



Munich Personal RePEc Archive

A model for removing blockades in the payment turnover

Nenovski, Tome

Faculty of Economics-Skopje

November 2011

Online at <https://mpra.ub.uni-muenchen.de/42250/>

MPRA Paper No. 42250, posted 24 Feb 2013 06:39 UTC

International Conference: "Finance and Monetary Policy after the Global Financial Crisis, Ekonomski fakultet Skopje, 18 November, 2011, Skopje;

Tome Nenovski, PhD
University American College Skopje
nenovski@uacs.edu.mk

A MODEL FOR REMOVING BLOCKADES IN THE PAYMENT TURNOVER

ABSTRACT

In the past 5-6 years a strong reform orientation of the Republic of Macedonia (RM) to improve the business climate in the country has been present. However, the economic/legal system of the Republic still has many weaknesses and limitations that does not allow the economical entities to smoothly carry out their activities and even limits their achievement of significant business results. In particular, they are manifested by the difficulties in the collection of claims. Very effective solution for overcoming the problems of (non)payment of obligations is to establish a system of automatic payment of liabilities (SAP). The basis for the introduction of this system is the introduction of a new instrument for payment or securing of payments in the RM – *a debit note*. It would be an instrument which is issued by the debtor at the request of the creditor in order to regulate their mutual debtor-creditor relations. The underlying logic of this instrument is the possibility to realize and/or guarantee payment of debt. It carries out the role of an off-court settlement instrument between the parties. The establishment and proper functioning of SAP would mean a kind of revolution in payment. It will increase mutual trust between the economic entities, as a result of which Macedonia will become a reliable and secure destination for the funds of investors.

Key words: *business climate, blockades, payment turnover; system for automatic payment, a debit note*

JEL CLASSIFICATION CODES:

Introduction

In the last few years, the Republic of Macedonia (RM) has been getting high appraisal by the World Bank project “Doing business”. It has been regularly ranked among the first ten countries in the world according to the strengths of the reforms needed for “doing business”, and among the first thirty countries in the world according to the working conditions of the economic subjects. These indicators refer to the country’s high commitment to reforms towards improving the business atmosphere in the country.

Certainly, these recognitions should not make us self-satisfied and we shouldn’t expect the economic situation to improve only as a result of the already made reforms in the separate segments. The economic-legal system of the RM still has many weaknesses and limitations which do not allow the economic subjects to perform their activities without any obstacles; as a matter of fact, they even constrain them in achieving more significant business results.

1. Regular limitations of the payment turnover

Among the many weaknesses of the economic-legal system, it is the financial indiscipline of the economic subjects that stands out with its limiting capacity, or the most common manifestations are connected with the difficulties in charging the demands, and with the slow insolvency procedures connected with the weaknesses in judiciary.

a. Due to the influence of the world economic crisis and the limiting character of the monetary and fiscal policy, most of the firms in the RM are facing the problem of non-liquidity. This problem is multiplied by the growing financial indiscipline of most of them (AMCC, 2011).

It is becoming more common that some companies do not pay their liabilities towards other companies because they are not liquid themselves, or they expect the country to take their liabilities over. That is additionally aided by the still actual payment with settling accounts (cessions, compensations, deposit forms, etc.), which enables some firms to evade efficient paying of the due debts to their creditors, even towards the country. Thus, there is a case when firms don’t pay their liabilities to other firms or to

the country. On the other hand, it is very common that the Government (due to the fiscal limitations) does not pay on time its own liabilities to the firms (Nenovski, 2010). That leads to increasing the non-liquidity of the economic subjects, blocking their mutual effective payments, stopping their more intensive economic effort, decreasing mutual trust, avoiding partners for cooperation, etc. Finally, this practice, in a rather very unreal way, increases the internal (domestic) debt in the country and hinders its economic growth.

b. It is very common (Nenovski, 2006) that some company owners consciously prolong the payment of their liabilities to the creditors, and in the meantime, they lead their own company (debtor) to insolvency. Despite the increased efficiency of the insolvency cases in the previous few years, unfortunately, this process still has serious weaknesses. On one hand, the time for announcing insolvency has to be prolonged, so that, in the meantime, the company owner takes the most part of the available means of that firm, and after balancing the insolvency means of the company in the process of insolvency there is nothing or very little for the creditors regarding their demand from that company. Or the insolvency lasts impermissibly long, in which period the available resources of the firm start to decrease, while the value of the creditor's demand is diminished, even if they manage to pay it out by distributing the debtor's insolvency means.

