

General Comments

The clauses in a contract which deal with payment are arguably some of the most important terms. Ultimately, the ability to extract prompt payment and recover late payments affects cash flow. That cash flow is the “very lifeblood of the enterprise” as Lord Denning described it.

Every type of business works on a different set of deadlines for payment, different methods of payment and by its very nature different collection methods. There are no hard and fast rules for any of the payment terms that I am going to discuss. Many contracts are market led, to a greater or lesser extent.

How to Get Paid

The clauses which deal with the prompt payment or the recovery of late payments should use clear simple language. The more contorted the language, the more confusion or misunderstanding there may be about its intent. Ultimately if the clause is not written in clear terms it might be difficult to enforce it at the end of the day.

Checklist of Payment Clauses that might appear in a Contract

When is payment to be made? The contract should specify:-

- The due date that payment is to be made – the trigger date. This might be an event, for example on delivery of goods or services, or a set number of days after an event, for example 7 days after a bill of lading is issued.
- The payment procedure. This might specify to which account monies are to be paid and in some situations the form which the payment is to take. For example, if funds are to be remitted by telegraphic transfer the contract might specify for whose account the banking charges are. Our standard terms of contract specify that payment of fees by credit card is permissible – but many other law firms will not accept payment by that method.
- International contracts should specify in which currency payment is to be made.
- The documents necessary to be presented for the payment to occur. However it is more usual to find these details in an appendix/supplemental document/side letter/oral agreement, which is separate from the central terms and conditions.
- The contract might specify that the time of payment is “of the essence”. This is effectively giving notice that if the payment date is missed that breach goes to the heart of the contract. There may be a right to bring the contract to an end if the payment date is not met.
 - No payment shall be deemed to have been received until the company has cleared funds.

What happens if payment is delayed/late/never arrives?

- Interest may be payable – the contract should specify on what date interest starts to run and how any interest is to be calculated.
- In some situations a contract can be brought to an end if payment has not been made and the timing of the payment was agreed to be of the essence.

In addition

- The contract might include a right to lien or to restrain goods or other property in order to secure the outstanding payment, which has not been made.
- In that situation the contract should include subsequential clauses dealing with what will happen if a lien does not work and funds are not forthcoming. The clauses should give a right to sell the goods, and provide for what will be done with the proceeds of sale – if they exceed the value of the debt due.
- The contract terms might give one or both parties the right to set off a debt due under one contract against monies payable to it under another contract.
- Alternatively it might specify that all payments due under the contract should be in full without any deduction, set off, counterclaim, discount.
- It might include a clause that all payments payable to the company under the contract are due and payable on its termination despite any other provision.
- Incorporate a retention of title clause, so that ownership of the goods in the buyer's hands remains with the seller – on non-payment.
- Incorporating provisions in the standard terms, which on the occurrence of an event such as presentation of a winding up petition entitles the seller to:-
 - Terminate the contract;
 - Suspend future deliveries;
 - Cancel any existing orders.

Additional liabilities may be imposed.

- For example, Lester Aldridge's terms and conditions specify that if a company does not pay its debts, the directors of a company can be held personally liable for the debt.
- If more than one party is a party to a contract, the contract terms should specify that liability is joint and severable.

The general rule with any of these clauses is to ensure that a company exercises its contractual rights to require payment in the way the contract specifies. In many situations a written contract might only be looked at in detail when it is signed or accepted. In many situations a course of dealing arises between companies who engage in a business relationship over a sustained period of time. This can mean that the payment terms in a contract are not as closely adhered to as was originally intended. The consequence of not requiring strict adherence in the first place is that the contract terms may not be fully enforceable at a later date.

If interest is said to be payable within 3 days of late payment – then interest should be demanded. If no interest is demanded during the life of a contract (which might be operational over several years), an English Court might not allow a company to recover interest at that specified contractual rate. This is because a course of dealing between the parties might have resulted in a waiver of the strict contractual right which was agreed in the first place. In that situation a company would have to rely upon the courts general discretion on whether interest should be awarded on the debt and at what rate.

A similar situation arises with clauses which entitle a company to bring contracts to an end if monies are not paid on time. The right to bring the contract to an end must be promptly exercised. If it is not, it may be fatal. The English Courts are not sympathetic to a party who tries to bring a contract to an end – after accepting late payments regularly. There is any number of cases in shipping law where owners have unsuccessfully tried to withdraw their ship from a slow paying charterer many months after accepting late hire payments. They have failed in their attempts – even though there is a clear right to withdraw in the charterparty contract.

The contract should also specify

- How any disputes are to be handled i.e. pursuant to the rules of a trade association, arbitration, court mediation.
- In international contracts the contract should specify which law will apply to the determination of the dispute ie. English Law.
- How notice of any dispute or any legal proceedings will be notified to the other party. In many situations parties will agree that notice should be given within set times and that the notice should be sent to a particular address.

Encouraging Prompt Payment

- Imposing a high but not excessive rate of interest on late payments.
- Giving the buyer a discount if payment is made before a specified date. Parking fines are a classic example of this technique.
- Where a buyer is paying the price by instalments, including a provision that if any instalment is late, the remaining outstanding balance becomes payable.
- Providing for future deliveries to be withheld whilst any instalment is overdue.

Advance Payments / Deposits

Many high value “one off” transactions require an advance payment, payment on account or a deposit, for example a deal involving the purchase of premises, land, goodwill, and items such as ships or aircraft.

In the service industry money on account may be required. For example when dealing with new clients some solicitors and accountants will ask for money on account before undertaking any work.

What do these type of contracts need to consider?

