Codes of payment practice: do they make a difference?

Full paper to be presented at the
Society for Business Ethics Annual Meeting, 6-9 August 2009

A-2 CODES OF ETHICS

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Abstract

In recent decades the use of trade credit has been extended as a short-term financing. In this paper we analyze the use of trade credit in United Kingdom from an empirical perspective of ethical relevance. The main contribution of the paper is to analyze the differences in trade credit practices between companies that sign a payment code and those that do not. The results show that signatories of payment codes complete all the legal requirements applicable to UK companies. However, although there are differences between signatories of payment codes and those firms that do not sign any payment code in terms of days to pay suppliers, differences are not statistically significant. So, taking fewer days to pay suppliers is not linked with signing a payment code, at least statistically; but signatories of more recent payment codes are quicker payers than in general. The weak association between signatories and better payers raises a doubt as to the use of signatories of payment codes as a factor to identify better payers and calls into question the effectiveness of such codes.

Keywords: Ethics in Finance, Payment Code, Payment Policy, Suppliers, Trade Credit.

JEL Classifications:

C200: Single Equation Models; Single Variables: General
G380: Corporate Finance and Governance: Government Policy and Regulation

1. INTRODUCTION

In spite of its importance, finance figures relatively little in writing on business ethics (Boatright, 1999; 2008); and with the intellectual “capture” of finance by financial economics (Whitely, 1986), little consideration is given to ethics within finance literature either (Prindl & Prodhan, 1994). Thus few mainstream financial topics have been analyzed adequately from an ethical perspective, and some have barely been addressed at all. One such latter topic is trade credit.

Trade credit is the provision of goods or services by one company to another in the expectation that payment will be made at some future date. It is a major source of finance for companies (Stern & Chew, 2003; Van Horne & Wachowicz, 2001), while it puts a strain on the resources of suppliers. Although it helps to promote sales and support economic activity, it puts suppliers in a vulnerable position as they wait to discover when they will be paid (if at all), notwithstanding their setting of terms of payment and the underpinning of contract law. For, as finance textbooks (e.g. Brealey et al., 2006; Ross et al., 2005) and conventional commercial wisdom point out, it is (ceteris paribus) to the benefit of businesses to delay paying suppliers as long as possible in order to take advantage of a free source of finance. Most financial textbooks recommend the use of trade credit as a fund.

Such practices raise ethical issues. For example, Gitman et al. (1976, p. 169-170) established that the “two basic cash management strategies normally applied are: (1) collect accounts receivables as quickly as possible without losing future sales due to high-pressure collection techniques. (2) Pay accounts payable as late as possible without damaging the firm’s credit rating and supplier relationship”. Thus, delay (or, even worse, default) by customers, especially major ones, can have severe, if not fatal financial consequences for suppliers, with repercussions in turn for their own suppliers and other stakeholders such as employees.

The aim of this paper is to establish the situation in the United Kingdom (UK) in terms of trade credit practices of signatories of payment codes. There are different aspects; macroeconomic
variables (Brechling & Lipsey, 1963; Meltzer, 1960; Nadiri, 1969; Ng et al. 1999; White, 1964) and finance theories (Emery, 1987; Fisman & Love, 2003; Nadiri, 1969) that analyze the influence of the use of trade credit. And, there is finance literature that analyzes the situation of trade credit in the UK (Cheng & Pike, 2003; Guariglia & Mateut, 2006; Howorth & Reber, 2003; Kohler et al., 2000; Paul & Boden, 2008; Pike & Cheng, 2001; Wilson & Summer, 2002), but there are no works that systematically study trade credit from an ethical perspective, although there are several technical and ethical questions that can be asked about it.

Moreover, the current financial situation; the credit crunch and economic downturn increases the financial problems of companies in terms of liquidity and highlights ethical issues in terms of the use of trade credit, in particular by large firms. The financial restrictions prompted by the credit crisis exacerbate firms’ cash flow problems especially as banks are in a weaker position. It is therefore more important than ever of companies to be able to identify which companies are likely to pay promptly and which are at risk of not doing so. In addition to traditional tools of credit rating, it is possible that some characteristics such as payment codes help to provide information about the quality of their future expected payments; those firms that sign a payment code might be expected to be “better” payers.

Thus, in this paper the focus is on signing a payment code. We will analyze the differences between companies that have signed a payment code and those firms that have not signed. Explicitly, the question that we will answer is the following one: do signatories of payment codes pay suppliers more quickly?

The contributions of this paper are twofold. Firstly, we analyze the payment codes from the perspective of characteristics of codes of ethics; content, communication, integration, culture or behaviour and control. Secondly, we examine the payment behaviour of companies that have signed a payment code. Unfortunately, although their behaviour in terms of carrying out the requirements of the law is correct, signatories of payment codes are not statistically better payers than firms that do not sign a payment code.

