



**Stanford – Vienna
Transatlantic Technology Law Forum**

A joint initiative of
Stanford Law School and the University of Vienna School of Law



European Union Law Working Papers

No. 33

**The Application of the European Late
Payment Directive to Loan Contracts**

Magdalena Gruber

2018

European Union Law Working Papers

Editors: Siegfried Fina and Roland Vogl

About the European Union Law Working Papers

The European Union Law Working Paper Series presents research on the law and policy of the European Union. The objective of the European Union Law Working Paper Series is to share “works in progress”. The authors of the papers are solely responsible for the content of their contributions and may use the citation standards of their home country. The working papers can be found at <http://tlf.stanford.edu>.

The European Union Law Working Paper Series is a joint initiative of Stanford Law School and the University of Vienna School of Law’s LLM Program in European and International Business Law.

If you should have any questions regarding the European Union Law Working Paper Series, please contact Professor Dr. Siegfried Fina, Jean Monnet Professor of European Union Law, or Dr. Roland Vogl, Executive Director of the Stanford Program in Law, Science and Technology, at:

Stanford-Vienna Transatlantic Technology Law Forum
<http://tlf.stanford.edu>

Stanford Law School
Crown Quadrangle
559 Nathan Abbott Way
Stanford, CA 94305-8610

University of Vienna School of Law
Department of Business Law
Schottenbastei 10-16
1010 Vienna, Austria

About the Author

Magdalena Gruber studied business law and international business and economics in Vienna and Lausanne. She is currently pursuing a PhD at the University of Vienna and is working as a university assistant at the Alpen-Adria-University Klagenfurt. Her fields of research are commercial and corporate law, as well as European business law.

General Note about the Content

The opinions expressed in this paper are those of the author and not necessarily those of the Transatlantic Technology Law Forum or any of its partner institutions, or the sponsors of this research project.

Suggested Citation

This European Union Law Working Paper should be cited as:
Magdalena Gruber, The Application of the European Late Payment Directive to Loan Contracts, Stanford-Vienna European Union Law Working Paper No. 33, <http://tlf.stanford.edu>.

Copyright

© 2018 Magdalena Gruber

Abstract

This paper examines the Late Payment Directive of the European Union and seeks to answer the question of whether the provisions of the Directive can be applied to loan contracts. The paper first describes and analyses the Late Payment Directive and provides a comprehensive analysis of relevant arguments and legal sources. It then argues that the Late Payment Directive should be applied to loan contracts and facility agreements, even if this is not explicitly foreseen in the Directive. The paper finally highlights the inconsistencies that emerge when such contracts are excluded from the Directive.

Table of Contents

- 1. Introduction2
- 2. The Late Payment Directive.....2
 - a. Commercial Background2
 - b. Genesis of the Directive4
 - c. Content Overview5
- 3. The Late Payment Directive and Loan Contracts6
 - a. Loan Contracts6
 - b. Commercial Transaction7
 - c. Undertakings and Public Authorities8
 - d. Delivery of Goods or Provision of Services10
 - e. The Concept of Remuneration13
- 4. Further Arguments16
 - a. Loan Contracts and the Aim of the Directive16
 - b. Article 5 of the Directive: Payment Schedules17
 - c. Linked Credit Agreements18
- 5. Excursus: Compound Interest21
- 6. Conclusion.....22

1. Introduction

Lending and borrowing have become common transactions in everyday life, now constituting an entire branch of business. Payment delays happen in this context almost daily, as well; when they occur on a broad scale, they even have the power to distort markets, as proven by the latest financial crisis in 2008. While the European Union has already been trying to remedy late payment in the European Single Market for most transactions, it still remains unclear whether the European measures apply to lending operations.

This paper addresses this issue and seeks to find a solution based on European law. The paper will start by offering a general overview of the Directive and its development. This initial section is necessary for fully understanding the background and aims of the Directive, as well as the possible results that are triggered by an application of the Directive to lending transactions. The second and main section of the paper focuses on the question of whether the Directive can be applied to loan contracts and, furthermore, which provisions in the Directive argue for or against such an interpretation.

2. The Late Payment Directive

a. Commercial Background

The Late Payment Directive is a European Union legislative act dating back to 2011 that aims at tackling the issue of late payments. In the commercial environment of the Member States, many payments are executed later than initially accorded in the contract, even if one party has already fulfilled its obligations (i.e., the goods have already been delivered or the services have already been performed).¹ This leads to a situation wherein the seller of a good or

¹ Cf. Explanatory Memorandum accompanying 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, COM(2009) 126 final, 2009/0054 (COD), 3.

provider of a service is forced to credit the outstanding amount to the buyer.

These late payments impact business transactions in a negative manner.² When the buyer withholds payment, the liquidity of the seller is impaired. This hinders the seller's effective financial management, as he is forced to wait for the outstanding amount, which he could have invested in the meantime. This can, in turn, impact his competitiveness and profitability.³ If the seller is forced to obtain external financing to fulfil his obligations, he is burdened with interest rates that are typically higher than the rates he usually charges to his contracting parties.

Small and medium-sized enterprises (SMEs) are especially vulnerable to late payments, as they typically have less liquidity than larger enterprises. SMEs tend to rely on large suppliers or other business actors that possess more market power.⁴ The bargaining power of SMEs is comparatively weak when contracting with larger, dominant enterprises.⁵ Additionally, when it comes to late payment, the administrative costs of pursuing debts are disproportionately high for SMEs. This results from a lack of time and manpower to chase outstanding debts, which generally requires specialised staff engaged specifically to manage the recovery of debt.⁶ Whereas larger entities can usually cope with late payment more easily and can employ additional staff due to economies of scale,⁷ SMEs are especially predisposed to late payment.

