THE LATE PAYMENT DIRECTIVES 2000/35/EC AND 2011/7/EU AND SUPPLIER PAYMENT BY A PUBLIC AUTHORITY BEFORE THE EUROPEAN COURT OF JUSTICE: FOR AN INTERPRETATION THAT IS COHERENT WITH THE ACQUIS

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I.- Introduction

The fight against late commercial payment is a matter of increasing concern to the EU Member States. This concern has been particularly intense in Spain since the beginning of the severe economic crisis in 2007. This general problem affecting trade relations and the good functioning of the economy has observed how late payment within the Spanish public administrations has reached extreme levels. Since 2007 the debts incurred by Spanish public administrations to suppliers and subcontractors have risen to incredibly high rates that have resulted in the financial instability of many companies, particularly SMEs.

The EU law has tried to put an end to this serious situation distorting the good functioning of the EU internal market. The Directives 2000/35/EC and 2011/7/EU have established a set of measures aiming to fight late commercial payment. In short, the EU law has recognized the right of the creditor to be automatically entitled to a high interest rate as long as he has fulfilled all his contractual and legal obligations and he has not received the amount due on time. Specific obligations have been imposed on the

Member States in order to implement these measures and the scope of the free will of the parties when establishing trade agreements has been limited.

Initially, Article 3 of the Directive 2000/35/EC stipulated that:

"1. Member States shall ensure that:

a) interest in accordance with point (d) shall become payable from the day following the date or the end of the period or payment fixed in the contract;

b) if the date or period for payment is not fixed in the contract, interest shall become payable automatically without the necessity of a reminder:

i) 30 days following the date of receipt by the debtor of the invoice or an equivalent request for payment.

[...]

c) the creditor shall be entitled to interest for late payment to the extent that:

i) he has fulfilled his contractual and legal obligations; and

ii) he has not received the amount due on time, unless the debtor is not responsible for the delay.

d) the level of interest for late payment ('the statutory rate'), which the debtor is obliged to pay, shall be the sum of the interest rate applied by the European Central Bank to its most recent main refinancing operation carried out before the first calendar day of the half-year in question ('the reference rate'), plus at least seven percentage points ('the margin'), unless otherwise specified in the contract. [...]

e) unless the debtor is not responsible for the delay, the creditor shall be entitled to claim reasonable compensation from the debtor for all relevant recovery costs incurred through the latter's late payment. Such recovery costs shall respect the principles of transparency and proportionality as regards the debt in question. Member States may, while respecting the principles referred to above, fix maximum amounts as regards the recovery costs for different levels of debt.

[...]

3. Member States shall provide that an agreement on the date for payment or on the consequences of late payment which is not in line with the provisions of paragraphs 1(b) to (d) and 2 either shall not be enforceable or shall give rise to a claim for damages if, when all circumstances of the case, including good commercial practice and the nature of the product, are considered, it is grossly unfair to the creditor. In determining whether an agreement is grossly unfair to the creditor, it will be taken, inter alia, into account whether the debtor has any objective reason to deviate from the provisions of paragraphs 1(b) to (d) and 2. If such an agreement is determined to be grossly unfair, the statutory terms will apply, unless the national courts determine different conditions which are fair.

4. Member States shall ensure that, in the interests of creditors and of competitors, adequate and effective means exist to prevent the continued use of terms which are grossly unfair within the meaning of paragraph 3."

Given that it was widely considered that Directive 2000/35/EC was not meeting its objectives[1], it was modified by Directive 2011/7/EU with the aim to strengthen the fight against late payment and enhance the efficacy of the EU measures. Article 7 of this new Directive stipulated that:

"1. Member States shall provide that a contractual term or a practice relating to the date or period for payment, the rate of interest for late payment or the compensation for recovery costs is either unenforceable or gives rise to a claim for damages if it is grossly unfair to the creditor.

In determining whether a contractual term or a practice is grossly unfair to the creditor, within the meaning of the first subparagraph, all circumstances of the case shall be considered, including:

a) any gross deviation from good commercial practice, contrary to good faith and fair dealing;

b) the nature of the product or the service; and

[1] As stated by Eleanor Sharpston, Advocate General at the European Court of Justice in Case C-555/14, which is the subject of this comment

c) whether the debtor has any objective reason to deviate from the statutory rate of interest for late payment, from the payment period as referred to in Article 3(5), point (a) of Article 4(3), Article 4(4) and Article 4(6) or from the fixed sum as referred to in Article 6(1).

2. For the purpose of paragraph 1, a contractual term or a practice which excludes interest for late payment shall be considered as grossly unfair.

3. For the purpose of paragraph 1, a contractual term or a practice which excludes compensation for recovery costs as referred to in Article 6 shall be presumed to be grossly unfair.”

In addition, Article 12 stated that “Member States shall bring into force the laws, regulations and administrative provisions necessary to comply with Articles 1 to 8 and 10 by 16 March 2013”.

For a correct assessment of the legislation mentioned above it is absolutely relevant to keep in mind that, after the 2011 Directive, on 29 April 2016 the Committee on Regional Development presented a motion for a European Parliament resolution which was finally approved and which stated that:

“*23. Calls on the Commission and the Member States to urgently find a lasting solution to the backlog of payments related to regional policy and to properly apply the Late Payment Directive (2011/7/EU), so as to ensure that SMEs, as project partners, will not be deterred from taking part in support programmes and projects during the current programming period on account of payment delays; also points out that more thorough compliance with this directive, requiring, inter alia, that public authorities make payments within 30 days for the goods and services that they procure, would contribute to creating the conditions for stabilisation and growth of SMEs.”*

This motion proves that the EU is convinced that Member States are not correctly applying the rules on the fight against corruption and that more efforts need to be made to instrumentalize actual efficient mechanisms. The success of the opinion of the Advocate General in Case C-555/14 would entail a huge backward step. In fact it would block all efforts made so far in the fight against late payment.