The remainder of this paper is organised as follows. The first section provides an overview of previous research around business codes and the differences between payment codes and business codes. Then, the public policy initiatives in the UK and the hypotheses to test are covered. The next section describes the data, variables and method. This is followed by the empirical results; a descriptive analysis of the variables to show the situation of signatories of a payment code and the results of the tests of the previously established hypotheses. The paper concludes with a discussion of the key findings.

2. BUSINESS CODES AND CODES OF PAYMENT PRACTICE

2.1. BUSINESS CODES: EFFECTIVENESS VARIABLES

“A business code is a distinct and formal document containing a set of prescriptions developed by and for a company to guide present and future behaviour on multiple issues of at least its managers and employees toward one another, the company, external stakeholders and/or society in general” (Kaptein & Schwartz, 2008, p. 113).

Most large companies in countries such as the UK have developed business codes. For example, Kaptein (2008) found that 86% of the two hundred largest companies in the world had
developed a code of conduct. However, the question is not just how many firms have developed an ethical business code, but whether business codes are effective (Dobson, 2003; Kaptein & Schwartz, 2008; Schwarz, 2001; Stevens, 2008).

Some scholars argue that firms should have a business code because it is the right thing to do, because the code shows the moral responsibility to help solving social problems, because it improves the reputation of the company, because codes increase the efficiency of the firm or because codes, if embedded in the organizational culture and communicated effectively, can shape ethical behaviour and guide employees in ethical decision-making (L’Etang, 1992; Logsdon & Wood, 2005; Mezher et al., 2002; Stevens, 2008). However, other scholars argue that: business codes are mere window-dressing; they make stakeholders more suspicious, cynical and distrustful; their cost is much greater than their yield; and most important evidence for their effectiveness is inconclusive (Hess et al., 2006; Kaptein & Schwartz, 2008; Moore, 2006; White & Montgomery, 1980). In sum, and in agreement with Cowton & Thompson (2000, p. 166), “it would seem that there is little strong systematic evidence to confirm the effectiveness of codes, although it would also be fair to say that the evidence to the contrary is also limited”.

Although previous results regarding to the usefulness of codes are not conclusive, there is some general agreement around the characteristics that would tend to make a code more effective: content, communication, integration, behaviour and culture, and control (e.g., Kaptein, 2004; Kaptein & Schwartz, 2008; Norberg, 2009; Stevens, 2008; Webley & Werner, 2008). Schwartz (2004) suggests that business codes are effective when they have features of readability, relevance and are written with a positive tone. Moreover, the success of the code (ceteris paribus) depends on the coordination and the relationship between the persons that write the code and those expected to operate it; a mere order from writers to staff is a barrier to the effectiveness of the business code (Stevens, 2008). Weeks & Nantel (1992) conclude that codes were ineffective except when well communicated in organizations. In general, codes are often communicated through meetings, work groups, notice boards, and so on, and/or posted on a company website (Stevens, 2008).

But, there is another constituent of the effectiveness of business codes – the process in which the code is developed. Kaptein & Wempe (1998, p. 853) argue that “a code is nothing, coding is everything”. The principal reason for establishing an integrated model as an instrument is to steer the conduct of management and employees to get favourable consequences for the company, its stakeholders, and society in general (Kaptein & Schwartz, 2008)[i]. Furthermore, although there is limited empirical evidence and no conclusive evidence about the relationship between ethical codes and the ethical behaviour that they support (Cowton & Thompson, 2000), we could agree with Stevens (2008) that in the case of a lack of appropriate organizational culture, the code could become simply a compliance document that is easily ignored.

The last step in the effectiveness of business codes is control. This includes enforcement. It could also include measuring the impact of the code. In relation to this, Kaptein & Schwartz (2008) recommend assessing the effectiveness of business codes against the objectives the companies have in mind in producing with a code.

2.2. THE PAYMENT CODE IN UK: DIFFERENCES FROM BUSINESS CODES

In UK payment codes have been developed since 1991; they are business codes that guide
payments between suppliers and customers. General business codes tend to pay less attention to competitors and suppliers than to the rest of stakeholders (Kaptein, 2004). Payment codes therefore complement general codes of conduct in terms of payments to suppliers.

A payment code could be defined as a formal document to establish ethical guidelines around payment conduct or behaviour in firms. There are some significant differences from business codes. Payment codes are written outside firms, by a government department or by a confederation of firms in the UK, and the target group is the top managers only – the financial director or payment manager.

There are different versions of the payment code in the UK. The code has been changed twice. In each development of the code, it is clearer when compared with the previous version; the changes provide greater detail. The focus is on paying on time suppliers and they encourage a good payment practice with suppliers. The firms that translate their responsibility with payments and sign the payment code have to sign the entire new versions, because if they are not among signatories of new codes, the stakeholders, society and suppliers in particular, probably are going to feel that something is wrong with the commitment of the firms in terms of payment.

