



## COVERSHEET

<b>Minister</b>	Hon Stuart Nash	<b>Portfolio</b>	Small Business
<b>Title of Cabinet paper</b>	<b>Improving Payment Practices: Release of Discussion document</b>	<b>Date to be published</b>	20 May 2020

### List of documents that have been proactively released

<b>Date</b>	<b>Title</b>	<b>Author</b>
19 February 2020	Improving Payment Practices: Release of Discussion document	Office of the Minister for Small Business
19 February 2020	DEV-20-MIN-0013	Cabinet Office

### Information redacted

**YES**

Any information redacted in this document is redacted in accordance with MBIE's policy on Proactive Release and is labelled with the reason for redaction. This may include information that would be redacted if this information was requested under Official Information Act 1982. Where this is the case, the reasons for withholding information are listed below. Where information has been withheld, no public interest has been identified that would outweigh the reasons for withholding it.

Some information has been withheld for the reason of Confidential advice to Government

In Confidence

Office of the Minister for Small Business

Chair, Cabinet Economic Development Committee

## **Improving Payment Practices: Release of Discussion document**

### **Proposal**

1. I am seeking Cabinet's agreement to release a discussion document which seeks public feedback on proposals to address business-to-business extended payment terms and late payments.

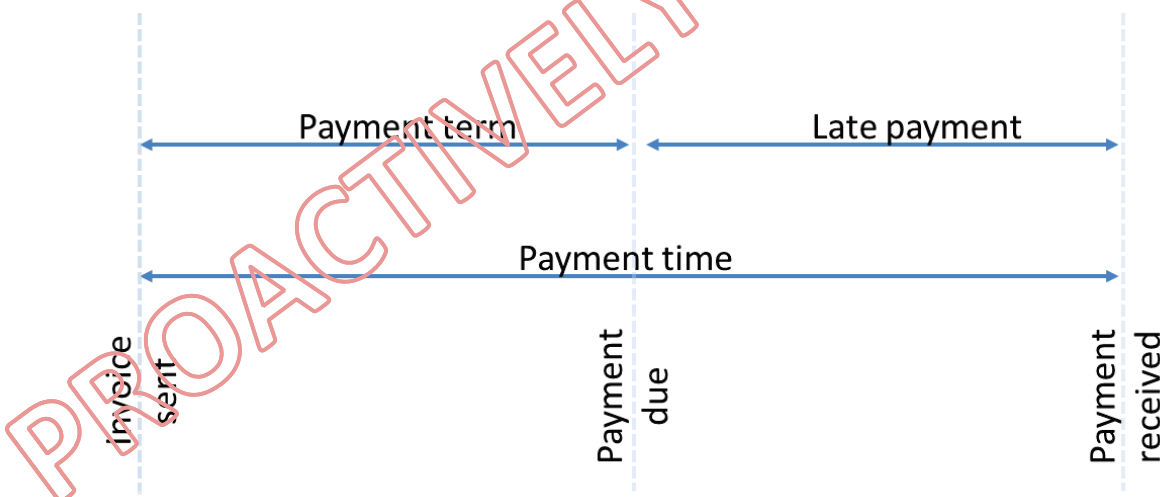
### **Executive Summary**

2. Extended payment terms are not uncommon between businesses, and cause financial harm and stress, particularly to small businesses. Businesses have limited recourse against the practice of extended payment terms, and late payments.
3. I propose to consult on proposals to introduce legislation to address this issue by specifying a maximum payment term of 20-days, and to introduce an automatic right to charge interest and debt recovery fees to address late payments.

### **Background**

4. The Government has a goal of building a more productive, sustainable and inclusive economy. One vital element to achieve this goal is for business people to operate in an environment that provides healthy competition through fair and reasonable business practices. Another vital element for businesses is good cash flow.
5. *A Focus on Small Business*, the Government's response to the Small Business Council's Strategy, notes the importance of small business to the economy and identifies a compelling opportunity for government to focus on lifting small business performance, building on the Economic Plan's focus on improving the productivity of all New Zealand businesses. The Small Business Work Programme will look to progress four key themes:
  - 5.1. Improving data collection to enable better understanding of the needs and experience of small business
  - 5.2. Improving access to appropriate finance options for businesses
  - 5.3. Considering the wider business support system to ensure small businesses develop the skills and capabilities they need to thrive
  - 5.4. Using the 'Better for Business' programme as a foundation to improve understanding of key business pain-points and help with the design of regulations and cross agency services for small businesses.

6. The Government is already working to improve business cash flow and stamp out unfair practices by:
  - 6.1. leading by example, with government departments aiming to pay 95 per cent of domestic invoices within 10 working days;
  - 6.2. implementing e-Invoicing, which makes sending and receiving invoices faster, easier, cheaper, more accurate and more secure;
  - 6.3. introducing the Fair Trading Amendment Bill that will prohibit unconscionable conduct and protect against unfair contract terms.
7. There are two practices that are currently hurting business cash flow, increasing owners' stress, and forcing them to waste time and money. These are:
  - 7.1. Extended payment terms, where businesses stipulate that they will only do business with suppliers who give them a very long time to pay; and
  - 7.2. Late payments.



8. Current technology means there is no longer good reason to have payment terms of 60 or 90 days. Even 20<sup>th</sup>-of-the-following month terms are a hangover from the days of posting invoices and paying by cheque.
9. Late payments are very common, are unfair and are harmful. Extended payment terms are often imposed by big business on smaller business, particularly where they have unequal bargaining power. This effectively allows large businesses to use their smaller suppliers as a source of free credit. Large businesses can also get cheaper finance than small businesses, making late payments particularly unfair to small businesses.
10. These two practices combine to impede business growth. Businesses receiving payments late must resource their operations from other sources of credit, or delay paying their own suppliers. This means that one large business demanding extended

payment terms could potentially start a flow-on effect that spreads through an entire supply chain.

11. From Ministry of Business, Innovation and Employment research, the major impacts on businesses receiving request for deferred payment related to:
  - 11.1. Cash flow (87%);
  - 11.2. An increase in stress levels (81%);
  - 11.3. A reduction in businesses' ability to grow (66%); and
  - 11.4. An increase in administration overheads (51%).
12. An Australian study showed the costs to their economy of large businesses effectively using small ones for cheap credit is \$2.54 billion over 10 years.<sup>1</sup>
13. I propose to release a discussion document that seeks feedback on two measures to address these practices:
  - 13.1. Legislating a maximum payment term of 20 days;
  - 13.2. Legislating an automatic right to claim interest on late payments.

### **Evidence indicates extended payment terms and late payments are common and harm businesses**

14. In 2018 the Ministry of Business, Innovation and Employment surveyed 1254 businesses from across New Zealand about their invoicing and payment practices. Key lessons about the impacts of extended payment terms and late payments are:

#### ***Extended payment terms***

15. Extended payment terms are quite common, and cause problems. Of the businesses surveyed, 27 per cent had customers request longer payment terms in the past 12 months. Most of those requests were for terms of 60 days, 90 days or longer than 90 days.
16. I have engaged with a number of those large businesses that have imposed extended payment terms on their suppliers. Some have responded positively to my view that such payment practices were not in the interest of New Zealand businesses. However some have been less inclined to change their behaviour.