II.- Spanish supplier payment mechanisms and the request for a preliminary ruling in Case C-555/14

The severe economic crisis brought Spanish local and regional public administrations to delay supplier payments for a long period of time, sometimes over 550 days. In this context, the central Government implemented several supplier payment mechanisms consisting in the identification of the local and regional authorities' debt and subsequent transfer of the amounts from the central Government to these administrations so that they could pay off debt. However, the transferred amounts were limited to the principal and did not include the interest for late payment. In accordance with these exceptional mechanisms, suppliers interested in this option had to expressly waive the recovery of the legal interest as well as the compensation for the recovery costs incurred.

The Extraordinary Mechanism for the Payment to Suppliers of the Local and Regional Public Authorities ("Mecanismo Extraordinario de Pago a Proveedores de las Administraciones Públicas de las Entidades Locales y de las Comunidades Autónomas") was financed through a €30 billion syndicated loan (which could be increased to €35 billion[2]) created by the Government and 26 financial institutions and signed by the Fund for Financing Supplier Payments ("Fondo para la Financiación de Pago a Proveedores"). The mechanism was implemented in several stages. The first one was adopted through the Agreement 6/2012, of 6 March, of the Fiscal and Financial Policy Council and through the Royal Decree-Law 4/2012, of 24 February. It is important to note that this process was limited to the recovery of the principal and required that the supplier waive the recovery of the interest for late payment and other associated rights such as compensation for recovery costs.

Considering the increase in the debt of the public administrations, the second stage was regulated by the Royal Decree-Law 4/2013, of 22 February, on measures to support entrepreneurship and promote growth and job creation. This legal text was also based on the general principles of the first stage, as well as on the obligation to waive the recovery of the interest for late payment and other associated rights.

[2] See MAR DELGADO TÉLLEZ, PABLO HERNÁNDEZ DE COS, SAMUEL HURTADO Y JAVIER J. PÉREZ. Los mecanismos extraordinarios de pago a proveedores de las Administraciones Públicas en España. Documentos Ocasionales Nº 1501. Banco de España. See also ARROYO DÍEZ E IRALA TIHISTA, El incumplimiento de la obligación de pago en operaciones comerciales, to be published by CIFE, July 2016.

The last stage was adopted through the Royal Decree-Law 8/2013, of 28 June, on urgent measures against late payment by public administrations and support for local entities with financial problems, which included due, liquid and enforceable obligations up to 31 May 2013. Following the previous model, Article 6 stipulated that "the debt is settled once the supplier is paid by the autonomous community or local entity, which includes principal, interest, court cost and other associated expenses". The Decree-Law wanted to make clear that whoever accepted this stage needed to know that once the principal was paid the supplier was waiving the right to interest, court costs and other expenses.

The aim of this Extraordinary Mechanism was to find an answer to the limitations on access to funding facing the Spanish public administrations and allow both local and regional authorities to make a credit transaction to settle the obligations incurred before 1 January 2012[3] and not paid off.

These different stages did not prevent several suppliers who accepted the payment system and received the principal from starting court proceedings to claim the interest to which they claimed they had the right according to the direct effect of the EU directives. Most of the judgments rejected such claims alleging that, following the system's internal rules, upon acceptance of the principal the supplier was voluntarily waiving the right to interest. Some of them, however, did recognize the right to interest as a consequence of the direct effect of the directives. This is the case of the Courts for Contentious Administrative Proceedings of Murcia and Valencia and the Court of First Instance No. 21 of Sevilla. They understood the waiver as acting against the EU Directives based on the supremacy of EU law and subsequent shift of the national law in favor of the EU law.

As said, the vast majority of the courts found that the Extraordinary Mechanism was not contrary to EU law on the grounds of: i) joining the Extraordinary Mechanism was voluntary, and ii) waiving the right to interest could not be considered grossly unfair to the creditor.

In view of this diversity of judgments, it was clear that an interpretation of the EU Directives was needed in order to specify their exact content and aim and give a

[3] During the third stage this was extended to the due, liquid and enforceable obligations incurred before 31 May 2013.

solution to the legal claims. The Court No. 6 of Murcia, at the request of the applicant, IOS Finance EFC SA, sought a preliminary ruling before the European Court of Justice as follows:

> *"Regard being had to Articles 4(1), 6 and 7(2) and (3) of [Directive 2011/7]:*
>
> *Must Article 7(2) of the directive be interpreted as meaning that a Member State may not make recovery of the principal debt conditional on the waiver of the right to interest for late payment?*
>
> *Must Article 7(3) of the directive be interpreted as meaning that a Member State may not make recovery of the principal debt conditional on the waiver of the right to compensation for recovery costs?*
>
> *Should the answer to those two questions be in the affirmative, where the debtor is a contracting authority, can it rely on the freedom of contract of the parties in order to avoid its obligation to pay interest for late payment and compensation for recovery costs?"*

Once the request for preliminary ruling was granted, arguments were presented by the legal representatives of the European Commission, the Spanish Government and the German Government.