² *McCormack*, Retention of Title and the EC Late Payment Directive, *Journal of Corporate Law Studies* 2001, 501, 502.

³ Recital 3 of the Late Payment Directive.

⁴ *McCormack*, *Journal of Corporate Law Studies* 2001, 502.

⁵ *Bilotta*, Ending the Commercial Siesta: The Shortcomings of European Union Directive 2011/7 on Combating Late Payments in Commercial Transactions, *Brooklyn Journal of International Law* 2013, 699, 702.

⁶ Commission Proposal for a European Parliament and Council Directive combating late payment in commercial transactions (1998) 126 final, 4.

⁷ A larger enterprise typically concludes more contracts than a SME, or, at least, handles a larger transaction volume. This entails that the outstanding amounts are generally higher. The break-even point, which economically justifies the employment of another staff member, is reached when the amount recoverable by receivables management equals the costs of this additional staff member.

Their very existence can be jeopardised due to late payment, especially when the outstanding amounts result in a lack of cash, which can force the undertaking into insolvency.⁸

In short, late payment is the major reason for illiquidity⁹ and the reason for twenty-five percent of all bankruptcies in the European Union.¹⁰ Larger enterprises can deliberately exercise their power over SMEs in a way that ‘starves out’ unwanted business partners or disliked competitors.¹¹ By intentionally withholding payments – a behavior that in the past was seldom followed by any negative consequences – a company could essentially force its contracting partner into insolvency proceedings.

b. Genesis of the Directive

The European Union legislation became aware of the situation and decided to address it in a broad manner. The first measures combating late payment in the European Union date back to 1995. The topic has, since then, remained high on the political agenda. The Late Payment Directive¹², as it is commonly referred to, was adopted in the European Union on 16 February 2011. The Directive replaced Directive 2000/35/EC¹³, the earlier version of the Late Payment Directive, whose repeal took effect on 16 March 2013.¹⁴

The Late Payment Directive is part of a larger package of measures aimed at fostering the European Single Market. First, it forms part of an initiative by the European Commission

⁸ *McCormack*, Journal of Corporate Law Studies 2001, 502.

⁹ *Opinion of the European Economic and Social Committee* 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, O.J. C 255/42.

¹⁰ Cf. the Proposal for a European Parliament and Council Directive combating late payment in commercial transactions, 126 final, O.J. C 168/2.

¹¹ Cf. *McCormack*, Journal of Corporate Law Studies 2001, 502.

¹² Directive 2011/7/EU of the European Parliament and of the Council of 16 February 2011 on Combating Late Payment in Commercial Transactions, O.J. L 48/1.

¹³ Directive 2000/35/EC of the European Parliament and of the Council of 29 June 2000 on combating late payment in commercial transactions, O.J. L 200/35.

¹⁴ Cf. Article 13 of the recast Late Payment Directive.

whose goal is to encourage the growth and success of SMEs.¹⁵ ‘*Think Small First: Priority to the SMEs – A Small Business Act for Europe*’ emphasises facilitated access to financing and the creation of a supportive business environment for SMEs. These goals may, according to the Commission, be achieved, *inter alia*, by timely payment in commercial transactions.¹⁶ Second, the Directive also complements the ‘*European Economic Recovery Plan*,’¹⁷ another initiative at the European level, which takes as one of its main goals the reduction of administrative burdens and the promotion of entrepreneurship for SMEs (among other market participants). This recovery plan explicitly foresees that said objectives should be met by compelling companies to pay their invoices within one month in order to ease the liquidity constraints of their contracting partners.¹⁸

c. Content Overview

The Late Payment Directive provides a number of approaches that should deter late payment; however, the central provisions of the Directive revolve around the ‘interest rule.’ The Directive provides companies with an entitlement to interest payments in the event of a buyer’s late payment¹⁹ without any reminder requirements.²⁰ The interest rate foreseen in the Directive is comparatively high, which should deter buyers from executing payments later

¹⁵ *Verse*, Das Gesetz zur Bekämpfung von Zahlungsverzug im Geschäftsverkehr, ZIP 2014, 1809, footnote 3.

¹⁶ Communication from the Commission to the Council, the European Parliament, the European Economic and Social Committee and the Committee of the Regions, *Think Small First: Priority to the SMEs – A Small Business Act for Europe* (2008) 394 final.

¹⁷ Commission Communication of 26 November 2008, not published in O.J., available under http://ec.europa.eu/economy_finance/publications/pages/publication13504_en.pdf, last access 6 March 2018.

¹⁸ Recital 7 of the Directive.

¹⁹ Articles 3 and 4 of the Late Payment Directive.

²⁰ The directive follows the principle *dies interpellat pro homine*, according to which the creditor is entitled to interest without sending any prior notice of non-performance (e.g. a reminder or a late notice). Cf. Recital 16 of the Directive.

than their due date.²¹ Parties individually may agree on a lower interest rate, which, however, is subject to an unfairness test.²²

Moreover, the Directive entitles the seller to a payment of EUR 40 when payment is late.²³ This lump sum is intended to compensate the creditor for the administrative and internal costs linked to the recovery of the debt claim, without obliging him to prove any specific damages.²⁴ In addition to the lump sum, creditors may also demand reasonable reimbursement of other recovery costs that they incurred in connection with the late payment. Such costs may have arisen internally, e.g. administrative expenses in the receivables management, or externally, by hiring a lawyer or a debt collection agency.²⁵

3. The Late Payment Directive and Loan Contracts

a. Loan Contracts

The Directive itself does not use the term ‘loan contract’ or any similar expression (such as credit agreement or facility agreement).²⁶ A loan contract is usually an agreement concerning the upfront provision of money for a certain period of time in exchange for interest-bearing recurrent repayments. In Austria, Section 988 of the Austrian Civil Code (Allgemeines Bürgerliches Gesetzbuch, ABGB) stipulates that the remuneration for a loan contract is the interest that is provided for in the contract.²⁷

²¹ Article 2 paragraph 6 stipulates that the statutory interest for late payment has to be at least eight percentage points above the reference rate of the European Central Bank.