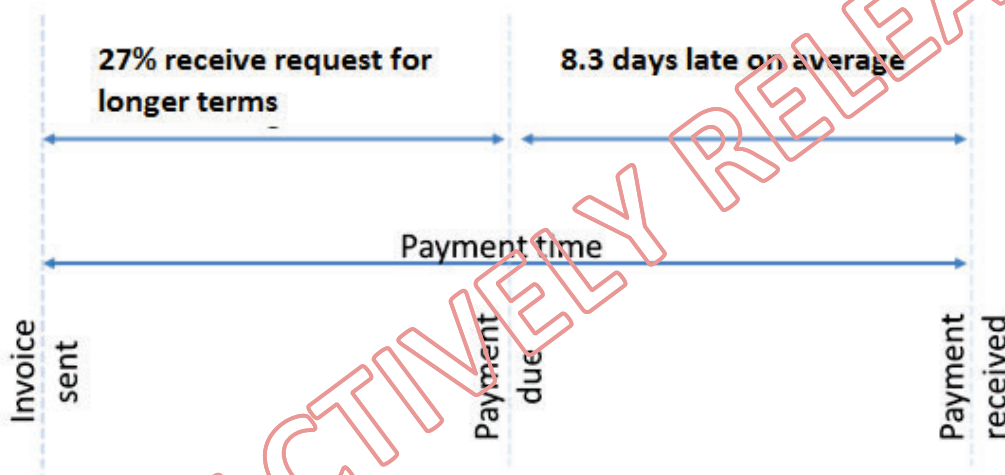
#### ***Late payments***

17. Late payments are very common and are a major source of stress and cash flow problems:
  - 17.1. 49 per cent said late payments hurt their cash flow;
  - 17.2. 48 per cent said late payments increased their stress levels;

---

<sup>1</sup> <https://www.xero.com/small-business-insights/wp-content/uploads/2019/06/xsbi-report-paying-the-price.pdf>

- 17.3. 30 per cent said late payments impacted their ability to grow.
- 18. Businesses tell us that when they are paid late they:
  - 18.1. use personal savings (38 per cent);
  - 18.2. cover their business expenses by organising overdrafts or personal loans with their bank (31 per cent) and/or;
  - 18.3. delay paying the invoices they have received (25 per cent).
- 19. According to Xero's Small Business Insights, small businesses on their platform are paid 8.3 days late on average.



**I propose to consult on a maximum payment term and an automatic right to interest on late payments**

- 20. I propose to consult with the public on two measures designed to combat extended payment terms and late payments, and therefore create more cashflow certainty:

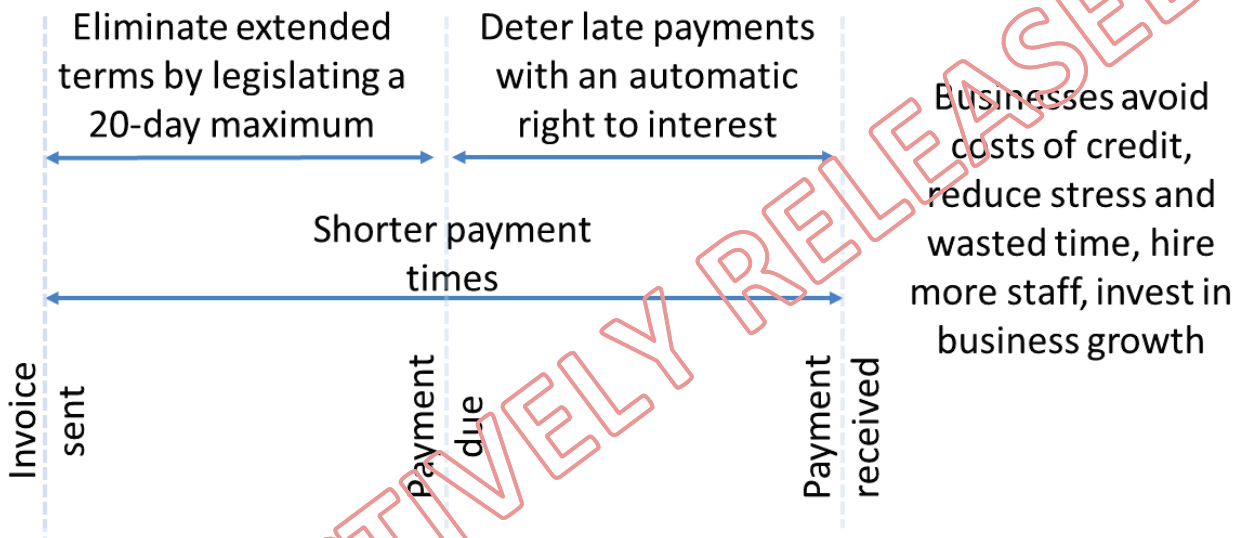
- 20.1. *A 20-day maximum payment term:*

Maximum payment terms are used overseas, for example, the European Union (EU) Late Payment Directive. Lessons from the EU are that a maximum payment term can be interpreted as the “recommended” term, and businesses may increase their payment terms to the maximum specified. We also note that with current technology, there is no longer any reason to impose 60 or 90-day payment terms. Even 30-day terms are a hangover of the days of posting invoices and paying by cheque. I propose that we test a more restricted, but reasonable, term specified in legislation.

- 20.2. *An automatic entitlement to charge interest to cover costs incurred from late payment*

Under the Interest on Money Claims Act 2016, suppliers may currently apply to the court, for interest as compensation for a delay in payment. I propose that we test providing for an automatic entitlement to interest on the cost of late payment, consistent with the European Union's *Late Payment Directive*.

I also propose we consult on setting an interest rate to one higher rate than that provided for under the Interest on Money Claims Act (which is based on the Reserve Bank's six-month term deposit rate, plus a base rate of 0.15 percentage points), as this rate does not recognise the true costs to all businesses of late payments.



21. I intend to consult specifically with businesses to ensure that the proposals are designed and applied to create certainty, speed up transactions across the economy, and do not create any unintended consequences for some forms of contractual obligations or for particular firms or industries (for example where late payments, or alternative structure payment approaches are in the best interest of both the purchaser and the supplier).
22. I also want to ensure that the proposals, and how they are incorporated in law, are workable for all businesses.
23. The discussion document notes other measures that could be considered and asks an open question on how to improve payment practices in New Zealand. These include:
  - 23.1. Introducing a disclosure regime requiring large businesses to publicly report on their payment time and/or terms;
  - 23.2. Introducing a voluntary code of practice;
  - 23.3. Encouraging businesses to use alternative dispute resolution mechanisms, beyond the formal disputes resolution services, which can be costly and timely.

## Risks/Concerns

24. Departmental consultation on these proposals has raised a number of risks and concerns. These are legitimate. I am proposing using this discussion document to help us understand business and community interest and concerns with legislative approaches to address late and deferred payments. The feedback will help me and my portfolio officials' to work closely with other agencies and portfolios to consider the best ways of addressing these impediments to cash flow and ensuring fair business practices.