In its written observations of 23 March 2015, the European Commission posed some questions on the transitional rights and concluded that the answers to both Directives would have the same results. After that, the Commission examined the substantive aspects of the case and concluded the following:

> *"The exhaustive effect of the obligation to pay interest for late payment upon payment of the principal derived from contracts with public administrations or contracting authorities in accordance with Article 6 of the Royal Decree-Law 4/2013 entails a restriction of the rights of the creditor and is contrary to the aim sought by Recital 19 of the Directive 2000/35/EC, as well as by Articles 3.1, 3.3, 3.4 and 6 notwithstanding the fact that access to the extraordinary mechanism is voluntary or requires previous request by the creditor.*

> *The exhaustive effect of the creditor's right to claim interest for late payment is equally contrary to the aim sought by Recital 12 of the Directive 2011/7/EU, and constitutes a breach of Articles 4.1, 7.2 and 7.12."*

The Commission had the same opinion regarding the exhaustive effect of the obligation to compensate for recovery costs and stated the following in Par. 73:

> *"The right to recover the principal, the interest for late payment and the compensation for recovery costs is recognized by EU law. It restricts the autonomy of the parties expressed through contractual terms and practices that are considered as grossly unfair or go beyond the limits of public order, thus entailing that a contracting authority shall not claim the enforceability of a grossly unfair term laying down a waiver of these rights in order to avoid payment. Likewise, the duty of the Member States to regulate these rights is contrary to a national law replacing the absence of such contractual term (prohibited by EU law) with a condition having equivalent effect but operating by law. Indeed, in addition to the fact that it is not neutral because it favors the defaulting debtor, it limits the rights recognized to the creditor by both Directives mentioned."*

The representatives of the German Government submitted their written observations on 25 March 2015. They made a clear difference between Articles 7.1 and 7.2 of the Directive 2011/7/EU inasmuch as, according to them, Article 7.2 establishes an irrefutable presumption that the term or practice that excludes interest for late payment is grossly unfair and shall be applied. Following this statement, the representatives analyzed if the Spanish legislation includes such a term or practice and if the waiver actually exists.

Concerning the first point, the German Government concluded that the concept of "practice" needs to be understood as "a uniform and long-lasting way to proceed that the contracting parties recognize as legally binding" and that the Spanish health authorities are following this practice through their supplier payment plans. As regards the existence of the waiver, the observations stated that "in the opinion of the German Government, there exists an exclusion of interest for late payment according to the literal sense of the words when the debtor introduces a contractual term or refers to a practice according to which no interest for late payment needs to be paid". This entails that the exclusion only exists if "the contracting parties, upon conclusion of the contract, agree that the practice carried out by the debtor of not paying interest will also be applied in the contract being concluded". As a consequence, "it cannot be deduced if the creditor's waiver of the right to interest after the conclusion of the contract is included in Article 7.2 of the Directive 2011/7/EU".

The last conclusion, if Article 7.2 is not applicable, refers to the applicability of Article 7.1. The national court will need to carry out a case-by-case analysis in order to ascertain if the term or practice is grossly unfair based on the principle of equality and the particular circumstances of the contract. Following the observations, "in order to assess if a term or practice is grossly unfair the judge will need to take into account all specific circumstances of the case that are against the creditor and jeopardize the protection awarded by the Directive through the promotion of a culture based on prompt payment".

Finally, the Spanish State Attorney submitted his observations on 27 March 2015. The State Attorney defended the Extraordinary Mechanism. It pointed out in particular that the EU Directives need to be construed in a way that they are not against the exclusion of interest for late payment and compensation for recovery costs when this is part of a special regime such as the Extraordinary Mechanism: established by law, alien to the contract, voluntary for suppliers, and when the supplier also has the option of starting court proceedings to claim the total amount of the debt, interest for late payment and compensation for recovery costs included.

After the hearing on 2 March 2016, Advocate General Sharpston delivered her opinion on 12 May 2016 and concluded that:

> *"In the light of all the foregoing considerations, I am of the opinion that the Court should answer the questions raised by the Juzgado Contencioso-Administrativo No 6, Murcia (Court for Contentious Administrative Proceedings No 6, Murcia, Spain) to the following effect:*
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> *– Directive 2000/35/EC of the European Parliament and of the Council of 29 June 2000 on combating late payment in commercial transactions, and in particular Article 3(3) thereof, and Directive 2011/7/EU of the European Parliament and of the Council of 16 February 2011 on combating late payment*

in commercial transactions, and in particular Article 7(2) and (3) thereof, should be interpreted as meaning that they do not preclude legislation under national law which:

(a) gives a creditor the right to subscribe to a scheme providing for 'accelerated' payment of the principal sum due under a contract to be made where the creditor has performed his obligations under the contract, subject to the condition that he waives entitlement to payment of interest for late payment and to compensation for recovery costs, whilst

(b) allowing the creditor to refuse to subscribe to such a scheme with the result that his entitlement to both interest and compensation will remain, albeit that it is likely that he will have to wait considerably longer to receive payment.

– *There is no need to answer the third question put by the referring court."*

In sum, the Advocate General's opinion was based on the fact that the Directives do not preclude Member States from setting a mechanism that allows suppliers to recover only the principal (she surprisingly describes the payment system as "accelerated" albeit being aware of the average figures of late supplier payment in Spain) while making the payment conditional on the waiver of the entitlement to interest for late payment as long as the waiver is voluntary and the supplier still maintains his right to payment of principal and interest, although with no guarantee of the time of payment[4].