²² Cf. Article 7 of the Directive. It is yet still unclear what is meant by the expression ‘grossly unfair’. Cf. *Schauer/Gruber* in Mankowski (ed.), *Commercial Law (2018) Late Payment Directive Article 7 paragraphs 8 et seq. (in preparation)*.

²³ Article 6 paragraph 1 of the Directive.

²⁴ Recital 19 of the Directive. Note, however, the limited effects of this modest figure, cf. *Schauer/Gruber* in Mankowski (ed.), *Commercial Law, Late Payment Directive Article 5 paragraph 7 (in preparation)*.

²⁵ Recital 20; Article 6 paragraph 3 of the Directive.

²⁶ Note however that Recital 13 of the Directive uses the term ‘trade credit’. Cf. footnote 60 for further treatise.

²⁷ Cf. *Welser/Zöchling-Jud*, *Bürgerliches Recht II*¹⁴ (2015) paragraphs 918 et seq.

b. Commercial Transaction

To establish whether loan agreements are subject to the Late Payment Directive, it is first necessary to determine whether the normative requirements are met. The Late Payment Directive only applies to commercial transactions.²⁸ Commercial transactions are defined by the Directive as ‘*transactions between undertakings or between undertakings and public authorities which lead to the delivery of goods or the provision of services for remuneration.*’²⁹

Commercial transactions traditionally happen on a contractual basis, by two parties in their private autonomy agreeing upon a certain transaction.³⁰ The Directive itself excludes some commercial transactions from its jurisdiction, as the European legislature did not intend to regulate certain areas. Payments under the laws on cheques and bills of exchange, for instance, are not regarded as commercial transactions in the context of the Directive.³¹ Moreover, the Directive does not govern compensation payments. This exemption includes payments from insurance companies, as the application of the Directive ‘*should be limited to payments made as remuneration for commercial transactions.*’³² The focus lies on the character of the term ‘remuneration,’ as compensatory payments are not regarded as

²⁸ Article 1 paragraph 2 of the Directive.

²⁹ Article 2 paragraph 1 of the Directive.

³⁰ Cf. ECJ 26 February 2015, C-104/14, *Federconsorzi*, where the question was posed whether statute-based relationships fulfilled the definition of ‘commercial transaction’. The ECJ did not rule on this specific question; yet, it can be assumed that such ‘contracts’ do not fulfil the requirements of a commercial transactions. For further details cf. *Schauer/Gruber* in Mankowski (ed.), *Commercial Law, Late Payment Directive Article 2 paragraph 4 (in preparation)*.

³¹ Recital 8 of the Late Payment Directive. The reason for this exclusion is that there exists a potential conflict of laws between the Directive and the *Convention Providing a Uniform Law For Bills of Exchange and Promissory Notes* (Geneva, 1930) as well as the *Convention Providing a Uniform Law for Cheques* (Geneva, 1931). Said conventions have been ratified by 14 Member States of the European Union and the Directive should not intervene in this regard. Cf. *Schroeter*, *UN-Kaufrecht und Europäisches Gemeinschaftsrecht* (2015), Article 6 paragraph 343.

³² Recital 8 of the Directive. Cf. also Article 1 paragraph 2 of the Directive. Article 1 paragraph 2 constitutes a compulsory norm of the Directive, whereas Recital 8, which stipulates a similar content, is not. For the legal value of Recitals in general see ECJ 19 November 1998, C-162/97, *Nilsson*, paragraph 54; cf. furthermore ECJ 1 April 2008, C-267/06, *Tadao Maruko*.

remuneration for a good or service.³³ The individual elements that are required by Article 2 paragraph 1 as cited are dealt with as follows.

c. Undertakings and Public Authorities

The Late Payment Directive uses the term ‘undertaking’ for what generally would be understood as a company. The concept of an **undertaking** includes ‘*any organisation, other than a public authority, acting independently in its economic or professional activity, even where that activity is carried out by a single person.*’³⁴ The definition therefore covers all kinds of enterprises, from corporations to unincorporated partnerships,³⁵ as well as sole traders and the liberal professions.³⁶ For a transaction to be concluded on behalf of an undertaking, a person has to act as an organisation within the framework of an independent economic or professional activity.³⁷ This framework can be defined as an ‘*activity in a structured and stable manner, so that the activity cannot be limited to an isolated one-off supply, and that the transaction in question must form part of that activity.*’³⁸

Public authorities do not operate in ordinary market conditions, nor do they aim to make a profit or bear eventual losses resulting from their activities. Such authorities typically are

³³ *Klimke*, Die Bedeutung der Zahlungsverzugsrichtlinie 2000/35/EG für die Prämienschuld des Versicherungsnehmers, *VersR* 2010, 1259, 1262; cf. *Schauer/Gruber* in Mankowski (ed.), *Commercial Law, Late Payment Directive Article 2 paragraph 7 (in preparation)*. Recital 8 creates a certain imbalance, as premium payments (from the insured party to the insurer) are covered by the Late Payment Directive, whereas the respective opposite transaction, namely compensatory payments by insurance companies to the insured party are not subject to the Directive’s provisions.

³⁴ Article 2 paragraph 3 of the Directive.