## I seek agreement to consult on the proposals

25. I propose a six-week public consultation period from early 2020. Confidential advice to Government

## Consultation

26. The Treasury, the Ministry of Justice, and Commerce Commission staff have been consulted on this Cabinet paper and on the attached discussion document. The Department of the Prime Minister and Cabinet has been informed.
27. In addition, as noted above, MBIE surveyed 1254 businesses in late 2018, which supported the development of the discussion document.

## Financial Implications

28. There are no financial implications arising from the recommendations in this paper.

## Legislative Implications

29. There are no immediate legislative implications arising from this paper. However, the consultation may result in policy recommendations being made to Cabinet that would require new legislation and/or amendments to legislation.

30. Confidential advice to Government

## Impact Analysis

31. The discussion document substitutes for a Regulatory Impact Assessment. MBIE's Regulatory Impact Analysis Review Panel has reviewed the discussion document and confirms that it is likely to lead to effective consultation and support the delivery of Regulatory Impact Analysis to support subsequent decisions.
32. The Ministry for the Environment has been consulted and confirm that the CIPA requirements do not apply to this proposal as the threshold for significance is not met.

## Human Rights

33. The proposals in this paper are consistent with the New Zealand Bill of Rights Act 1990 and the Human Rights Act 1993.

## Publicity

34. We intend to issue a media statement accompanying the release of the discussion document. The discussion document will be made publicly available on the MBIE website.

## Proactive Release

35. MBIE will publish this Cabinet paper along with the discussion document on the MBIE website.

## Recommendations

The Minister for Small Business recommends that the Committee:

36. **note** that extended payment terms can be unfair and have a negative impact on businesses;
37. **note** that late payments are hurting business cash flow, increasing owners' stress, and forcing them to waste time and money;
38. **note** that the attached discussion document seeks feedback on two proposals to address business-to-business extended payment terms and late payments:
  - 38.1. A 20-day maximum payment term;
  - 38.2. An automatic entitlement to charge interest for late payment to reflect costs incurred, and seeks feedback through consultation on what this interest rate might be.
39. **agree** to the release of the attached discussion document for public consultation, subject to any minor or technical amendments that may be required;
40. Confidential advice to Government
41. **note** that this Cabinet paper and the discussion document will be published on the MBIE website.

Authorised for lodgement

Hon Stuart Nash

Minister for Small Business





**MINISTRY OF BUSINESS,  
INNOVATION & EMPLOYMENT**  
HIKINA WHAKATUTUKI

# Discussion paper

---

Improving business-to-business payment practices in  
New Zealand

February 2020

PROACTIVELY RELEASED

## Permission to reproduce



Crown Copyright ©

This work is licensed under the Creative Commons Attribution 4.0 International License. To view a copy of this license, visit <http://creativecommons.org/licenses/by/4.0/>.

## Important notice

The opinions contained in this document are those of the Ministry of Business, Innovation and Employment and do not reflect official Government policy. Readers are advised to seek specific legal advice from a qualified professional person before undertaking any action in reliance on the contents of this publication. The contents of this discussion paper must not be construed as legal advice. The Ministry does not accept any responsibility or liability whatsoever whether in contract, tort, equity or otherwise for any action taken as a result of reading, or reliance placed on the Ministry because of having read, any part, or all, of the information in this discussion paper or for any error, inadequacy, deficiency, flaw in or omission from the discussion paper.

ISBN 978-1-99-001902-9 (online)

PROACTIVELY RELEASED

# How to have your say

---

## Submissions process

The Ministry of Business, Innovation and Employment (MBIE) seeks written submissions on the issues raised in this document by 9am on Tuesday 14 April 2020. Your submission may respond to any or all of these issues. Where possible, please include evidence to support your views, for example references to independent research, facts and figures, or relevant examples.

Please include your contact details in the cover letter or e-mail accompanying your submission.

You can make your submission by:

- sending your submission as a Microsoft Word document or using the IPP Submission form on the MBIE consultation webpage to:

[FeedbackImprovingPaymentPractices@mbie.govt.nz](mailto:FeedbackImprovingPaymentPractices@mbie.govt.nz)

- mailing your submission to:

Small Business Policy  
Ministry of Business, Innovation & Employment  
PO Box 1473  
Wellington 6140

Please direct any questions that you have in relation to the submissions process to

[FeedbackImprovingPaymentPractices@mbie.govt.nz](mailto:FeedbackImprovingPaymentPractices@mbie.govt.nz)

## Use and release of information

The information provided in submissions will be used to inform MBIE's policy development process, and will inform advice to Ministers on improving payment practices.

MBIE intends to upload PDF copies of submissions received to its website at [www.mbie.govt.nz](http://www.mbie.govt.nz).

MBIE will consider you to have consented to uploading by making a submission, unless you clearly specify otherwise in your submission. If your submission contains any information that is confidential or you otherwise wish us not to publish, please:

- indicate this on the front of the submission, with any confidential information clearly marked within the text
- provide a separate version excluding the relevant information for publication on our website.

Submissions remain subject to request under the Official Information Act 1982. Please set out clearly in the cover letter or e-mail accompanying your submission if you have any objection to the release of any information in the submission, and in particular, which parts you consider should be withheld, together with the reasons for withholding the information. MBIE will take such objections into account and will consult with submitters when responding to requests under the Official Information Act 1982.

The Privacy Act 1993 establishes certain principles with respect to the collection, use and disclosure of information about individuals by various agencies, including MBIE. Any personal information you supply to MBIE in the course of making a submission will only be used for the purpose of assisting in the development of policy advice in relation to this review. Please clearly indicate in the cover letter or e-mail accompanying your submission if you do not wish your name, or any other personal information, to be included in any summary of submissions that MBIE may publish.

# Contents

- 1 Minister’s Foreword ..... 5**
- 2 Poor payment practices hurt businesses ..... 6**
  - Extended payment terms are fairly common and cause problems ..... 7
  - Businesses that freely enter into contracts with extended payment terms have very limited recourse at present ..... 8
- 3 Introducing a maximum payment term to address extended payment terms ..... 10**
  - Introduce a maximum payment term of 20 days ..... 10
  - Payment terms legislation could be applied to only some kinds of business relationships ..... 11
  - We want to ensure prompt payment is appropriate to the contractual relationship ..... 11
  - Does size of business matter when it comes to maximum terms? ..... 12
  - Such a provision could apply only to standard form contracts? ..... 13
  - We could consider different maximum terms for different industries or classes of goods ..... 13
  - Should businesses be allowed to contract out of a maximum term? ..... 14
  - When should the 20-days payment term run from? ..... 14
- 4 Introducing a right to interest and debt recovery fees to address late payments ..... 16**
  - Late payments are very common and are a major source of stress and cash flow problems ..... 16
  - Businesses that are paid late already have several options for recourse ..... 17
  - Legislation would provide for a right to interest ..... 17
  - How much would businesses be entitled to? ..... 18
- 5 There are other ways to address poor payment practices - we could do these as well, or instead ..... 21**
  - Disclosure ..... 22
  - Voluntary codes of practice ..... 22
  - Alternative dispute resolution ..... 22

# 1 Minister's Foreword

---

We want New Zealand to have a productive, sustainable and inclusive economy. An element to achieve this goal is for business people to operate in an environment that provides healthy competition through fair and reasonable business practices.