2. System for automatic payment of the liabilities - SAP

Establishing a system for automatic payment of the liabilities (Nenovski, 2010) is a very efficient solution to the payment/non-payment of the liabilities. Its simple essence comes down to the following: after the mutually agreed time limit for paying the invoice has passed, the clearing house or special agency for charging the demands (in the following text: Agency) would give an order to the debtor's bank to automatically take the corresponding amount from the available means of the debtor's transaction accounts, and to transfer it to the creditor's account without giving any previous warnings to the debtor. The possible delay of the payment could be made only on the basis of written consent made in advance between both parties.

The time limit given for paying the liabilities should be in accordance with the rules of the European Union and be at most thirty days¹ for the companies and citizens' liabilities, or forty five days² for the Government's liabilities since the day the invoice has

¹ In June 2000, EU carried out a Directive on combating late payment in commercial transactions. In October 2010 modifications and amendments in the Directive were made, according to which invoices in the public and private sector must be paid in mostly 30 days.

² As exception, the final date for paying EU public institutions (public health and so on) may be prolonged up to mostly 60 days.

been delivered. If it hasn't been agreed for the previously determined time limit to be extended, which should not exceed thirty days, the bank will automatically transfer the amount from the debtor's account to the creditor's account. If there is no means on the debtor's account or it is unlikely that there will be influx in the next fifteen days, the account will be blocked and an insolvency procedure will be started against the debtor in a way that is explained in the text below.

2.1. Introducing a new instrument for paying and ensuring payment – A debit note

The basis for introducing a system for automatic liabilities payment is introducing an appropriate (new) instrument for paying or ensuring the payment in the payment turnover in the RM, and that is a debit note (Enforcement Law, 2010). This would be an instrument issued by the debtor upon the creditor's request, in order to regulate their mutual debtor-creditor relations. The debit note would be a kind of security whose function should be regulated by the Contract law in a similar way to the one that regulates the existence and function of the cheque and the bill of exchange as paying instruments. As can be seen in the explication given below, the debit note has certain similarities to the bill of exchange. However, since the debit note can expand the scope of the debtor's assets (property) which can be used for paying the liabilities to the creditor, the debit note would get bigger responsibilities and possibilities for its practical use than the bill of exchange.

The basic feature of the debit note is to realize or guarantee paying a debt. By issuing it, the debtor obliges himself that the debt the note refers to shall be paid in accordance with the terms stipulated in the note. Hence, in its issuing the debtor admits that he owes and obliges that he will pay the debt according to the terms in the document. This is where the suggested name of this financial document comes from – a debit note. Its form, structure and way of usage should be regulated in detail with a specific bylaw or a manual from the Ministry of Justice or the Ministry of Finance.

The following would give a short description of the way this financial document should be used:

Let's suppose that on the basis of mutual stock-financial relations, the debtor 'M' owes to the creditor 'N' 1.000.000 denars. In order to be protected in case of possible non-payment or delayed liability payment by the debtor, the creditor wants the debtor to issue a debit note to him as a guarantee that the payment will be made in the agreed time period. If the debtor accepts this, then he will issue such a note. For the creditor to be convinced in the debtor's financial potential before agreeing to accept a debit note, he should have the opportunity to conduct an inspection in the public documents about the debtor's financial situation at the Central Register of the RM.

The note will basically have the following elements (Regulation..., 2010): name, address, and tax number of the debtor's company, debtor's consent with the content of the note; name, address, and tax number of the creditor's company; a sum of the debtor's debt; the ground for the debt; the time limit (the shortest and/or the longest) for paying the liabilities (the debt); interest rate (regular and/or punitive) that the debtor would pay to the creditor if there is delay in his paying the liability, a name of at least one of the banks where the debtor has a transaction account; a name of the bank where the creditor has a transaction account; the debtor's consent that the specified amount shall be paid from any of his transaction accounts in any bank in the RM; a debtor's consent saying that if there is no means or its influx until the agreed time limit for payment of the liabilities, the creditor can use the note as an executive document for collecting the debt from the total assets of the debtor by engaging an executor of the creditor's own choice; a debtor's consent giving right to the creditor to endorse the note to a third party within the agreed time limit for payment of the debt, etc.