³⁵ Cf. *Schulte-Braucks/Ongena*, *The Late Payment Directive - a Step towards an emerging European Private Law?*, *ERPL* 2003, 519, 528.

³⁶ *Oelsner*, Die Neufassung der Zahlungsverzugsrichtlinie, *EuZW* 2011, 940, 941. Liberal professions can be regarded as undertakings only for the purpose of the Late Payment Directive. Member States should not derive any assimilation to undertakings or merchants for purposes outside the scope of the Late Payment Directive as this is not the intention of the Directive. The expansion of the Directive’s scope to liberal professions was criticised due to the concernment that those professions could be assimilated with undertakings or merchants; however, Recital 10 of the Directive avoids such interpretation beyond the Directive itself. Cf. *Schulte-Braucks*, *Zahlungsverzug in der Europäischen Union*, *NJW* 2001, 103, 105; *Schauer/Gruber* in Mankowski (ed.), *Commercial Law, Late Payment Directive Article 2 paragraph 14 (in preparation)*.

³⁷ ECJ 15 December 2016, C-256/15, *Nemec*, paragraph 33.

³⁸ *Ibid.*, paragraph 34.

‘state, regional or local authorities, bodies governed by public law, associations formed by one or several such authorities or one or several of such bodies governed by public law.’³⁹ A ‘body governed by public law’ has to fulfil several criteria. First, it has to be established for the specific purpose of meeting needs in the general interest; therefore, it must not pursue an industrial or commercial purpose.⁴⁰ Secondly, a body governed by public law must have a legal personality. Finally, for the third criterion, one out of three following alternatives has to be fulfilled: (1) the body is financed (at least for the most part) by a State, regional or local authority or another body governed by public law; or (2) the body is subject to management supervision by those bodies; or (3) the body has an administrative, managerial or supervisory board, more than half of whose members are appointed by named authorities. Each of these three alternatives essentially indicates that there must be proximity to the public sector.⁴¹

The Late Payment Directive does not apply to **consumers**, which are explicitly excluded from the scope of the Directive.⁴² Business-to-consumer (B2C) transactions are covered by other specific provisions of European Union law.⁴³ Transactions with other entities such as associations, political parties, trade unions or religious communities are typically

³⁹ Article 2 paragraph 1 lit a of Directive 2004/17/EC coordinating the procurement procedures of entities operating in the water, energy, transport and postal services sectors, O.J. L 134/1. Cf. *Schauer/Gruber* in Mankowski (ed.), Commercial Law, Late Payment Directive Article 2 paragraph 8 et seq. (*in preparation*).

⁴⁰ Even if such bodies were set up with the goal of meeting needs in the general interest, the activity might still be of an industrial or commercial character. Cf. Recital 12 of 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, O.J. L 94/243, Recital 10 of 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, O.J. L 94/65. Those two Directives apply due to the reference made in Article 2 paragraph 2 of the Late Payment Directive to the earlier version of each Directive; cf. *Schauer/Gruber* in Mankowski (ed.), Commercial Law, Late Payment Directive Article 2 paragraph 8 et seq. (*in preparation*) for further details.

⁴¹ Article 1 paragraph 9 of Directive 2004/18/EC on the coordination of procedures for the award of public works contracts, public supply contracts and public service contracts, O.J. L 134/144, which defined the same criteria as Article 2 paragraph 1 lit a of Directive 2004/17/EC coordinating the procurement procedures of entities operating in the water, energy, transport and postal services sectors, O.J. L 134/1. The institutions of the European Union can be qualified as public authorities as well, cf. Recital 27 of the Late Payment Directive.

⁴² Cf. Recital 8 of the Directive.

⁴³ Cf. European Commission, Late Payment Directive 2011/7/EU, FAQs, accessible under <http://ec.europa.eu/DocsRoom/documents/16222/attachments/1/translations/en/renditions/native>, last access 6 March 2018.

characterised by a non-commercial nature and are also not governed by the Late Payment Directive.⁴⁴

As an initial result of the above constraints, it appears that the Late Payment Directive can, if at all, only be applied to loan contracts between two undertakings or an undertaking and a public authority. It can therefore be argued that the Late Payment Directive can likely be applied to **corporate loans**.

d. Delivery of Goods or Provision of Services

As previously explained, only commercial transactions can be subject to the Late Payment Directive.⁴⁵ More specifically, these transactions must take place between two undertakings or an undertaking and a public authority.⁴⁶ Furthermore, the commercial transaction must involve the delivery of goods or the provision of services, both for remuneration.⁴⁷ These are the typical components of a synallagmatic relationship (i.e., the delivery of goods or the provision of services for remuneration).

In the case of corporate loans, it has to be clarified whether the provision of money constitutes a service at all. First, a contractual agreement regarding a loan has to constitute a ‘commercial transaction’ within the meaning of Article 1 paragraph 2 of the Directive. Article 2 paragraph 1 explains that a commercial transaction can include a service provided by an undertaking in exchange for remuneration. *Prima facie*, this definition seems to cover loan

⁴⁴ Cf. *Oelsner*, *Zwingendes Recht im Geschäftsverkehr*, GPR 2013, 182, 183; cf. for the definition of consumers for the purpose of European Directives *Ullreich*, *Der Verbrauchervertrag* (2016) 128.

⁴⁵ Article 1 paragraph 2 of the Late Payment Directive.

⁴⁶ Article 2 paragraph 1 of the Directive. Cf. 3.c.