New Zealand ranks first in the world under the World Bank's ease of doing business index. We know, however, that concerns about cash flow are ever present as owner/managers work hard to operate within terms of trade imposed both customers and suppliers.

We have heard from businesses that extended payment terms, where businesses are forced to give their business customers an unusually long time to pay, are detrimental to growth and prosperity. Small businesses often don't feel able to ask for more reasonable terms. If possible, they pass on long terms to their own suppliers. But often this can't be done, thus leaving some businesses unnecessarily exposed and vulnerable.

We know that late payments can cause real harm. About half of businesses say late payments hurt their cash flow and increase their stress levels. Nearly a third say late payments inhibit their business growth.

With current technology, there is no longer any reason to impose 60 or 90-day payment terms. Even 30-day terms are a hangover of the days of posting invoices and paying by cheque. If you deliver goods and services as agreed, you should be paid according to the agreed terms. And agreed terms should now reflect the ability of twenty-first century technology to process invoices almost immediately. We still have a culture where too many people see paying on time as optional. This is unacceptable.

Government is working to improve business cash flow and stamp out unfair practices. We are leading by example, with government departments aiming to pay 95 per cent of invoices within 10 working days. We are implementing e-Invoicing, which makes sending and receiving invoices faster, easier, cheaper, more accurate and more secure. We have introduced a Fair Trading Amendment Bill that will prohibit unconscionable conduct and protect against unfair contract terms in agreements between businesses.

The time is now right to address extended payment terms and late payments. This document discusses new potential measures to make it easier to do business fairly. We want to know whether we should legislate for these measures, and, if we do, how we can make the measures effective, fair and enforceable.



Hon Stuart Nash  
**Minister for Small Business**

## 2 Poor payment practices hurt businesses

---

Good cash flow is crucial to a successful business. When customers take too long to pay it makes it harder for business to pay their own bills, increases businesses stress and forces them to waste valuable time and money chasing debts. It can keep businesses from growing; in the worst cases it can cause businesses to fail.

Small businesses tell us that large businesses sometimes impose what they feel are unfair 'extended' payment terms on them. That is, large businesses tell their small suppliers they will only buy from them if they are allowed, for example, 90 days to pay invoices. Increasing payment terms seem to be a global trend; many countries are trying to combat this problem.

We are interested in improving payment practices so that:

- businesses are paid in a timely manner, reflecting technology and the ability to process invoices much faster than ever before
- businesses have the cash-flow they need to operate effectively
- organisations don't have to waste so much time chasing debts
- payment terms are fair and reasonable
- technology adoption becomes 'business as usual' across the supply chain.

Improving payment practices has benefits for all organisations and for the economy as a whole.

We know a lot of businesses also struggle to get individual consumers to pay on time. This document doesn't cover this topic. This document is about *organisations* – mostly businesses, but also entities such as partnerships and trusts – and how they pay each other. We would like to see a regime where all organisations apply efficient and speedy resolution to their debts, while recognising that there are some contractual arrangements and entities where a strict prompt payment rule may have unintended consequences, or be inappropriate to apply.

We are interested in how to encourage organisations – businesses, government and non-governmental organisations – to:

- adopt fair payment terms;
- pay bills on time and in full.

The Government is considering introducing legislation to help with these challenges. This document:

- tells you what we know about extended payment terms, and proposes legislating a maximum payment term;
- considers the types of contractual relationships where a maximum payment rule might apply;

- tells you what we know about late payments, and proposes legislating a right to charge interest;
- discusses what we might do instead, or as well; and
- asks for your feedback.

## Extended payment terms are fairly common and cause problems

Unusually long terms are known as 'extended payment terms'. Some customers, especially large businesses or those that dominate markets, are able to *impose* extended payment terms on their suppliers.<sup>1</sup> That is, they will only do business with suppliers who accept very long payment terms. For instance, we have heard of businesses that have told their suppliers they will not pay for 120 days. Some of these businesses will offer to pay faster if they are offered a discounted rate. Others will offer their suppliers loans or refer them to a finance company (supply chain finance) to cover the delay in payment.

These same businesses often require fast payment from their customers. We have seen instances where businesses pay their suppliers after 90 days, but require payment from their customers within seven days.

Effectively this allows large businesses to use their smaller suppliers as a source of free credit. Given that large businesses can get cheaper finance than small businesses, this situation is inefficient and unfair to small businesses. An Australian study showed the costs to their economy of large businesses effectively using small ones for cheap credit is \$2.54 billion over 10 years.<sup>2</sup>

### How common are extended payment terms?

We did a survey<sup>3</sup> that found that half of businesses that send invoices with due dates on them request payment by the 20<sup>th</sup> of the following month. 43 per cent have shorter payment terms such as requiring payment on receipt of goods or services, or within seven days of the invoice date.<sup>4</sup>

However, 27 per cent of businesses have had customers request longer payment terms in the last 12 months. That is, they have been asked to have longer to pay their bills. Of those requests, half have been for payment terms of 60 days or 90 days.<sup>5</sup> Another 12 per cent have been asked for terms of longer than 90 days. Analysis by Xero found that the average delay for all payments was 8.3 days<sup>6</sup>.

---

<sup>1</sup> Imposed extended payment terms are also sometimes called 'unilateral deferred payments'.

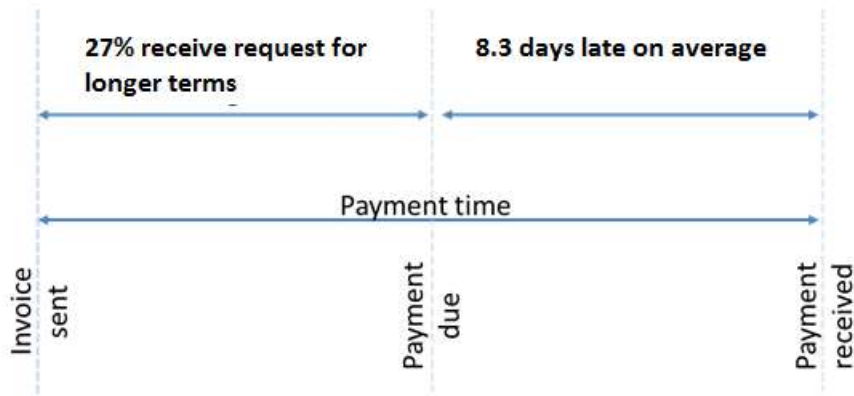
<sup>2</sup> <https://www.xero.com/small-business-insights/wp-content/uploads/2019/06/xsbi-report-paying-the-price.pdf>

<sup>3</sup> In August and September 2018 MBIE commissioned a survey of 1,254 businesses from across New Zealand about their experiences of sending and receiving invoices.

<sup>4</sup> Others have either longer payment terms, variable terms, 'other' terms or didn't know what their terms were.

<sup>5</sup> 21 per cent of requests were for 60-day terms and 29 per cent of requests were for 90-day terms.