- When the deposit, or money advance is to be paid. What event triggers the payment?
- What will happen if the deposit or monies are not paid on time? In many situations time is of the essence in these contracts. If the money is not received the contract can be brought to an end.
- Who will “hold” the money and where will it be held?
- How will interest earned on the deposit be dealt with?
- What event will allow the deposit monies to be released and to whom
- If the contract fails what will happen to the funds on deposit?
- What expenses can be deducted from the fund if the monies are to be returned?
- What forum and what law will be applied for deciding any disputes about the deposit monies?

Documentary Letters of Credit

These are used in international trade. They deal with the situation where an importer or exporter wants to ensure that they get paid for the goods/services they provide and the importer wants to be sure that they only pay for the goods and services they require.

Documentary letters of credit are operated through the international banking system. In practical terms it is a written undertaking given by a bank on behalf of an importer. It agrees to pay the exporter an amount of money within a specified time provided the exporter presents documents in accordance with the terms laid down in the letter of credit.

As such there is a certainty of payment, which ultimately means exporters can offer extended credit terms to their buyers. Importers gain more control over their terms of trade because of the certainty of payment, the ability to improve credit terms or achieve price discounts.

The letter of credit will specify when payment is to be made. This is either:-

- When certain documents are presented to the buyers bank – the paying bank. The letter of credit will specify which documents are to be presented.
- Or at some future date - usually within 180 days of receipt of the documents by the paying bank.

Letters of Credit are administered by the Banks using an international set of Rules known as the Uniform Customs and Practice for Documentary Credits (1993) Revision. This document is known in its short form as UCP 500. Agreeing to accept payment by letter of credit might inadvertently incorporate UCP 500 into a company's standard terms and conditions. This is because the letter of credit will specify that the Rules apply.

The letter of credit system operates in tandem with the standard terms and conditions. It is a method of guaranteeing payment – not ordinarily expressly included in the body of the terms and conditions.

Sometimes there maybe a reference to a letter of credit in the body of the terms and conditions. Ordinarily the banking arrangements, which underlie the letter of credit system, are not dealt with in the basic contract. Care should be taken to ensure that any addendum to the original contract dealing with the method of payment by letter of credit – is not contrary to the enforcement/recovery clauses in the terms and conditions.

Payment by Bills of Exchange

Used in international trade in a similar way to letters of credit as a way of ensuring payment arrives on time. A bill of exchange is an unconditional order to pay a specific sum of money on a particular date. The letter of credit system works slightly differently by specifying a range of dates when payment is to be effected.

A bill of exchange is payable immediately and is usually issued payable at sight- ie. once the demand for payment is made.

Alternatively the bill might be payable at some future date ie. drawn payable at 60 days from sight.

Bills of exchange are commonly used against a letter of credit. In a lot of jurisdictions the government levys a heavy tax on the drafts used on a bill of exchange and they are unpopular for that reason.

The central terms and conditions are unlikely to contain any reference to bills of exchange. They will be treated in the same way as agreeing to accept a payment by way of letter of credit.

Terms of Trade

Sometimes terms of trade can be inadvertently or expressly incorporated into the standard terms of a contract.

For example, it is common to see references to a standard set of trade terms applying to a contract. These are incorporated even though those terms are not expressly dealt with in the body of the contract. An example of this might be the Freight Forwarders Association Rules.

Often those rules will cover areas such as payment, time limits for presenting claims, dispute forum etc.

A company's standard terms and conditions need to highlight any variances or differences between a trade associations rules and their own terms and conditions. Where there are differences it maybe necessary to include a specific provision/clause dealing with the differences.

International Conventions can often be implied or expressly incorporated into contractual terms. My colleague Michael Giddins will deal with some of these later today when looking at limitation. In shipping the Hague and Hague Visby Rules are incorporated in that way in many contracts.

In addition, a course of dealing between parties can imply a term of trade into the body of a contract without either party necessarily understanding what has taken place. If two parties contract over a long period of time (sometimes on an oral basis) to do business, and then there is a disagreement between those two parties, both of would turn to the terms and conditions. However, the way in which the business has been done over a number of years may not be in line with what was expected to be done by the standard terms of contract nor, expressly covered by that contract.

Contracts should be kept under constant review.

Discounts

These are not generally covered by a standard term or condition in a contract unless the price which is payable for a unit, is based on volume. They are subject to market forces in the same way as many other businesses. If discounts are specifically dealt with in the body of the contract the clauses must be clear as to their intent.

Form of payment

Not always dealt with in the body of the terms and conditions themselves unless particular situations have arisen. For example, the case of our own terms and conditions where the facility to pay by credit card has been included. Generally dealt with by a separate agreement.

Agreed payment for non performance

There are two ways in which these operate. Either deposit monies are retained as a sum of liquidated damages for a breach of contract. Alternatively the contract includes a specific clause which enumerates how much is payable as a liquidated damages sum. This might be put on the basis of a simple formula.

It is important to cover the following points in clauses of these types:-

- What event /due date will trigger the agreed payment?
- Within what time frame will the amount be payable?
- What procedure will be invoked if the agreed payment is not made. The clause might include a statement that the agreed payment for non-performance should be treated differently from debts that are due but disputed.

Set off Clauses

A contract should specify whether either party is entitled to set off part of the debt owed against monies which are payable to the other party.

If company A owes company B US\$10,000 but company B owes company A US\$5,000 in credit on the same contract, there may be an implied right to set off the sums against each other.

Contract Clauses Differ

- Some contracts allow no set off at all.
- Some permit some deductions – which are specifically identified to be made.
- Some contracts permit amounts on different contracts to be set off against each other for any items i.e. claims.

Whichever situation is agreed – the contract must be clear about what can / can not be done.

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