⁴⁷ *Ibid.*

contracts. Nonetheless, it is not made conclusively clear by this clause whether financial services should also be covered.⁴⁸

Commonly, in the European primary as well as secondary law, financial services are classified as services.⁴⁹ Article 58 paragraph 2 of the Treaty on the Functioning of the European Union (TFEU)⁵⁰, for instance, stipulates that the '*liberalisation of banking and insurance services connected with movements of capital shall be effected in step with the liberalisation of movement of capital.*'⁵¹ Additionally, other directives of the European Union qualify financial services as services. Directive 2002/65/EC,⁵² which holds that a financial service '*means any service of a banking, credit, insurance, personal pension, investment or payment nature,*' provides just one example.⁵³

Secondary law of the European Union often exempts financial services from provisions that govern general services.⁵⁴ However, it appears that the European legislature regards financial services as services and merely excludes them from certain service-related directives which are not applicable to the financial sector.⁵⁵ In other words, an exemption would not be

⁴⁸ Freitag, Unternehmenskredit und Zahlungsverzug, ZIP 2015, 1805, 1809.

⁴⁹ Junglas, Darlehensrückzahlungsforderungen als Entgeltforderungen iSd § 288 II BGB?, NJOZ 2015, 241, 242; Freitag, ZIP 2015, 1809.

⁵⁰ Treaty on the Functioning of the European Union, O.J. C 326/1.

⁵¹ Article 58 paragraph 2 of the TFEU.

⁵² Directive 2002/65/EC of the European Parliament and of the Council of 23 September 2002 concerning the distance marketing of consumer financial services and amending Council Directive 90/619/EEC and Directives 97/7/EC and 98/27/EC, O.J. L 271/16.

⁵³ Article 2 lit b of Directive 2002/65/EC of the European Parliament and of the Council of 23 September 2002 concerning the distance marketing of consumer financial services and amending Council Directive 90/619/EEC and Directives 97/7/EC and 98/27/EC, O.J. L 271/16.

⁵⁴ Examples for such exemptions can be found for instance in Article 2 paragraph 2 lit b of the *Services Directive*, Directive 2006/123/EC of the European Parliament and of the Council of 12 December 2006 on services in the internal market, O.J. L 376/36. It says that the Directive shall not apply to '*financial services, such as banking, credit, insurance and re-insurance, occupational or personal pensions, securities, investment funds, payment and investment advice, [...]*'. Another example can be found in Article 3 paragraph 3 lit d of the *Consumer Rights Directive* (Directive 2011/83/EU of the European Parliament and of the Council of 25 October 2011 on consumer rights, amending Council Directive 93/13/EEC and Directive 1999/44/EC of the European Parliament and of the Council and repealing Council Directive 85/577/EEC and Directive 97/7/EC of the European Parliament and of the Council, O.J. L 304/64), which stipulates that the Directive shall not apply to contracts regarding financial services.

⁵⁵ Cf. Freitag, ZIP 2015, 1809.

necessary if financial services were not first considered services in general, and excluding financial services from certain legislative acts makes sense given the particular nature of financial services.

Along with the legislature, the European Court of Justice (ECJ) qualifies financial services as services. This was made clear in a judgement in 1998 wherein the Court held that the ‘*grant of a credit facility is indeed the provision of a service [...]*’.⁵⁶ This is maintained in other holdings of the ECJ, as well.⁵⁷ It is already well-settled case law that an institution that provides credit is to be understood as a service provider.⁵⁸

Even the Late Payment Directive itself indicates that financial services are covered by the Directive. This follows from Recital 8 Sentence 2 of the Late Payment Directive, which exempts some financial transactions from the scope of Directive, such as payments made as compensation for damages (including payments from insurance companies).⁵⁹ This exemption, however, implies that insurance contracts in general can and should be subsumed under the Late Payment Directive. Insurance contracts undoubtedly belong to the financial services sector, which suggests that the Late Payment Directive covers other contracts within this sector as well.⁶⁰

⁵⁶ ECJ 17 March 1998, C-45/96, *Bayerische Hypotheken- und Wechselbank AG v Edgar Dietzinger*, paragraph 18, on the interpretation of Council Directive 85/577/EEC of 20 December 1985 to protect the consumer in respect of contracts negotiated away from business premises, O.J. L 372/31.

⁵⁷ ECJ 15 March 2012, C-453/10, *Jana Pereničová and Vladislav Perenič v SOS financ spot sro* on the interpretation of Council Directive 93/13/EEC of 5 April 1993 on unfair terms in consumer contracts, O.J. L 95/29; ECJ 14 November 1995, C-484/93, *Svensson and Gustavsson v Ministre du Logement et de l'Urbanisme*, paragraph 11; ECJ 9 July 1997, C-222/95, *Société civile immobilière Parodi v Banque H. Albert de Bary et Cie*, paragraph 17. Cf. *Junglas*, NJOZ 2015, 242.

⁵⁸ ECJ 3 October 2006, C-452/04, *Fidium Finanz AG v Bundesanstalt für Finanzdienstleistungsaufsicht*, paragraph 39 et seq. When the ECJ had to determine into which category of the fundamental freedoms the activity of granting credit on a commercial basis falls, the Court concluded that this activity indeed constitutes a provision of services.

⁵⁹ See 3.b. above.

⁶⁰ *Freitag*, ZIP 2015, 1809. When the Late Payment Directive uses the term ‘trade credit’ in Recital 13, however, this is no indication that the Directive should cover loan agreements. Even if the wording is misleading, trade credits do not qualify as credits as such. Trade credits are granted by the seller of a product to the buyer in the

The financial services sector is subject to more comprehensive regulation in the European Union than the traditional services sector.⁶¹ However, this fact alone does not mean that the ‘classic’ services sector and the financial services sector should be understood to be more different than similar. In fact, the increased regulation of the financial services sector simply represents a supplement to the general provisions in order to meet the specific nature of financial services.