<sup>6</sup> <https://www.xero.com/nz/resources/small-business-insights/s/metric/getting-paid/>



Nearly half of the businesses who have been asked for extended payment terms have experienced some impact or a major impact from those requests.<sup>7</sup>

Since four per cent of businesses (that is, large businesses) send half of all invoices, it is *possible* that a small proportion of businesses are making the majority of the requests for extended payment terms. Our research supports this theory; only one per cent of our research respondents who include payment terms on their invoices said they had 60 or 90-day payment terms.<sup>8</sup>

Since our research did not capture many businesses that *impose* extended terms but did capture large numbers who *receive* requests for extended payment terms, the most likely explanation is that there is a relatively small number of businesses making most of the requests.

We have also heard of cases where small businesses that have accepted extended payment terms feel compelled to pass on those terms to their suppliers. This means one large business demanding extended payment terms could potentially start a flow-on effect that spreads through an entire supply chain.

We know from talking to officials in other Organisation for Economic Co-operation and Development (OECD) countries that extended payment terms appear to be a growing problem worldwide.

## Businesses that freely enter into contracts with extended payment terms have very limited recourse at present

Businesses that are offered unfair contract terms, including extended payment terms, may try to negotiate better terms. However, we know that, for many small businesses, this is not a genuine

<sup>7</sup> 24 per cent said they experienced some impact. A further 24 per cent said they experienced a major impact.

<sup>8</sup> Interestingly, the one per cent with 90-day terms were small businesses. Even so, given that requests for extended terms are so common, it seems likely that the bulk of requests are being made by businesses with a very large number of suppliers.



option; if they do not accept the terms offered, they lose business. In some cases, small suppliers effectively have no choice but to accept their large business customers' terms.

In response to issues around unfair trade, the Government has introduced a Fair Trading Amendment Bill to:

- introduce a prohibition against unconscionable conduct in trade;
- extend the existing protections against unfair contract terms in standard form consumer contract terms to also apply to standard form contracts that form part of business-to-business trading relationships with a value below \$250,000 in a given year.

If the Fair Trading Amendment Bill passes, protections against unfair contract terms could potentially apply to extended payment terms. An extended payment term would be unfair if:

- there was not effective negotiation between the parties over the contract containing the extended payment terms;
- the term would cause a significant imbalance in the parties' rights and obligations arising under the contract
- the term is not reasonably necessary to protect the legitimate interests of the party who would be advantaged by the term
- the term would cause detriment (whether financial or otherwise) to a party if it were applied, enforced, or relied on.

For a contract term to be prohibited, the Commerce Commission would need to seek a declaration from a court that it was unfair. If found to be unfair, the extended payment term would be unenforceable. If, following a declaration of unfairness, parties continued to include such a term in their contracts, a court could impose penalties and award damages.

The Government is also considering whether the enforcement regime for unfair contract terms can be strengthened – such as by allowing small businesses to take their own action in respect of unfair contract terms directly, rather than via the Commerce Commission.

If the Fair Trading Amendment Bill passes and unconscionable conduct is prohibited, this could also apply to poor payment practices, including late payments. However, there would likely be a high threshold before conduct would be a breach of this provision. Businesses would be able to take their own legal action in respect of unconscionable conduct, or complain to the Commerce Commission. These generic protections could have a similar effect to a specific law on extended payment terms.

It would likely take several years for this process to work though in terms of any court decisions on extended payment terms and there is no guarantee that extended payment terms would end up ruled unfair. Therefore, the Government believes that a specific regulation of extended payment terms is warranted. This recognises, and make clear, that such terms are unfair, unnecessary with today's technology, and can hurt businesses. Such practice slows transactions across the economy.

# 3 Introducing a maximum payment term to address extended payment terms

---

## Introduce a maximum payment term of 20 days

We propose to introduce legislation that specifies a maximum payment term. This would mean that payment terms may not be longer than a specified number of days.

Legislation could either impose maximum payment terms without permitting any exceptions, or it could be the default position, with some opportunities to allow businesses to mutually agree to a longer term under certain limited circumstances (such as if the term is fair to both parties to the contract). This could mean that if a contract does not specify a particular term, or if there is no written contract, that the default term would be the one in legislation. This approach has been used overseas (see box overleaf).

There is at least one risk in legislating maximum payment terms. European Commission research<sup>9</sup> has found evidence that businesses may see a maximum payment term as a *recommended* term and may increase terms to the legislated maximum. That is, if there were, say, a 30-day maximum term, businesses that currently require payment within 20 days may increase their payment terms to 30 days.

The Swedish government, for example, has a 60-day maximum payment term. They have found that since they introduced the maximum term, average payment terms have increased in all sectors.

Given this, there's a risk that, in trying to stamp out the longest payment terms, we might inadvertently increase the payment terms of the best performers. For this reason, while the main intention of this proposal is to stamp out very long terms we do not favour having a 60-day maximum term like that required by the EU Directive. We also note that with today's technology, there is no longer any reason to impose 60 or 90-day payment terms. Even 30-day terms are a hangover of the days of posting invoices and paying by cheque. Therefore **we suggest a 20-day**

---

<sup>9</sup>[https://www.advokatuur.ee/uploads/files/Study\\_%20a%20comparative%20analysis%20of%20legal%20measures%20vs%200.pdf](https://www.advokatuur.ee/uploads/files/Study_%20a%20comparative%20analysis%20of%20legal%20measures%20vs%200.pdf)

## EU experience: maximum terms

The EU adopted a Late Payment Directive in 2011. The main provisions of the Directive were to set maximum payment terms for both government and private organisations, and to automatically entitle suppliers to claim interest when payment is received late (we discuss interest in the following section).

The Directive says EU countries must have laws that require:

- Public authorities to pay for the goods and services that they procure within 30 days or, in very exceptional circumstances, within 60 days.
- Enterprises to pay invoices within 60 days, unless they expressly agree otherwise and provided it is not grossly unfair.

Some countries have laws that just meet the EU Directive and some have shorter maximum payment terms. For instance, Germany and the Netherlands have a 30-day maximum payment term. The law implies that a higher payment term, whilst possible to negotiate, could be considered unreasonable in case of a dispute.

**maximum payment term.** While it is best practice to have shorter terms, this would remove the worst extended terms. We are keen to hear businesses views on this proposed payment period.

If we introduce a maximum payment term in New Zealand, there are a number of decisions we would need to make:

- To what types of contractual relationships should a maximum payment term apply?
- Should businesses be able to “contract out”?
- Should it apply to businesses of all sizes?
- Should it apply equally to all industries and classes of goods?
- When should the 20-days come into effect?

We do not underestimate the complexity of the issues the questions above raise. As we work through these proposals, we will give careful consideration to how the proposals can be best made workable for all businesses.

## Payment terms legislation could be applied to only some kinds of business relationships

We want to ensure prompt payment is appropriate to the contractual relationship

Today’s technology means that it is no longer reasonable or acceptable to excessively delay payment of debt. However we do recognise that there are some contractual relationships where a blanket rule to restrict payment terms may not be appropriate, and could have unintended consequences.