Her main arguments were:

a. "Provided always that the right to await payment in full was real and not illusory, I cannot see that such an arrangement could be classified as 'grossly unfair' to the creditor" (Par.42).

b. "The Court has held that, although the terms on which a contract is entered into are in general characterised by the principle of freedom of contract, there may nonetheless be limitations on that principle arising from the application of rules under EU law. But for that reasoning to apply, EU law must first have intervened to restrict that freedom.

[4] The Advocate General made a difference between the Directive 2000/35/EC and the Directive 2011/7/EU as their enforcement depends on the date of conclusion of the contract. However, in her opinion of 12 May 2016 she stated that the enforceability depends on the national judge and that due to the similar content of both Directives they can be examined together.

While it may be observed that the effect of the directive was, through the provisions of Article 3(3), to impose a degree of restraint on the parties' freedom to contract as regards any failure on the debtor's part to make payment on the due date, in my view it did not do so as regards the situation described in point 41 above [when the creditor can opt for prompt payment or await payment in full]" (Par. 43).

c. "The financing mechanism introduced by Law 8/2013 gave the creditor a choice. He might subscribe to the mechanism, in which case he would be paid, if not forthwith, at least in early course. Alternatively, he could opt for the situation to continue as before". "Indeed, that element of choice — and the risks associated with it — seems to me to be a normal part of business life. Following the introduction of the financing mechanism, two alternatives were on offer. The first (subscribing to the mechanism) provided a lower degree of risk and a lower degree of reward. The second (opting to continue as before) offered greater risk but also the possibility of greater reward. I do not see that that type of situation was one which the directive was enacted in order to prevent" (Par. 44 and 45).

d. It makes no difference to the overall outcome if the debtor in the case was the original supplier of the goods or services or a factoring company (Par. 48 to 50).

e. First, Article 7(2) provides that, for the purposes of Article 7(1), a contractual term or a practice which excludes interest for late payment is to be considered as grossly unfair. While the expression 'contractual term' requires no explanation, the concept of a 'practice' may do. The term is not defined in the directive. It seems to me that it must be understood as something that has effect at the time the contract is entered into. By this I mean an arrangement which, although not expressly recorded or set out in the contract, nonetheless has binding force as between the parties, most usually as a result of a course of dealing between them or by reason of usage and custom in the particular trade or business concerned. That reflects the overall scheme and purpose of the relevant part of the legislation, which is to lay down rules governing the substantive effect of contracts entered into between parties who will typically be of unequal bargaining power. With a view to providing the necessary protection, Article 7(2) sets out rules as to payment and the consequences of late payment which, by definition, the parties are encouraged to incorporate within their contracts (the carrot) and which, should they not be so incorporated, are either to be treated as leading to unenforceability (or, in some cases, being capable of leading to unenforceability) or as giving rise to a claim for damages (the stick)” (Par. 57).

f. “There is in my view nothing in Directive 2011/7 which precludes a creditor from validly entering into a voluntary arrangement with the debtor, following performance of the contract by the creditor, whereby he is to receive immediate payment of the principal sum due under the contract in exchange for renouncing the claims to which he would otherwise be entitled in respect of late payment and to compensation for recovery costs. In particular, it seems to me that the provisions of such an arrangement do not represent a ‘contractual term or practice’ for the purposes of Article 7(1) to (3) of the directive nor, by extension, are they ‘grossly unfair’ for the reasons already set out in point 42 above. As regards the application of that directive to the case in the main proceedings, the observations I have set out in points 43 to 50 above regarding Directive 2000/35 are equally relevant to Directive 2011/7” (Par. 62).

III.- The answer to the preliminary ruling. Criteria to be applied

According to the background briefly set forth above, we believe that the correct resolution of the preliminary ruling in Case C-555/14 should take into account the considerations exposed here and conclude, against the Advocate General’s opinion, that the practice established by the Spanish Government through the different supplier payment plans is strongly opposed to the spirit and content of the EU Directives.

a. EU legal framework

The preliminary ruling was referred on the interpretation of the Directive 2011/7/EU. The question of the transitional provisions applicable to the case raised by the representatives of the European Commission makes no difference, and neither does the need to take into consideration the Directive 2000/35/EC. Firstly, because the transitional provision of the Royal Decree-Law 4/2013 does not concern the supplier payment mechanisms as it refers to the content of the public procurement contracts according to the late payment legislation, but not to the rules on the payment of accumulated debt. Secondly, as underlined by the Advocate General, this is a matter falling entirely within the jurisdiction of the national court and there is no point in analyzing this matter. Finally, the existence of a problem with the transitional provisions is equally irrelevant given the identity in substance of the 2000 and 2011 Directives on late payment. For this reason, no significant differences would arise from the analysis of the adequacy of the Royal Decree-Law 8/2013 to the EU Directives mentioned and the request for preliminary ruling is still valid.

In any case, given that the core subject of the request for preliminary ruling issued is the Directive 2011/7/EU, we will focus our analysis on this legal text.

b. Teleological interpretation of the Directive 2011/7/EU

Effectiveness is the key principle for the necessary teleological interpretation of EU law, that is, the interpretation technique aiming to achieve the objectives set by the legislator. As the ECJ has pointed out in several cases, the interpretation of the articles of the directives "must be considered in the light of the system established by the regulation and its aims" (see Judgment of 2 October 1991, Vandevenne and others, C-7/90, Page I-04371, Par. 6, and Judgment of 12 December 1996, Kontogeorgas, C-104/95, Page I-06643, Par. 25).

