

## **Late payment penalties and capitalization of interest**

**In a judgment dated November 10, 2015, the *Cour de Cassation* (French Supreme Court) confirmed that late penalties provided for under Article L. 441-6 of the French Commercial Code are to be considered as default interest.**

**As such, these penalties can bear interest, as per Article 1154 of the French Civil Code.**

Article L. 441-6 of the French Commercial Code - that determines the content of the general terms of sale and the maximum payment terms - stipulates *inter alia* that the terms and conditions of payment must specify the interest rate that will be applied to calculate late penalties that become due after the payment due date set forth in the invoice as well as the conditions in which such late penalties will be applied.

These penalties are calculated on the basis of the interest rate applied by the European Central Bank to its most recent main refinancing operation plus ten percentage points, unless expressly stipulated otherwise by the parties. Yet, late penalties may not be calculated at a rate that is less than three times the legal interest rate.

The issue at stake in the commented decision<sup>[1]</sup> was to know whether the late penalties provided for under Article L. 441-6 of the French Commercial Code can bear interest as per Article 1154 of the French Civil Code.

It should be recalled that the capitalization of interest provided for under Article 1154 of the French Civil Code and that applies to contractual interest and legal interest (or default interest) means that the interest due on capital can itself bear interest (it being specified that such capitalization is permitted only if interest is due for at least one year).

In the commented case, a supplier, arguing that a buyer had failed to pay the invoice, obtained from the court a payment order that was challenged by the buyer. The appellate judges granted the supplier's payment claim and held that the late penalties of 10.65 % and 10.38 % per year (based on the interest rates applicable in 2010 and 2011, plus ten percentage points) were to bear interest as per Article 1154 of the French Civil Code<sup>[2]</sup>.

The buyer appealed before the *Cour de Cassation* and argued that the trial judges had erred in holding that the penalty provided for under Article L. 441-6 of the French Commercial Code ought to bear interest because, according to him, such penalty was not to be considered as default interest and, as a result, the provisions set forth in Article 1154 of the French Civil Code could not apply in this case.

In its decision dated November 10, 2015, the *Cour de Cassation* upheld the judgment of the Court of Appeals and expressly stated that “*as the late penalty provided for under Article L. 441-6 of the French Commercial Code is to be considered as default interest, the Court of Appeals was entitled to order the capitalization of interest as per Article 1154 of the French Civil Code*”, in accordance with the supplier’s claim.

It follows from this decision that the late penalties provided for by Article L. 441-6 of the French Commercial Code are to be considered as default interest and may be capitalized.

However, it should be underlined that the *Cour de Cassation*, relying on the provisions set forth in Article L. 441-6 of the French Commercial Code, invalidated the part of the appellate judgment that had ordered the buyer to pay late penalties effective as from July 9, 2010 “*after having noted that the wood panels - that formed the subject-matter of the disputed invoices - had been ordered in April 2010 and delivered in July 2010*”.

The *Cour de Cassation* criticized the Court of Appeals for ruling so “*without noting that the general terms applicable between the parties or an agreement signed by the professional organizations of the relevant industry had granted an exception to the thirty-day payment term provided for under the aforementioned Article*”. According to the *Cour de Cassation*, the trial judges should indeed have determined whether the 30-day payment term that, in principle, applies as from the delivery of the products, had not been set aside by specific provisions agreed upon between the parties or by a professional agreement, as provided for under Article L. 441-6 of the French Commercial Code.

[1] Commercial Chamber of the *Cour de Cassation*, November 10, 2015, n°14-15.968

[2] Court of Appeals of Nancy, November 27, 2013, n°12/02367

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