

Tax treatment of interest and compensation paid under S.I. No. 580 of 2012 European Communities (Late Payment in Commercial Transactions) Regulations 2012

1. General

This article sets out the tax treatment of interest and compensation paid under [*S.I. No. 580 of 2012 European Communities \(Late Payment in Commercial Transactions\) Regulations 2012*](#) (the “2012 Regulations”). The tax treatment of interest and compensation payments made under [*S.I. No. 388 of 2002 European Communities \(Late Payment in Commercial Transactions\) Regulations 2002*](#) (the “2002 Regulations”) was outlined in Tax Briefing, Issue 52 (May 2003).

With effect from 13 March 2013, the 2002 Regulations were repealed by the 2012 Regulations. The 2012 Regulations give effect to Directive 2011/7/EC of the European Parliament and of the Council of 23 February 2011 on combating late payment in commercial transactions. The 2012 Regulations apply with effect from 16 March 2013, with some exceptions, to commercial transactions in both the public and private sectors. Many features of the 2012 Regulations are similar to existing provisions in the 2002 Regulations. As a transitional measure, the 2002 Regulations continue to apply to a contract which was made prior to, and is still in force after, the coming into operation of the 2012 Regulations

The 2012 Regulations provide that interest shall be payable in respect of a late payment and that it will be an implied term of every contract that interest is payable if debts are not paid on time. A payment is regarded as late when 30 days have elapsed unless an alternative payment period is specified in an agreed contract. The interest chargeable for late payment is the European Central Bank main refinancing rate plus eight percentage points unless otherwise agreed.

The 2012 Regulations also provide that where late payment interest falls due in respect of a payment, in addition to this amount, the supplier is also automatically entitled to compensation for debt recovery costs. Suppliers are entitled to charge a minimum of €40 in relation to expenses incurred as a result of the late payment and may also be able to claim any reasonable recovery costs incurred. Like the late payment interest, compensation is an implied term of every “commercial transaction”, i.e., it forms part of the terms of the contract itself and is not in addition to the contract.

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2.1 VAT

The statutory late payment interest received in accordance with Regulation 4 of the 2012 Regulations is not regarded as consideration for VAT purposes.

Any such payment collected by a taxable person due to the late payment of the purchaser's account does not represent consideration for a taxable supply and is therefore outside the scope of VAT.

2.2 *Income Tax/Corporation Tax*

The interest is regarded as a trade expense, which is tax deductible in computing the profits of the person making the payment (i.e., the purchaser) provided the payment for the goods/services, on foot of which the interest payment is made, was incurred wholly and exclusively for the purpose of the purchaser's trade/profession. The interest is taxable in the hands of the recipient (i.e., the supplier). Although strictly chargeable under Case III of Schedule D, it may be included as a trade receipt and accordingly assessed under Schedule D Case I.

2.3 *Professional Services Withholding Tax (PSWT)*

Where interest is paid in accordance with Regulation 4 of the 2012 Regulations on foot of payments, which are payments for professional services, within the meaning of *Section 520 TCA 1997*, PSWT should **be deducted** from the interest. When completing Forms F45 for issue to specified persons (i.e., suppliers), accountable persons should include interest amounts.

2.4 *Relevant Contracts Tax*

Where interest is paid in accordance with Regulation 4 of the 2012 Regulations on foot of payments, which are payments to subcontractors in certain industries, within the meaning of *Section 530 TCA 1997*, RCT should be deducted from the interest. When submitting payment notifications regarding relevant payments to be made to sub-contractors, principal contractors should include interest amounts.

2.5 *Withholding tax on interest payments by companies and to non-residents*

Interest paid under the 2012 Regulations is not yearly interest. Accordingly, *Section 246 TCA 1997* does not apply where penalty interest is paid.

Tax treatment of compensation paid under [S.I. No. 580 of 2012](#)

The tax treatment of compensation paid under the 2012 Regulations is the same as interest paid under the Regulations as outlined above, with the exception that the issue of the application of *Section 246 TCA, 1997* does not arise.

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