The aims of the 2000 and 2011 Directives on late payment can be found on the recitals, being their main aim the effective fight against late payment. The 2000 Directive makes a call to "ensure that the consequences of late payments are such as to discourage late payment" (Recital 16) in order to "prohibit abuse of freedom of contract to the disadvantage of the creditor" (Recital 19). The 2011 Directive recognizes that late payment "constitutes a breach of contract which has been made financially attractive to debtors" and, as a consequence, "a decisive shift to a culture of prompt payment, including one in which the exclusion of the right to charge interest should always be considered to be a grossly unfair contractual term or practice, is necessary to reverse this trend and to discourage late payment" (Recital 12). It is also stated that the "exclusion of the right to charge interest should always be considered to be a grossly unfair contractual term or practice" while the "exclusion of the right to compensation for recovery costs should be presumed to be grossly unfair".

These recitals send two very clear messages. The Directives' aim is the effective fight against late payment and one of the mechanisms to achieve this is the prohibition to exclude the right to interest, as this always constitutes a grossly unfair contractual term or practice. Such a pact does not fall within the free choice of the parties of a commercial agreement.

Consequently, the Directive needs to be interpreted as prohibiting under any circumstance any contractual term or practice allowing the suppression of the right to interest. If this depended on the free will of the parties, it is obvious that the debtor would always delay payments with the aim to demand the waiver of the right to interest in exchange for the recovery of the principal when the creditor were in a difficult financial situation. In fact, this waiver will never be voluntary even if it formally appears as such. The opportunity to claim the right to interest in a slower process and without any guarantee of the time of payment of the principal and interest does not constitute a real alternative to the recovery of the principal while waiving the recovery of the interest.

No-one suffering from financial pressure is in a position to choose. To accept recovering the principal while waiving the right to interest is the only possible option. For this reason, by admitting that the waiver of the right to interest falls within the free will of the parties, the Directive's aim will lose its meaning. The fight against late payment will cease to exist and debtors with a dominant position, and public administrations always have a dominant position, will always be able to buy low and delay payments until they decide to offer the payment of the principal in exchange for the waiver of the right to interest to a creditor who is no longer in a position to choose because their serious financial problems push him to accept the payment of the principal without interest. This will entail in practice that debtors will never need to assume the interest for late payment.

It must be finally remembered that the ECJ (more specifically the previous one) has set forth that the provisions laying down substantive or procedural rights of individuals (in this case, the right to interest) shall not be construed in a restrictive manner. Accordingly, the silence or lack of clarity of a legal text affecting individual rights (which is not the case in the analyzed Directives) should not be interpreted as detrimental to them (25/62 Plaumann v. Commission (1963) ECR 95, p. 107; 8 to 11/66

Cimenteries v. Commission ECR 75, p. 92; 140/73 Mancuso (1973) ECR 1449, p. 1456; 66/74 Farrauto (1975) ECR 157 p. 161-2; 32/75 Cristini (1975) ECR 1085, p. 1094-5; 104/76 Jansen (1977) ECR 829, p. 842).

c. Literal interpretation of Articles 7.1 and 7.2 of the Directive 2011/7/EU

Article 7 of the 2011 Directive lays down that:

> "*1. Member States shall provide that a contractual term or a practice relating to the date or period for payment, the rate of interest for late payment or the compensation for recovery costs is either unenforceable or gives rise to a claim for damages if it is grossly unfair to the creditor.*
>
> *In determining whether a contractual term or a practice is grossly unfair to the creditor, within the meaning of the first subparagraph, all circumstances of the case shall be considered, including:*
>
> *(a) any gross deviation from good commercial practice, contrary to good faith and fair dealing;*
> *(b) the nature of the product or the service; and*
> *(c) whether the debtor has any objective reason to deviate from the statutory rate of interest for late payment, from the payment period as referred to in Article 3(5), point (a) of Article 4(3), Article 4(4) and Article 4(6) or from the fixed sum as referred to in Article 6(1).*
>
> *2. For the purpose of paragraph 1, a contractual term or a practice which excludes interest for late payment shall be considered as grossly unfair."*

The first paragraph of this provision establishes that Member States shall declare unenforceable any grossly unfair contractual term or practice based on the date or period for payment, the rate of interest for late payment or the compensation for recovery costs. It also adds several general criteria for the determination of grossly unfair contractual terms or practices.

The second paragraph lays down that all contractual terms or practices that aim to exclude the right to interest for late payment will be considered grossly unfair and shall be prohibited or deemed unenforceable. Therefore, no analysis of the contractual term or practice will be needed in order to determine if it is grossly unfair or not. And, following this, the exclusion of interest for late payment imposed by the Spanish legislation through the special supplier payment plans is grossly unfair and contrary to the Directive. The difference between the first and second paragraph of Article 7 is decisive for the interpretation of the meaning of the Directive, that is, the aim sought by the Directive.