In light of all the above factors, the provision of money seems rightly classified as a service. Consequently, the provision of capital should constitute a ‘service’ in the context of the Late Payment Directive, which therefore renders said Directive applicable to loan contracts.

e. The Concept of Remuneration

The final criterion of Article 1 paragraph 2 of the Directive that has to be fulfilled is the presence of remuneration, as the ‘[...] Directive shall apply to all payments made as remuneration for commercial transactions.’⁶² In Recital 8, it is specified that no other payments but remuneration payments should be covered by the scope of the Directive.⁶³ Consequently, not all commercial payments are governed by the Directive, but only such payments that are made as remuneration for a commercial transaction.⁶⁴

Even if the Directive uses the term, it does not provide an exact definition for ‘remuneration’.

In the German version of the Directive, the expression ‘*Entgelt*’ is found, which usually

context of the sale of a certain good and bear the character of a payment deferral rather than a classic credit agreement; *Junglas*, NJOZ 2015, 242.

⁶¹ *Freitag*, ZIP 2015, 1809.

⁶² Article 1 paragraph 2 of the Late Payment Directive.

⁶³ Recital 8 of the Late Payment Directive stipulates that ‘*The scope of this Directive should be limited to payments made as remuneration for commercial transactions.*’ Cf. footnote 33 above.

⁶⁴ This clarification was added by the Council in the course of drafting the initial Late Payment Directive, Directive 2000/35/EC; cf. Common Position (EC) No 36/1999 adopted by the Council on 29 July 1999, O.J. C 284/6.

describes any consideration for a contractual obligation. In general, it can be stipulated that remuneration only comprises monetary obligations.⁶⁵

In order to subsume facility agreements under the Late Payment Directive, it has to be clarified which part of a loan agreement can be regarded as remuneration. The remuneration aspect of corporate loans is argued in different ways in the German literature.⁶⁶

The predominant view holds that only the contractual entitlement to interest represents the creditor's consideration for the provision of capital. The German literature thus qualifies the interest for a credit as remuneration,⁶⁷ which has to be distinguished from the simple repayment of the credited amount. The credited amount is hereinafter referred to as the 'proceeds of the loan'. Said proceeds of the loan do not constitute remuneration for the provision of the service, but have to be returned as part of the contractual obligations in the synallagmatic relationship.⁶⁸

Freitag invokes two Directives to supplement his arguments in favour of this view. Alongside the *Consumer Credit Directive*,⁶⁹ he mentions the *Mortgage Credit Directive*.⁷⁰ He argues that neither of these Directives considers the proceeds of a loan as remuneration. They in fact differentiate between the terms 'borrowing rate' and other 'charges' versus 'repayment.'

⁶⁵ Schauer/Gruber in Mankowski (ed.), Commercial Law, Late Payment Directive Article 1 paragraph 10 (*in preparation*); Freitag, ZIP 2015, 1806.

⁶⁶ Cf. Junglas, NJOZ 2015, 242 et seq. versus Freitag, ZIP 2015, 1809.

⁶⁷ Freitag, ZIP 2015, 1806; Löwisch/Feldmann in Staudinger, Kommentar zum Bürgerlichen Gesetzbuch – Buch 2: Recht der Schuldverhältnisse¹⁷ (2014), Section 286 paragraph 97.

⁶⁸ Löwisch/Feldmann in Staudinger, BGB, Section 286 paragraph 97 in conjunction with Section 288 paragraph 21; Freitag, ZIP 2015, 1806; Ernst in MüKoBGB⁷ (2016) Section 288 paragraph 19; Palandt/Grüneberg, BGB⁷⁴ (2015) Section 288 paragraph 8.

⁶⁹ Directive 2008/48/EC of the European Parliament and of the Council of 23 April 2008 on credit agreements for consumers and repealing Council Directive 87/102/EEC, O.J. L 133/66.

⁷⁰ Directive 2014/17/EU of the European Parliament and of the Council of 4 February 2014 on credit agreements for consumers relating to residential immovable property and amending Directives 2008/48/EC and 2013/36/EU and Regulation (EU) No 1093/2010, O.J. L 60/34.

Nevertheless, Junglas recently tried to disprove this common perspective and argued for the classification of the proceeds of the loan as remuneration. According to his point of view, remuneration is the counter-value of a service and, therefore, the equivalent of the service in question. According to this view, if the provision of money constitutes the service, everything that is provided in return should be regarded as remuneration. Junglas qualifies the repayment of the loan as remuneration for the provision of money and the interest on the loan as remuneration for capital utilisation. He points out that the repayment of the proceeds of the loan has a recompensing effect, and that is not the money *in rem* that is given back but a certain *amount* of money (which will not be the exact same bank notes that were provided at first).⁷¹ Both the proceeds of the loan, as well as the interest, consequently constitute remuneration in Junglas' view.

This discussion is relevant, as the actual outcome determines how much interest is due in the case of late repayment of a loan. If the first, predominant view is supported, interest for late payment can only arise on the loan interest that is paid back late, but not on the outstanding amount that qualifies as the proceeds. If, however, Junglas' approach is followed, interest for late payment can be demanded for the entire outstanding amount, i.e. for the proceeds of the loan and for the outstanding interest.

This second view constitutes an undoubtedly more effective measure against the late repayment of loans and makes more economic sense. To claim interest for just part of an outstanding instalment seems inadequate. Junglas argues that the prevailing view in Germany is too narrow and relies too much on the national, German interpretation of the so-called 'synallagma'.⁷²

⁷¹ Cf. *Junglas*, NJOZ 2015, 243 et seq.