We don’t want to fix a problem, only to create unnecessary risk or uncertainty elsewhere. We want to ensure that any fix recognises the commercial reality of business relationships, while providing for contractual

certainty. We also want to target the known problem of extended payment terms which are hurting enterprises and the economy.

We know that the problem primarily lies in the supply of goods and services, generally between a small business and a large business, and involves the issue of an invoice on delivery.

Therefore, we suggest that this proposal would apply to a contract for the supply of goods and services between entities that are in trade.

However we recognise that there are some contractual relationships where a 20-day maximum payment term might be inappropriate. Such examples include

- 'Goods' that are:
  - property such as land and buildings
  - intangible, such as rights in intangible property that can only be claimed or enforced by court action. Examples include intellectual property rights such as patents, or shares in a company
  - subject to a 'security', such as a vehicle until it is paid off<sup>10</sup>.
- 'Services' that are contracts of services, such as employment contracts.

We suggest such a provision be clear about the types of contractual relationships where it would be inappropriate to apply, and seek your feedback on what these might be.

## Does size of business matter when it comes to maximum terms?

The stories we hear of extended payment terms usually involve a power imbalance between parties, generally a bigger business imposing extended terms on a smaller business.

Large businesses dealing with other large businesses can generally effectively negotiate terms without anyone being unfairly treated.

It seems likely that the main harms associated with extended payment terms come about when large businesses are dealing with small businesses.

It might be an option to have maximum terms that only apply when large businesses are dealing with small businesses or for maximum terms to only apply to contracts below a certain value. This raises the question of how to define small and large businesses.

In New Zealand, we often define small businesses as those with fewer than 20 employees. However it can create complications when businesses are at the 'margin' of large or small. Would a business with 19 employees have to change all its contracts before it could take on a 20th employee? We note that power imbalances can also occur between a sole trader dealing with a small business with under 15 employees.

Alternatively large businesses could also be defined by turnover. For example, large businesses could be defined as having over \$30, \$50 or \$100 million annual revenue.

---

<sup>10</sup> Under the Personal Property Security Register

There could be added contractual complexity in trying to define the size of business, and what provision to apply. We also note that poor payment practices, such as delayed payment terms, can also occur between small businesses.

We could instead limit the proposal to contracts below a certain value. The Fair Trading Bill Amendment Bill's provisions apply to contracts that form part of trading relationships with an annual value of less than \$250,000. This is because larger contracts are likely to be subject to more sophisticated negotiation. This same limit could be applied to any specific rule relating to payment practices, and we are seeking your views on setting such a limit.

### Such a provision could apply only to standard form contracts?

One approach could be to apply the provisions to 'standard form contracts', similar to the unfair contract terms provisions in the Fair Trading Act. This means that extended payment terms would only be prohibited in contracts that are not subject to effective negotiation. This would protect entities in cases where there are imbalances of power, but would still allow for, say, two very large organisations to trade on terms mutually agreed through effective negotiation.

Using the 'standard form contract' test of 'effective negotiation' could also act as a proxy for large firms or contractual arrangements, generally subject to more considered and sophisticated negotiation. In addition, it does not have the same definitional and threshold issues that arise by limiting to size of firm or contract outlined above. We seek your views on this limitation. We could consider different maximum terms for different industries or classes of goods

### We could consider different maximum terms for different industries or classes of goods

Some jurisdictions have different maximum payment terms for different industries. Having more than one payment term increases complexity. However, there might be good reasons why longer payment terms are reasonable in some industries or in relation to certain classes of goods or services.

For instance, Romania's law sets a maximum payment term of 30 days for food products, but 7 days for *fresh* food products because these products have a short shelf life. Some jurisdictions allow longer maximum payment terms for products sold seasonally (such as winter sporting goods).

Some industries, such as horticulture, may have very lumpy cash flow over the year, depending on when produce is ripe and available for sale, and when they might be paid for their own supplies.

Retailers generally only accept on-the-spot payment so have cash available immediately to pay suppliers. Whereas businesses that supply to other businesses may have to wait for an invoice to be paid before they have cash available to pay their own bills.

Our preliminary view is that there should be one simple rule that would be consistently applied to all business transactions. Having different rules for different sizes and kinds of businesses and/or products becomes complicated for business. We also note that the aim of this change would be to

speed up the flow of cash between businesses, potentially ameliorating cash flow issues that might currently exist.

We note that the construction sector, characterised by large and bespoke projects, and a retention regime, already has its own system for regulating payments under the Construction Contracts Act 2002, this includes a regime for dealing with disputes as an alternative to the Courts. We would need to ensure any industry specific regime has common principles and objectives.

## Should businesses be allowed to contract out of a maximum term?

We do not want to unnecessarily restrict businesses' freedom to contract. Yet we know that some large businesses already force small businesses to accept very long terms. Having a contract out option might undermine this proposal, as those businesses imposing extended terms now may continue business-as-usual if there is a way to contract out.

Some countries, such as the United Kingdom, have a maximum payment term that allows businesses to agree to a longer term than the one set out in legislation, if the term is not "grossly unfair" to the supplier.

Terms like "grossly unfair" can be open to interpretation. Although there are examples in other jurisdictions where of such interpretations are applied, such as the United Kingdom, which specified that in determining something is grossly unfair, all circumstances should be considered including:

- Anything that is a gross deviation from good commercial practice and contrary to acting in good faith and honesty
- The nature of the goods or services in question
- Whether the purchaser has any objective reason to deviate from the maximum term.

On balance, we think it would be better to allow contracting out, but only in very limited circumstances, such as where it is "grossly unfair", and we are seeking your views on the interpretation of "gross unfairness" as outlined above.

## When should the 20-days payment term run from?

There are a range of ways to determine the period of the "20-day" limit including from time of receipt of the goods or service, from invoice of the goods or services, or when the goods and services are accepted.

A working definition of "20-days", which we seek your views on, is a 20-day payment period from the later of:

- The day on which the goods or services to which the payment relates are provided
- The day on which the purchaser is notified of the amount of the payment (i.e. receives an invoice)

There may be instances where there are issues around whether the goods or services provided are actually what was contracted for.

In such circumstances we propose there be a procedure for confirming and verifying acceptance. The purchaser could receive an invoice during, or at the end of, this verification procedure. The 20-day payment period could run from the end of the verification procedure, with the verification period capped at a specified number of days in the legislation.

The 'verification period cap' could be contracted out of if to do so would not be grossly unfair to the supplier.

1	Have you experienced problems with extended payment terms? Do you require your suppliers to offer them? Please tell us about your experiences.
2	Would you support a legal maximum payment term? If you do support a legal maximum term, do you think it should be 20 days or some other term?
3	Should they only apply to large businesses, or to large contracts, or to standard term contracts?
4	Should any industries or classes of goods have longer or shorter maximum terms?
5	What sorts of contractual relationships might it be inappropriate to apply a maximum term to?
6	Should businesses be able to contract out, and if so, in what circumstances?
7	If you agree with contracting out where a term is not "grossly unfair", do you agree with the circumstances to be considered in determining "gross unfairness"? Are there other circumstances that we should consider?
8	Do you agree with the proposed definition for determining the 20-day period, and a process of acceptance or verification of goods or services?