This conclusion derives in our opinion from a literal interpretation of the Directive that does not require a special effort (in claris non fit interpretatio). Some voices have risen against this conclusion; however, we do not share their arguments.

c.1. It is not true that the prohibited practices must have been laid down in the contract

For the representatives of the German Government, the expressions "contractual terms or practices" in Article 7.2 are to be understood as contractual terms or practices ("practice" meaning a uniform and long-lasting way to proceed) that need to be established or recognized in the contract laying down the legal transaction between creditor and debtor. As, in our case, the practice imposing the waiver took place after conclusion of the contract, Article 7.2 is not applicable. This Article would have been enforceable had the parties, upon contract conclusion, agreed that the practice of the debtor of not paying interest was also applicable to the contract at issue. This, but not a practice subsequent to the contract conclusion, is prohibited. The German representatives were aware of the weakness of their arguments and concluded ambiguously that "it cannot be easily deduced if the creditor's waiver of the right to interest for late payment subsequent to the contract conclusion falls within the scope of Article 7.2 of the Directive 2011/7/EU".

Similar arguments submitted but the Advocate General cannot be accepted either. For the Advocate General, Article 7.2 of the Directive 2011/7/EU makes a difference between "contractual term" and "practice" excluding interest for late payment: "while the expression 'contractual term' requires no explanation, the concept of a 'practice' may do. The term is not defined in the directive. It seems to me that it must be understood as something that has effect at the time the contract is entered into. By this I mean an arrangement which, although not expressly recorded or set out in the contract, nonetheless has binding force as between the parties, most usually as a result of a course of dealing between them or by reason of usage and custom in the particular trade or business concerned. That reflects the overall scheme and purpose of the relevant part of the legislation, which is to lay down rules governing the substantive effect of contracts entered into between parties who will typically be of unequal bargaining power. With a view to providing the necessary protection, Article 7(2) sets out rules as to payment and the consequences of late payment which, by definition, the parties are encouraged to incorporate within their contracts".

The Advocate General coincided with the representatives of the German Government and focused her argument on the requisite that the contractual term or practice must be specified in the contract.

In our opinion, Article 7.2 is fully applicable in the case of the Spanish legislation on supplier payment. It is true that the supplier payment system cannot be understood as a contractual term (although a contractual agreement accepting the payment of the principal and the waiver of the right to interest does indeed exist) in the sense of Article 7.2 of the Directive. It is not a contractual term inasmuch as there is no formal agreement in the contract between creditor and debtor which gives rise to the interest for late payment. However, it is a practice, that is, a set of rules of conduct imposed subsequent to the contract as a practice through which the creditor accepts recovery of the principal while waiving the right to interest. And the Directive does not state that the practice must be incorporated in the contract.

Secondly, the teleological interpretation and the principle that the provisions laying down substantive rights of individuals (in this case, the right to interest) shall not be construed in a restrictive manner lead us to conclude that Article 7.2 is directly enforceable in the case at issue. It is inasmuch as the Spanish supplier payment mechanisms constitute a practice that excludes interest for late payment and, consequently, it is a grossly unfair practice directly prohibited by the Directive. Furthermore, this practice, upon acceptance, renders the content and aim of the Directive, as well as the effective fight against late payment, meaningless.

We do not share the statement that the only thing prohibited by the Directive is that "the parties, upon contract conclusion, agree[d] that the practice of the debtor of not paying interest [will be] also applicable to the contract at issue" (statement shared by the German representatives although with some doubts).

When the 2011 Directive added the term "practice" next to "contractual term", it aimed to cover the acts subsequent to the contract carried out by the debtors, and in particular by the public administrations, and targeted at excluding interest for late payment. Creditors cannot prevent public administrations from using their legislative power after the conclusion of a contract in order to establish a practice that is against the payment of interest. And this is precisely why the Directive includes a specific mention of the practices, which might be subsequent to the contract and which, if they exclude interest for late payment, will be considered as grossly unfair and contrary to the Directive.

c.2. It is not true that the supplier payment system recognizes the freedom to make contractual arrangements to the extent that it cannot give rise to grossly unfair contractual terms or practices. The waiver of the right to interest does not fall within the free choice of the parties

Both the Spanish representative and the Advocate General maintain that the supplier payment practice is not contrary to the Directive considering that creditors can choose to accept or not the proposed system and may still claim the right to interest through a slower and uncertain procedure for the recovery of both principal and interest.

The Advocate General sharply states that "provided always that the right to await payment in full was real and not illusory, I cannot see that such an arrangement could be classified as 'grossly unfair' to the creditor". In the same vein, the Spanish representative expresses that the supplier payment mechanism created by the Spanish Government allows the creditor to voluntarily renounce resorting to the mechanism and start legal proceedings to recover the totality of the debt, including both interest for late payment and compensation for recovery costs. This thesis is also supported by the German representatives. These add as well that "it is a matter of legitimate interest for the creditor, in case of late payment, to waive the right to interest in order to, at least, receive prompt payment of the principal". And they conclude that "the parties are subject to what they agreed upon. As a consequence, the risk that the debtor might abuse the freedom of contract to demand contractual privileges does no longer exist. It must be expected that the creditor will only waive the right to interest subsequent to the contract conclusion if this is favorable to their interests".

It is now important to underline that, in order to analyze the conformity of the Spanish Government's practices with the 2000 and 2011 Directives, it is not necessary to examine if creditors are actually willing to proceed this way, which might depend on the financial situation of each of them and on how long they need to wait for the recovery of the amount. In any case, it is true that many companies disappeared due to late payments and many others were not in a position to renounce the principal without the risk of disappearing.