⁷² *Ibid.*

From a dogmatic point of view, Junglas' argumentation cannot be followed, as it does not fit in with the Austrian or German legal system or the general understanding of the law.⁷³ Nevertheless, in terms of content, his rationale is persuasive. An approach that solely relies on the national legal background is too formalistic and does not reflect European law. As the goal of the Directive is to ensure liquidity, the predominant German view turns out to be too focused on national legal doctrine. The Late Payment Directive is a European legislative act, and national understandings of the law have to be applied restrictively for the benefit of European law as a whole. Nothing in the Directive indicates that the proceeds of a loan are not covered by its jurisdiction, resulting in a situation where interest can only arise for late payment of the contractual interest. This speaks for an application of the Directive to loan contracts, especially in view of the inappropriate result that a different conclusion might trigger.

4. Further Arguments

a. Loan Contracts and the Aim of the Directive

An argument supporting the predominant view is that no indication can be found in the Directive that the European legislature intended to create a regulation for loan contracts. It rather seems that the Late Payment Directive envisages classic sales and services instead of financial services. As laid out in the preliminary remarks, the Directive aims to protect SMEs as creditors. Small and medium-sized enterprises typically do not act as finance providers in the commercial context.

However, even if SMEs were the target group of the Directive, the Late Payment Directive has the objective to combat late payment in general and is not limited to SMEs. It is

⁷³ Cf. *Freitag*, ZIP 2015, 1807 et seq.

reasonable to assume that the unclear situation when it comes to facility agreements in terms of evaluating the scope of the Late Payment Directive constitutes an unintended gap in the European legislation. Said gap could be closed either by legislative action or by conclusion by analogy. As analogies generally should be applied only very restrictively, the question remains whether the legal situation in the present case provides a sufficient basis for an analogy. The Late Payment Directive includes a provision that has not been mentioned so far that could serve as a pertinent basis, which will be outlined below.

b. Article 5 of the Directive: Payment Schedules

Article 5 of the Late Payment Directive provides that the Late Payment Directive ‘*shall be without prejudice to the ability of parties to agree, subject to the relevant provisions of applicable national law, on payment schedules providing for instalments [...]*’.⁷⁴ The rationale behind this provision is the fact that payment schedules or payments in instalments traditionally follow a different idea than conventional payments. In predefined payment schedules, the creditor usually considers the payment deferral and, consequently, prices the costs for said deferral. This can be done either by including interest in the purchase price in the contract or by agreeing on a surcharge on the price for the goods or services in the agreement.⁷⁵ Either way, for the owed debt this results in maturity arising partially in instalments rather than the entire outstanding amount becoming due instantly.

Even if Article 5 seems to contradict the regulatory system of the Late Payment Directive at first glance, as it permits agreements that prolong payment periods, it still fits in with the Directive’s purposes and intentions. The main objective of the Directive is to prevent late payment, which should not have an impact on agreements that allow a proper functioning of

⁷⁴ Article 5 of the Late Payment Directive.

⁷⁵ *Weller/Harms*, Die Kultur der Zahlungstreue im BGB, WM 2012, 2305, 2305.

the market. Payments by instalments or staggered payments that are predefined in the initial contract should thus not be affected or hindered by the Directive.⁷⁶ The European legislature has decided not to subject this form of payment to the Directive, as there is no intention or reason to prohibit it, especially due to its very common occurrence in business transactions.

Nonetheless, each instalment or partial payment is subject to the Directive's provisions, and each rate itself has to be paid pursuant to the agreed terms. If an instalment is late, interest accrues for the delay. The Directive clarifies that in cases where an instalment is not paid by the agreed date, interest and compensation costs shall be calculated solely on the basis of the overdue amount.⁷⁷

As laid out, the European legislature deems a situation acceptable where the payment is initially prolonged. It therefore appears odd that the Late Payment Directive should not cover credit facilities, as the underlying rationale and principle resembles payment schedules. In both cases, payment is deferred based on an arrangement in the initial contract, with interest charged for the longer period until full payment is effected. This is especially true for the case where a credit facility is granted in connection with the purchase of a good. It can therefore be argued that at least certain loan contracts have to be covered by the Late Payment Directive, namely those that are granted by the seller of a good in connection with a purchase.⁷⁸

c. Linked Credit Agreements

Article 5 of the Late Payment Directive (entitled '*Payment Schedules*') regulates a certain kind of loan agreement: it covers credits granted by the seller or service provider to his

⁷⁶ Cf. Recital 22 of the Late Payment Directive; furthermore, *Oelsner*, *Strengere Zahlungs- und Verzugsregelungen für öffentliche Auftraggeber durch die Reform der EU-Verzugsrichtlinie*, *KommJur* 2013, 241, 244.

⁷⁷ Article 5.

⁷⁸ Cf. also Recital 13 of the Directive. Trade credits, which are granted by the seller of a product to a buyer, are explicitly permitted, cf. footnote 60.

contracting partner in the context of the sale of goods. This follows from Article 5 of the Directive, allowing agreements between the two contracting parties regarding payment in instalments. In these situations, the borrower is granted a credit line and the payment period for the remuneration of the contract is prolonged.⁷⁹

The Directive only seems to target cases where the seller of a good defers payment. It is, however, common practice that third parties provide money to the creditor or debtor in exchange for a claim to the purchase price against the buyer. Such third parties typically are banks or other financial institutions.