PROACTIVELY RELEASED

# 4 Introducing a right to interest and debt recovery fees to address late payments

---

Late payments are very common and are a major source of stress and cash flow problems

Late payments are very common

Two-thirds of the businesses we surveyed said that, at some stage in the last 12 months, they had not paid an invoice on time. Xero's Small Business Insights for the year to September 2019 show that small business invoices on their platform are paid 8.6 days late on average. Xero estimates New Zealand small businesses are owed about \$7.4 billion total in unpaid invoices.

Businesses told us some of the reasons they pay invoices late. The most common reasons<sup>11</sup> they gave were:

- forgetting to pay or mistakenly thinking they had already paid (46 per cent of businesses identified this as a reason);
- having insufficient funds to pay (42 per cent of businesses identified this as a reason);
- not having been paid by their customers (35 per cent of businesses identified this as a reason).

When businesses are not paid on time, most (89 per cent) follow up the customer with an email or telephone call. Only 10 per cent of businesses surveyed have an automatic system to send reminders to later payers and 10 per cent of businesses offer plans so invoices can be paid in instalments.

When it comes to the process of invoicing, having to follow-up late payers (36 per cent) and sending reminder notices (28 per cent) were the most significant 'pain points'.

This suggests that greater use of automatic reminder systems might make life easier for many businesses.

---

<sup>11</sup> Businesses could choose more than one reason so percentages total more than 100%



## Late payments hurt businesses

Late payments seem to have a severe effect on businesses. Of the businesses we surveyed:

- 49 per cent said late payments hurt their cash flow;
- 48 per cent said it increased their stress levels;
- 30 per cent said it impacted their ability to grow.

The businesses experiencing cash flow problems because of late payments often themselves delay paying the invoices they have received (25 per cent), cover their business expenses by organising overdrafts or personal loans with their bank (31 per cent) and/or use personal savings (38 per cent).

## Businesses that are paid late already have several options for recourse

Businesses that are paid late already have several options for recourse. They can:

- send notices reminding customers of their contractual obligations;
- enlist debt collectors;
- take the matter to the Disputes Tribunal if the money sought is under \$30,000<sup>12</sup>;
- take the matter to court:
  - a court may make a range of orders, including payment of the money owed and awards for damages. The Interest on Money Claims Act 2016, discussed shortly, provides for the award of interest as compensation for a delay in the payment of debts, damages, and other money claims in respect of which civil proceedings are commenced.

Despite the availability of these options, businesses may not pursue late payments due to the cost involved, or because they worry it could damage relationships with their business customers – potentially to the point that the business customer in question refuses to do business with them in future.

## Legislation would provide for a right to interest

Late payments have direct and indirect costs on businesses.

---

<sup>12</sup> The Disputes Tribunal cannot consider matters where there is a payment owing which is not in dispute. However, it can make a range of orders – including the payment of interest or damages – where there is a payment owing which is disputed, or where a late payment has been made.

## EU experience: interest and debt-recovery costs

The EU Late Payment Directive requires member countries to have legislation saying businesses are automatically entitled to interest for late payment and €40 *minimum* as compensation for recovery costs. The United Kingdom has rates ranging from £40 to £100 depending on the size of the debt.

The statutory interest must be at least eight percentage points above the European Central Bank's reference rate. Germany, for instance, has opted to provide for a higher rate of interest of nine percentage points above the reference rate.

Businesses do not need to go to court to be awarded costs. Rather they just send an invoice for the interest and/or debt recovery fee.

However, **few businesses claim the interest or costs to which they are entitled.** This seems to be because they fear that exercising their right to this money might antagonise their customers.

Although 85 per cent of businesses are aware they are entitled to debt recovery costs, only 7 per cent actually claim it.

This suggests that, if we had a legislated right to interest and/or debt recovery fees there would need to be supporting work to encourage a culture of exercising those rights.

Businesses are already entitled to charge interest and/or debt recovery fees to help recoup these costs. Our survey showed that 18 per cent of businesses include information on late payment penalties on their invoices. We do not know how many businesses have interest or penalty provisions in their *contracts*. However, only five per cent of businesses surveyed say they actually charge penalties when customers have not paid an invoice on time.

We are considering legislation to:

- help businesses recover the costs they experience from late payments AND/OR
- provide an alternative means for businesses to obtain compensation for their losses arising from late payment.

We are proposing an *automatic entitlement* to interest for late payments. That is, businesses would not have to go to court to create a legal basis under an Act to claim interest. Rather they could be claimed as a right.

This approach has been used overseas [see box opposite].

### How much would businesses be entitled to?

We already have legislation that gives businesses the right to interest as compensation for late payments if a business takes civil proceedings (goes to court). Businesses can also agree to include late payment charges in their contracts.

The Interest on Money Claims Act 2016<sup>13</sup> provides “for the award of interest as compensation for a delay in the payment of debts, damages, and other money claims in respect of which civil proceedings are commenced”. That is, if you take a business to court for a late payment, the Interest on Money Claims Act sets out how to calculate the interest you will receive.

The Act provides for a Civil Debt Interest Calculator<sup>14</sup> which calculates the total amount owed (including interest) on court-awarded civil judgments where the Interest on Money Claims

<sup>13</sup><http://www.legislation.govt.nz/act/public/2016/0051/latest/DLM6943301.html>

<sup>14</sup><https://www.justice.govt.nz/fines/civil-debt-interest-calculator/>

Act 2016 has been applied. The interest rate is calculated based on the Reserve Bank of New Zealand's six-month term deposit rate plus a base rate of 0.15 percentage points. At November 2019 this works out to roughly 2.8 per cent per annum.

This rate is intended to "reflect fairly and realistically the cost to a creditor of the delay in payment of a money claim by a debtor".

If there were an automatic right to interest in New Zealand, it would be relatively simple to use the existing approach set out in the Interest on Money Claims Act 2016.

However, small businesses in New Zealand are very likely to face higher costs from late payments, and also may face opportunity costs from the reduced cash flow.<sup>15</sup> They often rely on credit to manage over periods of non-payment, with the interest at a rate higher than the rate estimates for the Money Claims Act. In some cases, particularly for a large firm, the value of deferring payment of bills may be higher to them than the interest costs they otherwise have to pay under the Money Claims Act.

We therefore think it's worth considering a higher interest rate than the Interest on Money Claims Act 2016 provides for, at least where small businesses are the creditors, to reflect the true costs they face from deferred payment. We would need to undertake some analysis to estimate the additional costs that small businesses incur from delayed payments. We are keen to hear from businesses on the sorts of costs they incur as a result of late or deferred payment terms.

**We propose that businesses would have the right to claim interest on late payments to reflect the true costs of non-payment faced by businesses.**

We are considering whether this right to interest should apply to businesses of all sizes and types, recognising that small businesses generally face higher costs of credit than larger ones. We are interested in hearing from businesses the costs they face from deferred payment terms.

How might a scheme to charge for late payments be implemented and enforced?

Whatever the interest rate, the scheme would only have an impact to the extent that businesses are willing to charge their customers for late payments. The EU example shows merely *providing* for interest in legislation is not enough. Rather legislation would likely need to be accompanied by a cultural change whereby paying on time is the norm and charging for late payment is seen as routine.