When interpreting the content of the Directives it should not be neglected that these have expressly excluded this possible agreement from the free will of the parties, since the legislation of the possible waiver of the right to interest by national law is in any case prohibited. As has already been mentioned, any agreement on the waiver of the right to interest is prohibited with the aim to set up an effective system to fight against late payment. At the time of legislation it was known that, if debtors with a dominant position were given this possibility (and public administrations always have a dominant position), they would always be able to impose this waiver on the creditors. It suffices to not pay, place the creditor in an untenable financial situation and then offer him the payment of principal with waiver of the right to interest.

Leaving the waiver of the right to interest out of the scope of the free will of the parties entails that neither the debtor nor the creditor can negotiate this waiver in the framework of their contract. This is what Article 7.2 of the Directive aimed for. There is no need to examine if it is a grossly unfair contractual term or resort to the Council Directive 93/13/EEC of 5 April 1993 on unfair terms in consumer contracts to be able to conclude that the waiver of the right to interest required by the debtor is a grossly unfair contractual term. The contractual term is grossly unfair under any circumstance pursuant to the Directive. The alleged free will in the acceptation of the waiver does not give effect to this point of the agreement. As stated above, the waiver is contrary to law and falls outside the scope of the free will of the parties.

At this point we should examine if a directive can restrict the free will of the parties in the context of their trade relations. In fact, there is no obstacle to a directive limiting the freedom of contract in commercial transactions if with this action it pursues an aim of general interest that guarantees the proper functioning of the internal market. The ECJ has recognized this point in several judgments, amongst which that of case C-434/08 (judgment of 20 May 2010, A. Tizzano being the President of the Chamber):

> "*(36) First, it must be borne in mind that, although a contract is characterised by the principle of freedom of the parties to arrange their own affairs, according to which, in particular, parties are free to enter into obligations with each other,* ***limitations on freedom of contract may none the less arise from the applicable European Union rules*** *(see, to that effect, Case C‑240/97 Spain v Commission [1999] ECR I‑6571, paragraph 99)."*

Let us now analyze the Judgment of the Court of 5 October 1999 in case C-240/97 brought up by the previous Judgment (to which Spain was party). Paragraph 99 stated that:

> *"(99). It must be observed, first of all, that the right of parties to amend contracts concluded by them is based on the principle of contractual freedom and* ***cannot, therefore, be limited in the absence of Community rules imposing specific restrictions in that regard****."*

The European Court of Justice has also taken a stand concerning Articles 1 to 3 of the Directive 2000/35/EC. The Judgment of 24 May 2012 in case C-97/11 established in this regard that:

> *"(36) […]* ***it is necessary to point out that Article 3 of that directive provides that the Member States are to ensure that interest is payable in the case of late payment*** *and may be claimed by the creditor if he has fulfilled his contractual and legal obligations and has not received the amount due on time, unless the debtor is not responsible for that delay.*
>
> *(37)* ***This obligation which is imposed on Member States is unconditional and sufficiently precise to have direct effect*** *[…].*
>
> *(38) Since Article 10 of Directive 1999/31 and Articles 1 to 3 of Directive 2000/35* ***have direct effect, they are binding on all the authorities of the Member States****, that is to say, not merely the national courts but also all*

> *administrative bodies, including decentralised authorities,* ***and those authorities are required to apply them*** *(see, to that effect, Case 103/88 Costanzo [1989] ECR 1839, paragraphs 30 to 33 and Case C‑243/09 Fuß [2010] ECR I‑9849, paragraph 61 and the case‑law cited).”*

These Judgments are two of the many judgments that recognize a crucial aspect of this case: **the autonomy of the parties has its limits and these must be established by EU law**. In our case, this limitation is laid down by the 2000 and 2011 Directives and the national legislator has the obligation to apply it in the national legislation as a decisive action to achieve the effectiveness of the aim laid down by the Directives.

Indeed, the EU legislator wanted to state this limitation in a clear manner in the 2000 and 2011 Directives. The text of the 2000 Directive stipulates that this “should prohibit abuse of freedom of contract to the disadvantage of the creditor” (Recital 19). The Directive 2011/7/EU is very precise as well in imposing the limits to the exclusion of the right to interest. Recital 12 states that “the exclusion of the right to charge interest should always be considered to be a grossly unfair contractual term or practice”. In addition, Recital 28 lays down that “the outright exclusion of the right to charge interest should always be considered as grossly unfair”.

Therefore, the waiver of the right to interest cannot be either expressly or tacitly agreed upon by the parties, as such a pact does not fall within the scope of the autonomy of the parties.

<u>c.3. The national law implementing the Directives should have established transitional rules on the temporary non-application of these, but in Spain no provision was adopted in this regard.</u>

The Judgment of the ECJ of 26 February 2015 in case C-104/14 establishes that “it must be held that, by its second to fifth questions which should be examined together and in the first place, the referring court asks whether the third paragraph of Article 288 TFEU and Articles 3(3) and 6 of Directive 2000/35 and Articles 7 and 12 of Directive 2011/7 must be interpreted as precluding a Member State, which made use of the option under Article 6(3)(b) of Directive 2000/35, from adopting, during the period prescribed for transposition of Directive 2011/7, legislative provisions, such as those at issue in the main proceedings, which are capable of modifying, to the detriment of a creditor of the State, the interest on a debt arising out of the performance of a contract concluded before 8 August 2002" (Par. 30).