Three different scenarios are conceivable. First, if the seller himself grants a credit, the transaction (and therefore the purchase price) is covered by the Late Payment Directive, which allows the seller to claim interest in the case of late payment by the buyer. Second, if a bank provides money to the seller, who then sells the goods to the buyer, the purchase agreement is covered by the Late Payment Directive, and the buyer will have to pay interest if he is late with payment. In the third scenario, if a credit is granted by a bank to the buyer, who then uses the money to buy goods, and he is late with payment to his bank, no interest will arise for late payment of the proceeds of the loan according to the abovementioned stipulations.⁸⁰ To summarize, the buyer has to pay interest for late payment in the context of a bank-financed purchase when the purchase price is credited by the seller directly or by a bank to the seller, but not if credit is granted to the buyer directly.

⁷⁹ Cf. Article 5 of the Late Payment Directive: *'This Directive shall be without prejudice to the ability of parties to agree, subject to the relevant provisions of applicable national law, on payment schedules providing for instalments. [...]'*. Cf. furthermore Recital 13 of the Directive: *'[...] there may be circumstances in which undertakings require more extensive payment periods, for example when undertakings wish to grant trade credit to their customers. It should therefore remain possible for the parties to expressly agree on payment periods longer than 60 calendar days [...]'*.

⁸⁰ Cf. Schauer/Gruber in Mankowski (ed.), Commercial Law, Late Payment Directive Article 3 paragraph 51 (*in preparation*).

This, however, cannot be upheld when following a holistic, economic approach. It would constitute an unjustified differentiation if the three scenarios lead to different consequences, as all three pursue the same purpose, namely allowing the buyer to purchase a product immediately by granting him additional liquidity. According to Article 3 subparagraph n of Directive 2008/48/EC⁸¹ (the *Consumer Credit Directive*), the described scenarios would constitute so-called **linked credit agreements**. A linked credit agreement can accordingly be defined as an agreement where

‘(i) the credit in question serves exclusively to finance an agreement for the supply of specific goods or the provision of a specific service, and

(ii) those two agreements form, from an objective point of view, a commercial unit; a commercial unit shall be deemed to exist where the supplier or service provider himself finances the credit for the consumer or, if it is financed by a third party, where the creditor uses the services of the supplier or service provider in connection with the conclusion or preparation of the credit agreement, or where the specific goods or the provision of a specific service are explicitly specified in the credit agreement.’⁸²

In the case of linked credit agreements, a relationship of interdependence exists between the purchase of goods or services and the credit agreement concluded for that purpose.⁸³ No distinction should be made on the basis of whether a loan is granted by the seller (creditor) or by a third party because any such differentiation would be unjustified. The above three scenarios pursue the same purpose and should consequently generate the same effects. A uniform treatment of the different case configurations generates legal certainty for the

⁸¹ Directive 2008/48/EC of the European Parliament and of the Council of 23 April 2008 on credit agreements for consumers and repealing Council Directive 87/102/EEC, O.J. L 133/66.

⁸² Article 3 lit n of Directive 2008/48/EC of the European Parliament and of the Council of 23 April 2008 on credit agreements for consumers and repealing Council Directive 87/102/EEC, O.J. L 133/66, the so-called *Consumer Credit Directive*.

⁸³ Recital 37 of Directive 2008/48/EC (*Consumer Credit Directive*).

contracting parties. The Late Payment Directive, therefore, should be interpreted as also covering linked credit agreements, even when this is not specifically mentioned in the Directive itself.⁸⁴

Interest should therefore also accrue if a credit is granted to the buyer of a product. There is also no reason why the Directive should be restricted to loans in the context of corporate sales while excluding other corporate loans, as it applies to financial services as well.⁸⁵ When following a holistic, economic approach and bearing in mind the general concept and aim of the Late Payment Directive, the result is that the Directive should apply to loan contracts.

5. Excursus: Compound Interest

A final issue worth mentioning is the treatment of compound interest. As set out above, late payment of the interest on a loan agreement entitles the creditor to demand interest on the outstanding amount (i.e., interest on interest). Even if it is not clear whether interest can be charged for the proceeds of a loan, interest on the contractual interest (which represents the remuneration in the contract) may be claimed in the case of late payment. Interest on interest constitutes so-called *compound interest*, and some Member States forbid its use.⁸⁶ The reasons for such prohibitions lie in the intended protection of the debtor. With a view to legal certainty, a debtor should have the possibility to foresee the amount of debt that may arise.⁸⁷

If national law provides for a prohibition on the accrual of compound interest, such limitation should still be interpreted narrowly. The law of the European Union demands an autonomous interpretation of directives. If an interpretation curbs the effects of a European directive, this

⁸⁴ *Schauer/Gruber* in Mankowski (ed.), Commercial Law, Late Payment Directive Article 3 paragraph 51 (*in preparation*).

⁸⁵ See 3.d above.

⁸⁶ See for example Section 289 of the German Civil Code (Bürgerliches Gesetzbuch, BGB).

⁸⁷ *Freitag*, ZIP 2015, 1809.

interpretation cannot be regarded as being in line with the directive.⁸⁸ For the purpose of the present analysis, this means that a restriction on a claim to interest would run counter the Late Payment Directive's objectives. This must lead to an interpretation that establishes conformity with the European legal situation.

6. Conclusion

The Late Payment Directive, though in existence since 2011, still provides ample material for discussion. An application of the Directive to the late repayment of loans in the context of corporate transactions seems convincing when taking into account all presented arguments. If a credit is granted in the context of a corporate sale, this loan should be covered by the Late Payment Directive, as a contrary conclusion would constitute an unjustified distinction and would distort the market situation.

The final evaluation of this issue will be conducted first by the courts at a national level and, ultimately, by the European Court of Justice. A binding interpretation as to whether loan contracts are covered by the scope of the Late Payment Directive therefore remains to be seen.

⁸⁸ Ibid., 1809 et seq. *Junglas*, NJOZ 2015, 244, reaches the same conclusion, even if his argumentative approach is different.