is a victim of such conduct. In doing so, that party's grounds for seeking redress through individual action in a case relating to late payment will be greatly improved.

RECOMMENDATION: AmCham EU recommends that the Proposed Directive reject the encouragement of litigation through "representative organisations" and that Article 6(3) be removed from the Proposed Directive.

Final comments

AmCham EU is concerned that **the Proposed Directive does not adequately protect the core principal of freedom of contract** and that this could have real, adverse effects on the competitiveness of firms subject to its jurisdiction – particularly those of SMEs. Payment terms are a very direct form of price competition, and extended payment often is desired by buyers in lieu of other price concessions in order to meet the varying needs of the enterprise – for example, for cash management or other measures imposed upon it internally or by external market conditions. If the buyer’s ability to accept such terms is called into question by operation of legislation under the Proposed Directive, the seller’s ability to compete against firms from other jurisdictions not subject to such a provision will be hampered. This effect will be felt most directly by SMEs – which form the core of the European supplier base.

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