This allows us to conclude, to the contrary, that the modification of the Directives to the detriment of a creditor can only be established if the Member State made use of the options proposed by the same Directives and in the way proposed. No other exception to the Directive, such as allowing the exclusion of the right to interest, is possible.

d. Systematic interpretation. The obligations of the Member States

As previously stated, the aim of the 2011 Directive is to strengthen the fight against late payment in order to achieve the correct functioning of the commercial transactions within the EU single market. To this end, it requires the Member States to adopt a set of positive measures (Articles 3, 4 and 10) and lays down several prohibitions (Article 7), amongst which the exclusion of the right to interest.

The different articles of the Directive oblige the Member States to achieve the proper functioning of the internal market through the fight against late payment. This means preventing the existence of grossly unfair contractual terms or practices in commercial transactions between companies, but more intensely it means prohibiting Member States from adopting laws that lay down grossly unfair practices favoring public debtors to the detriment of private creditors. Member States have the obligation to achieve specific results: they need to adopt all necessary measures so that grossly unfair contractual terms or practices on interest are not enforced or, at least, give rise to a claim for damages.

Consequently, the fact that a Member State has created a practice contrary to the norms and the spirit of the Directives is a particularly serious matter. As mentioned by the representatives of the Commission in their written observations, "the duty of the Member States to regulate these rights is contrary to a national law replacing the absence of such contractual term (prohibited by EU law) with a condition having equivalent effect but operating by law. Indeed, in addition to the fact that it is not neutral because it favors the defaulting debtor, it limits the rights recognized to the creditor by both Directives mentioned” (Par. 73).

e. The Royal Decree-Law 8/2013 does not entail the participation of a third party who is not affected by the Directive 2011/7/EU

The argument of the Spanish representative must also be rejected. In particular Paragraph 37, according to which the practice established by the Royal Decree-Law 8/2013 implies, from a material perspective, the participation of a third party who is alien to the contract, in this case, the Spanish public administration.

The reasons for not defending this argument are the following. As seen above, the Directive 201177/EU imposes positive measures and prohibitions addressed to the Member States. Amongst the prohibitions are the practices involving grossly unfair measures against the rights of the creditors. This means that the public administration is not a third party alien to the problem but the main party involved in the enforcement of the law. Member States are, according to EU law, the main responsible for the fight against late payment. Unfortunately, in Spain, the adoption of such a practice entails a performance carried out by the State that is contrary to the Directives. The State has played a prominent role in the promotion of late payment inasmuch as it has clearly fostered the waiver by the creditors of the right to interest for late payment in order to recover the principal. This has in turn favored the debtor public administrations and coerced the creditors.

IV.- Conclusions

The previous considerations lead us to conclude that the supplier payment mechanisms created by the Spanish Government with the aim to pay off the debt of the local and regional public administrations are contrary to the 2000 and 2011 Directives on late payment. They are contrary to the Directives because they *imperatively* lay down that accepting the payment of the principal implies waiving the recovery of the interest, the compensation for recovery costs and other amounts accrued in favor of the creditor.

The EU Directives aim at fighting late payment. To achieve greater efficiency the legislator has expressly determined that the exclusion of the right to interest will not fall within the scope of the autonomy of the parties. Such a contractual term or practice is in all events grossly unfair and clearly against the EU law. There is no need to analyze the specific case, nor the typology of the possible creditors, the amount due or the delay. Article 7.2 of the 2011 Directive is clear and precise when laying down that "a contractual term or a practice which excludes interest for late payment shall be considered as grossly unfair". As a consequence, any national law establishing a practice that contains this waiver of the right to interest is contrary to the Directive.

The spirit and letter of the law being so clear, they cannot be contradicted by a Spanish system allowing the creditor to opt to claim principal and interest through court proceedings at a second stage. This possible incorporation of the free will of the parties regarding the waiver of the right to interest is precisely what the Directive prohibits, thus turning this prohibition into a structural element of the aim sought by the Directive. In other words, if the waiver of the right to interest was allowed, the debtor with a dominant position (and the public administration always has a dominant position) could always delay their payments for as long as wanted to provoke the creditor's serious financial problems and then offer the creditor a false voluntary waiver of the right to interest. The European Commission, fully aware of this possibility posing a permanent threat, drafted the 2011 Directive in the clear terms exposed above. Recognizing the conformity of the Spanish practice to the Directive would, in our view, render the Directive meaningless and useless.

In addition, the meaning of "prohibited contractual terms and practices" of the 2011 Directive does not exclusively refer to actions included in the contract between creditor and debtor. By adding the term "practices" the Directive aimed to include all actions subsequent to the contract, this is to say, all actions carried out by the debtor in order to avoid their obligations to pay interest. The teleological interpretation of the Directive requires in any case a broad interpretation of the prohibition of any clause allowing for the waiver of the right to interest.

We believe that the answer to the questions referred should be as follows. Regarding the first question, "Article 7.2 of the Directive must be interpreted as meaning that a Member State may not make recovery of the principal debt conditional on the waiver of the right to interest for late payment". The second question should be answered like this: "Article 7.3 of the Directive must be interpreted as meaning that a Member State may not make recovery of the principal debt conditional on the waiver of the right to compensation for recovery costs". Finally, concerning the third question, "the Directive 2011/7/EU fully applies to national contracting authorities. This means that, where the debtor is a contracting authority, it shall not rely on the freedom of contract of the parties in order to avoid its obligation to pay interest for late payment and compensation for recovery costs". We look forward to the answer of the Court.