

## Contractor guide to charging interest on late payments

The right of any business, including [contractor limited companies](#), to claim interest on unpaid bills from customers and clients is enshrined in UK and European law.

The [Late Payment of Commercial Debts \(Interest\) Act 1998](#), and amendments in 2000 and 2002, mean that contractors have a statutory right to claim interest from their clients or agents who don't pay bills on time.

But how is interest calculated? When is a payment deemed to be late? And when should interest be charged? ContractorCalculator's [late payment interest calculator](#), in conjunction with this guide, can work out how much contractors should charge and when.

### When is a payment late?

When a contractor enters into a contract with their client or agency, one of the key clauses in the contract will be the payment terms. Typically, the contract will specify after how many days from the date of invoicing the payment should be made. In some rare cases, it will state how many days after performing the service or getting a signed timesheet the client or agent must pay.

Because contractors come in all shapes and sizes, so do their payment terms. Most, however, expect to be paid within seven days of invoice if they are a 'weekly' contractor, or within 30 days of invoice if they are a 'monthly' contractor.

The law says that, in the absence of agreed terms between the supplier, ie the contractor, and their customer, ie the client or agent, the payment terms are assumed to be 30 days from invoice.

This means that if the contractor sends an invoice dated the first of the month, the payment should be expected to arrive by the 30th day of that month. Some client's and agency's finance departments will try and flannel contractors by saying it's '30 working days', but according to the law there is no doubt – 30 calendar days it is.

### What interest can be charged?

Interest can be charged on an overdue payment from the day after the last day that it should have been paid. So, using the example above, if the invoice was dated the first of the month and the terms are 30 days, then the contractor can start charging interest from the 31st day, which could be the 31st of that month or the first of the next.

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From the point that the payment on the invoice becomes due, the interest will start to accrue on the principal debt owed to the contractor by their client or agency, based on a formula of the 'reference rate' of the [Bank of England](#) plus 8%.

The interest calculated is simple, not compound, according to the following:

Debt x interest rate x (the number of days late/365) = interest

Interest is charged on the gross amount of the debt including VAT, but VAT is not charged on the interest.

It all sounds rather complicated, but don't worry, ContractorCalculator's [late-payment calculator](#) will do the hard work for you.

If you'd like an example, though, here you are:

Say a contractor is owed £851.06 plus VAT of £148.94 for their fee, which makes the nice round sum of £1,000. The contractor invoiced their client for this sum on 1st May with 30 day terms, meaning the client must pay them £1,000 by or on 30th May. Failure to do so means the contractor can start charging interest from 31st May.

Let's say the client has not paid by 29th June, which is 30 days after the debt should have been paid. The contractor can then charge the client 30 days interest.

If the 'reference rate' of the Bank of England is 4%, then the total interest is 12% (reference rate plus 8%). To calculate the interest on the late payment:

£1,000 x 12% = £120 (the interest to be paid in a year)

£120/ 365 = 32.9p (the daily interest)

32.9p x 30 days = £9.86 (the interest owed to date on 30 days)

For the average contractor, owed several months fees over three months or more, this sum starts to add up. And for the agency or client it adds up too, hopefully providing them with the incentive to pay the money they owe the contractor without further delay.

### Make sure everything is in writing

To be sure that the legislation works completely in their favour and there is no chance of the client or agency getting off on a technicality, the contractor should ensure that their paperwork is squeaky clean. This means:

- o Agree payment terms in writing
- o Include interest charges, and the intention to claim them, in the payment terms
- o Ensure timesheets are correctly signed off, to avoid disputes
- o Ensure there is no reason for agencies or clients to dispute invoices
- o Make sure that your terms clearly state the time period in which the client or agent must raise a dispute (otherwise they could buy themselves time by waiting until the invoice is due for payment before disputing it)
- o Inform the client in writing when the debt is due that action will be taken and interest charged.

Case law now works in contractors' favour when invoices remain unpaid and clients and agencies can no longer hide behind minor inconsistencies or errors in invoices and refuse to pay their suppliers – the courts will give them short shrift.

But this does not mean contractors should be anything less than totally efficient and professional in their paperwork and debtor management, particularly as the next stage of chasing late payments is to start debt recovery proceedings.

### Be reasonable...

Although the law allows you to start charging interest immediately, remember that genuine errors and oversights do occur, and that accounts departments are made up of fallible people.

So rather than being heavy-handed as soon as payment is due, it is always best to start the process with a friendly telephone call to the client or agent, followed up with a polite and friendly letter.

Better still is to avoid such situations ever arising, by following the advice given elsewhere on this site, and detailed in the [Contractors' Handbook](#), on how best to ensure you get paid on time, every time.

Further advice on using the Late Payment of Commercial Debts (Interest) Act 1998 is available from [Business Link](#) and [The Better Payment Practice Campaign](#).

**Published: Tuesday, March 17, 2009**

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