If the debtor pays his liabilities within the time limit marked on the note, the note expires and becomes invalid. If the debtor does not pay the liabilities within the time limit, the creditor has the right to submit the note and a demand for its activation at the Agency in order to collect the debt, the interest and the other costs until the day of the debt's payment. The Agency should immediately send the note to the debtor's bank. If there is no means or not enough means on the assigned bank account of the debtor, the Agency should ask every bank where the debtor has transaction account to transfer the assigned amount of the note to the creditor's account. If there is no means or not enough means for the debt to be collected on the day of the demand, the banks should do it from the first cash flow on the debtor's accounts.

The banks should be obliged to charge the notes of the same debtor according to the date they were received, starting from the first received to the last. Furthermore, the bank would have to inform the agency about the balance of the account and its movements, or, in other words, about the (im)possibility for the debt to be collected from the debtor's account. If there is not enough means on the debtor's accounts to collect the entire amount of the debt within 30 days of the filed note, the Agency should block every debtor's account and start an insolvency procedure.

The note could be issued in two ways: a) a note where the exact amount of the debt and its ground would be stated; b) a blank note where the previously stated elements wouldn't be specified. The blank note would give right to the creditor to additionally fill in the amount of the debt and its grounds, which might appear as a result of future mutual collaboration with the debtor along with the time limit that the creditor considers as the most appropriate. After its completion, the note would be effectuated in the same way as the note that had been issued completed.

Furthermore, the note could be in cash or in total asset. *The cash note* would refer to the possibility to charge the debt from the means on the transaction accounts of the debtor. The *total asset note* would refer to the possibility to charge the debt not only from the means on the transaction accounts of the debtor, but from the debtor's total asset as well. In order to abide the existing laws in RM, and, at the same time, put these ideas into practice, it is necessary for the note to contain a clause stipulating its executive trait. This means that if the creditor cannot collect the debt due to a lack of means on the transaction accounts, the creditor could call on the clause in question and hand in the note to an executor of the creditor's choice in order to activate this given possibility. By implementing the existing laws and regulations, which would also have to be amended in order to be applicable in the cases when the note would be activated as an executive order, the executor would collect the debt from the debtor's total assets in a manner already described in the Law on executive action. In this way, there would be no need of legal proceedings and a court order for starting an executive procedure. The executive procedure would be automatically activated by fulfilling the criteria in the note.

Thus the note would also have a role of an instrument for extrajudicial settlement of the parties. If the means for settling the debt cannot be collected within thirty days of the beginning of the executive procedure, the Agency would ask all assets of the debtor to be frozen and would start an insolvency procedure.

For the note to be valid, it must be signed by authorized entities of both parties (debtor and creditor) whose signatures have been certified in the Central Register of the RM. A note signed by other persons would be considered illegal and the note invalid. At the same time, the persons would be charged for unauthorized representation.

The note can be withdrawn by the creditor at any time regardless of the payment of the amount on it. In that case, the legal action pursuant to it would stop. The note (both versions) must be previously printed and unified. It would be an official form regulated by the Ministry of Justice or the Ministry of Finance with a suitable Bylaw or manual.

In the first phase of the implementation of this instrument, it is advised to be used by the legal entities only. In the later phases, after the assessment of the implementation of this revolutionary project, individuals can also use the note and its system of payment.

In the whole procedure of issuing and effectuating the notes (in appropriate stages of its implementation), the following parties should be included: the debtor, the creditor, the Agency, the banks, the executors, and the courts. Their involvement in this system should be made possible by suitable changes and amendments in the existing laws on system payments.