In addition, New Zealand could consider the right to debt recovery costs, as they have in the European Union. There is some merit to this, as it may act as a stronger deterrent to paying late. However, this is a bigger departure from current practice than charging interest. We do not propose

---

<sup>15</sup> Our research showed businesses delay paying the invoices they have received (25 per cent), cover their business expenses by organising overdrafts or personal loans with their bank (31 per cent) and/or use personal savings (38 per cent). For instance, according to the Reserve Bank, the average SME overdraft rate in recent times has been over 9 per cent <https://www.rbnz.govt.nz/statistics/b3>

to legislate for a right to debt recovery costs at this stage. Businesses are still free to charge for debt recovery. This could be reviewed as we assess the uptake and effectiveness of charging interest.

We also need to consider how a late payment rule would be put into practice, and the consequences of failure to comply. For example, would it be possible for business to negotiate to vary, or remove, the interest, or to replace it with an alternative “substantial remedy”, as provided for in some other jurisdictions<sup>16</sup>.

We are not proposing a new enforcement mechanism beyond those already available to businesses, including through access to the Courts. However note that access to the Courts can be time consuming and costly, particularly for small business.

As a result, in addition to the rules around maximum payment terms and interest on late payments, one option would be to introduce an implied dispute resolution clause. This would mean that, if contracts did not include their own provisions around dispute resolution, they would be required to include a clause as specified in the legislation.

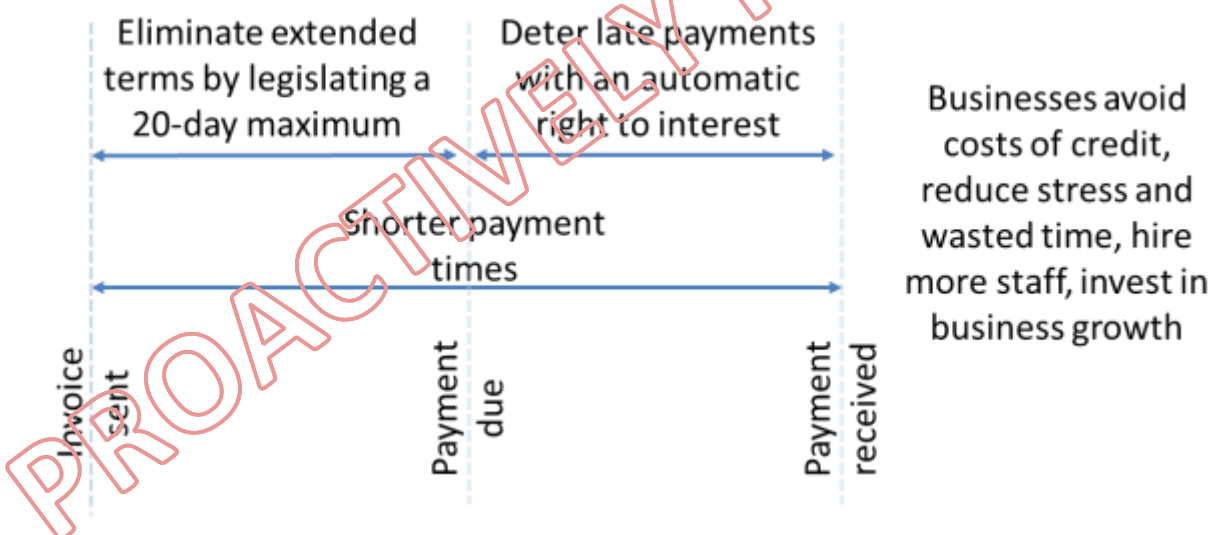
9	Have you experienced problems with late payments or paid invoices late yourself? Please tell us about your experiences.
10	What costs do you incur as a result of late, or deferred, payments?
11	Would you support an automatic right to claim interest for late payments? Why or why not?
12	Do you have late payment fees or interest clauses in your contracts or on your invoices? Do your suppliers charge you interest or fees for late payment?
13	Should a right to claim interest apply equally to all kinds and sizes of businesses?
14	Should there be some ability to vary or replace the interest rate for late payment in some cases? If so, in what cases?
15	If there were to be new legislative requirements designed to prevent unfair payment terms and invoicing practices, what do you think would be the best way to encourage businesses to comply?

<sup>16</sup> United Kingdom’s Late Payment of Commercial Debts (Interest) Act 1998

## 5 There are other ways to address poor payment practices - we could do these as well, or instead

So far, we have discussed two proposals for legislation to address poor payment practices. The proposals are:

- A 20-day maximum payment term. Businesses can mutually agree a longer term provided the term is not grossly unfair to either party
- The right to charge interest on late payments. We propose that the interest rate be the Reserve Bank of New Zealand's six-month term deposit rate plus a base rate of five percentage points.



As mentioned earlier, the Government is already working to improve payment practices. This is largely through leading by example, implementing e-Invoicing and introducing the Fair Trading Amendment Bill. Government also issues guidance on [business.govt.nz](http://business.govt.nz) on good invoicing practices and how to chase up late payers.

In addition, there are possibilities we have not yet discussed. Below is a brief overview of the main ideas and why we are not considering them at present.

### We are leaving some ideas off the table for now

There are a few other initiatives that have been used overseas, with varying degrees of success. We might consider these in the future. We are noting some of the main candidates now so you know

what other avenues we could pursue in the future, whether or not we legislate maximum payment terms and/or interest and debt recovery fees.

## Disclosure

Other countries require, or are considering requiring, large businesses to publicly report on their payment times and/or terms.

A disclosure regime might have two benefits:

- it would mean organisations could decide not to enter business relationships with known poor payers;
- the prospect of being “named and shamed” as a poor payer might encourage organisations to be better payers.

We are not considering a disclosure regime at present, but will monitor how overseas regimes work. From what we know so far, it is very hard to establish whether disclosure regimes have any effect. The costs of compliance to large businesses are direct, while any benefits to small businesses would be indirect and hard to measure.

## Voluntary codes of practice

Some countries have codes of payment practice to which organisations may choose to sign up, declaring that they will meet certain standards in their payment times and terms. In some countries, these Governments administer the codes. In others, business representatives run them.

Generally, voluntary codes seem to have very low levels of uptake and there is scant evidence they are effective.

## Alternative dispute resolution

Disputes are one reason for late payments. This is sometimes because there are genuine disagreements about whether goods or services have been delivered to an acceptable standard. We also hear of cases of vexatious disputes, designed to delay payment.

Some contracts already contain clauses setting out what to do if there are disputes. However many businesses are reluctant to use formal disputes resolution services because they are concerned about cost, time and antagonising their customers.

We think there might be a case for encouraging businesses to use alternative dispute resolution mechanisms and will consider this in the future.

# Extended payment terms and late payments are a problem; we want to hear your views on how to make things better

---

We know that extended payment terms and late payments are a significant source of stress and cash flow problems for businesses. Small businesses feel these problems especially acutely.

We welcome your feedback on the proposals in this discussion document.

16 Do you have any other views you would like to share on how to improve payment practices in New Zealand?

PROACTIVELY RELEASED