During the operational preparations and the possible implementation of this model for mutual payment of debts, the authorities, especially the Ministry of Justice, should make estimations whether it is necessary to include the Notaries public at a certain stage of the issuing of the notes in order to ensure the validity of this obligational instrument. If it's not indispensable, then it is better not to include the Notaries public in the process of issuing the notes in order not to expose the firms to additional expenses. The executors would be included in the process of collecting the debt on the demand of the creditors after having created conditions for it. A court order wouldn't be required. The executors would get their reward from the debtor or from the amount of collected debt through the executive procedure.

2.2. Abandoning the system of payment by settling accounts

The SAP wouldn't be able to create the expected effects and results when the so called payment by settling accounts (cessions, compensations, deposit forms, etc.) is still widely used (Nenovski, 2008). If this system of payment still persists, it will be still possible to manipulate the payment of the liabilities to the detriment of the creditor. Furthermore, even if the note was activated, when there isn't means on the debtor's account, the debt couldn't be collected. In the meantime, the debtor could make payments using the system of payment by settling accounts and, in that way, he would be able to work in his interest and accomplish his goals disregarding the interest, goals and needs of the creditor on the note.

Thus, in order to enable SAP to function freely, it is necessary for the articles in the Law on Payment Turnover that ban the payment by settling accounts to come into effect. Due to the world economic crisis and the already present (and additionally increased) problems with liquidity that the firms were facing, the coming into effect of the decision to ban the payment with settling accounts was postponed to January 2012. Having in mind the decreased intensity of the economic crisis, now, it would be the right time to implement the decision and disable the possibility for payment with settling accounts in order to reinforce the financial discipline in the economy. However, I must say that it would be best to start the SAP from the first day when the decision to ban the payment with settling comes into force. In order to do this, it is necessary to synchronize the active effect of the regulations referring to the SAP.

2.3. Speeding up the bankruptcy procedures and increasing the efficiency of the judiciary sector

To increase the financial discipline and thus increase the effectiveness of SAP stepping up the pace of the realization (finalization) of the bankruptcy procedures is much needed. A solution to the problem is a regulation requiring the company in question to pay its debt before thirty days expire, after which the Agency automatically

blocks the company's accounts. The account will be used to pay off the debt of the debtor company, unless the company lacks sufficient funds in which case the Agency immediately initiates a bankruptcy procedure. This will result in decreasing the possibilities for manipulations by the owners or managers in paying their debt.

The bankruptcy procedures would be conducted by the Commercial Court. In the applicable law in the Commercial Court, a provision needs to be inserted for mandatory (except for exceptional cases defined by law) completion of the bankruptcy proceedings within six months of its initiation.

Moreover, in function of reinforcing the new payment system of mutual obligations of economic entities will be strengthening the efficiency and effectiveness of the judicial system through:

- change in court's laws that will require for the debtor to pay the litigation costs, and not the creditor (as it is now), which would speed up judicial proceedings and protect creditors;

- establishing a Commercial Court that will quickly, efficiently and effectively resolve commercial disputes in up to ten days after a complaint with proper documentation has been filed, and with no possibility for postponing the scheduled hearing. Any appeals against the decision of the Commercial Court are to be resolved by the Appellate Court within, at most, 10 days after the appeal;

- liquidation of the company after the request has been made, or in cases postulated in the laws within three months of the initiation of the procedure.

3. Legal basis of SAP

In order for SAP to be successfully established and set up to function smoothly, an appropriate modification and amendment of certain laws that regulate this matter is required. It will be necessary, therefore, to change and synchronize them accordingly, to avoid collision and/or conflict of the regulations, or incomplete regulation of SAP, which will deprecate the realization of the project (payment model).

Under the current structure of the payment operations in the country and according to the proposals for establishing SAP, it seems that additional amendments are mandatory to the following system laws:

- a. Contract Law. This law regulates the check, bill of exchange and other securities as payment instruments and/or instruments securing payments. The same or similar way the functions of these securities are regulated, a legal basis needs to be established for the functioning of the debit note as a necessary (obligatory) instrument in the regulation of mutual obligations and payments of economic entities (parties);

b. Law on Enforcement Procedure. Since the proposed model for automatic payment provides a possibility for use of the issued debit note as an instrument of the clause of enforceability, if it is not enforced in the selected period, it will entitle the creditor to activate the clause of enforceability. In this case, the debit note needs to act like an executive court document (current situation). Therefore, provisions containing several acts that will determine the way the debit note is handled in function of carrying out the obligation of the debtor as indicated in that document, should be included in the Law on Enforcement Procedure;

c. Law on payment turnover. The introduction of SAP and the debit note as an instrument for its realization would mean appropriate adjustment to the future of the current system of payment in the country. Therefore, it will take appropriate adjustment (change and / or addition) of the law in the direction of accepting the debit note as an instrument of payment and its full recognition as an equal (albeit forced) instrument in the payment system in the country;

d. Banking Law. To ensure a no-obstacle flow in the implementation of the submitted debit note, a provision needs to be inserted in the Banking Law stipulating that the submitted debit note needs to be monetized immediately, i.e. without delay, after its delivery to the bank, with punitive measures against the bank that will not immediately carry out the payment if on the debtor's account there are free assets (pending obligations on other grounds);

e. Regulation for form, content and operation of the debit note. SAP would be a revolutionary change in the payment system of the country. Application of the debit note as its manifestation can cause a range of unknown and uncertain issues, conflicts and collisions in the understanding of its role, etc. Therefore, in parallel with the adoption of appropriate legislation that will regulate the establishment of the SAP, i.e. the introduction of the debit note as an instrument of payment and/or securing the payment, it will be required to have (Ministry of Justice, in cooperation with the Ministry of Finance) regulations or instructions on the form, content and operation of debit note;

f. Commercial Court Law. Current problems in the realization of economic disputes can be very vigorously and effectively resolved by establishing a Commercial Court. Its efficient operation is aimed at strengthening the organization and effectiveness of the SAP for reasons previously mentioned. However, if costs are estimated to be high for the country to establish such a court, then it's possible to be delayed for a future period. This means that SAP, initially, could function without establishing Commercial Court, and disputes would be solved in the current courts.

4. Conclusion

The introduction of SAP will undoubtedly improve the business climate in the country. It will increase mutual confidence of economic agents, and Macedonia will become a reliable and secure destination for investors' funds. The effects of this measure will be: increase in the liquidity of economic entities, elimination of the practice of firms avoiding cooperation with firms' debtors, increase in the activity of enterprises (increased sales), increase in production, reduction of companies' costs (now being a condition of forced tax payment (by law) without effective flow of funds), increase in the income of enterprises, increase in the state budget, GDP growth, etc.

The possible establishment of a SAP will ultimately lead to a revolution in payment operations. Therefore, for its successful completion a prior preparation of the completed system project that will eliminate any weaknesses and possible future quakes in payment operations in the country is required. The ultimate effect of such measure would be to increase the reliability, stability and liquidity of economic entities.

References:

1. Association of Macedonian Chambers of Commerce (AMCC), *Strategy for economic growth through the development of SME's*, Skopje, 2011;
2. Banking Law, "Official Gazette of RM" no 67/2007,..., Skopje, Republic of Macedonia;
3. Contract Law, "Official Gazette of RM" no 18/2001,..., Skopje, Republic of Macedonia;
4. Directive on combating late payment in commercial transactions,
<http://www.europarl.europa.eu/sides/getDoc.do?pubRef=-//EP//TEXT+TA+P7-TA-2010-0374+0+DOC+XML+V0//EN&language=EN#BKMD-20>
5. Enforcement Law, "Official Gazette" no 139/10, Zagreb, Republic of Croatia;
6. Law on Enforcement Procedure, "Official Gazette of RM" no 35/2005,..., Skopje, Republic of Macedonia;
7. Law on payment turnover, "Official Gazette of RM" no 113/2007,..., Skopje, Republic of Macedonia;
8. Nenovski, T., *Transitional tunnel* (pp. 172-174), Nampres, Skopje, 2006;
9. Nenovski, T., *Economic clearing up*, (pp. 26-39), Nampres, Skopje, 2008;
10. Nenovski, T., *Macedonia and the world economic crisis* (pp. 100-102), Nampres, Skopje, 2010;
11. Regulation for form and contest of a debt note, "Official Gazette" no 147/10, Republic of Croatia.