The first payment code (developed by the Confederation of British Industry-CBI) called “Prompt Payers Code” started operating in November 1991 (see Appendix 1). Between 1991 and 1997 (operating period), this code was signed voluntarily by 1000 firms, most of them limited companies.

In 1997 another payment code superseded the CBI code; the “The Better Payment Practice Code” developed by the Department of Trade and Industry (DTI) (see Appendix 1). This second voluntary code is more direct and clear. Although the ideas of both of the codes are similar, in the second one the words used to describe the relationship between seller and buyer are clear, direct and positive; they use “explain” instead of “provide”, “pay bills” instead of “not extend or alter” and “tell suppliers without delay” instead of “ensure that there is a system”. More than 1000 firms signed this payment code from 1997 to 2008. Most of them are limited companies, associations and agencies (90%).

More recently, in December 2008, the third UK payment code has appeared supported by the Institute of Credit Management (ICM), on behalf of the Department for Business, Enterprise and Regulatory Reform (BERR) – the “Prompt Payment Code” (see Appendix 1). This recent voluntary payment code is focused in a direct way, not only on information and paying bills, but also on helping increase the speed of payments to smaller companies. In this version of the code the relevant ideas are “pay on time” and “encourage good practice”.

There is a double communication involved. Firstly, the communication of writers of payment codes in which writers (government departments) show the code to companies and to society. The government departments (the last two versions) or confederation of industries (the first version) have developed the payment code and they communicate to members, for example by posting letters (the existence of last payment code in 2008 has been communicated by posting letters to CBI members) or by web page[ii] (each of the last two payment codes are in creators web pages with added information around the payment code as benefits of paying on time or cash flow guide for firms). Secondly, the communication by signatories of payment codes indicates, by a logo, that “a firm that fulfils some ethical guidance in terms of payments” is the most important form of communication between firms and society, or in particular with suppliers. However, the communication of signatories of the payment code and staff responsible in the company is
unnecessary or easy because they are the same people or they are very close (normally the high level staff; chief-executive or Financial Director).

Once the firms voluntarily sign the payment code, there are two possible behaviours. First, if they continue the same payment policy as before they at least give clearer commitments and guidance to suppliers. The second possibility is that the firm actually changes its payment policy.

Regarding control, the last version of the payment code, “Prompt Payment Code”, is more complex, because there is a prior and a posterior control element to being a signatory. The pre-control is that the references are required from two suppliers of each potential signatory firm, to certify their good practice in terms of payment before becoming a signatory. Moreover, each May and November, they will review all approved signatories and request confirmation from their referees that signatories are still paying promptly – the post-control of the good payment practices. Although this measure does not control the total effectiveness of the payment code guidelines, it shows that the signatory of the “Prompt Payment Code” pays promptly to two of its suppliers. This control originates from outside the company (e.g. government departments) to firms. Unlike many code of ethics, where many staff of different levels are involved, the internal control challenges are relatively limited because the relevant staff work in relatively small terms.

3. PUBLIC POLICY INITIATIVES IN THE UK: HYPOTHESES

Brought into sharper focus by current economic problems, the promptness and clarity of payments related to trade credit have been subject to various initiatives in the UK in recent years (since 1997). Plcs (and Plc subsidiaries which qualify as ‘large’ companies) were required to disclose their policy on the payment of trade creditors in the United Kingdom[iii] by 1997 Regulation (see Appendix 2). The “Policy on the Payment of Creditors” (Part VI) establishes that companies should settle the terms of payment with suppliers when agreeing the terms of each transaction, ensure that those suppliers are made aware of the terms of payment, and abide by those terms (the 3 “ideas” in the 1997 Regulation are used in our empirical analysis as a variable). Instead of using these 3 ideas, some firms use some general phrases to describe their relationship with suppliers that are based on common logic, and less exhaustively than the 3 ideas required in the 1997 Regulation. Firms use phrases such as “the group values its suppliers and recognises the benefits to be derived from maintaining good relationships with them”, “explain its payment procedures to its suppliers” or “the policy of the group is to agree terms of payment with suppliers prior to entering into a contractual relationship” (we have called this variable “Similar Words” and we have used it in our empirical analysis). The annual report should disclose the company’s policy to follow any code or standard on payment practice (signing a Payment Code is used as a variable in our empirical analysis), and if so, the name of the code or standard and the form to get copies of the code. These aspects of the 1997 Regulation have been active since 1997. Furthermore, it is now a requirement[iv] that the directors’ report should make a quantitative statement relating the amount outstanding to suppliers to the total invoiced during the year (number of days in Directors’ Report [DR] is a variable that we have used in our empirical analysis):

\[
\text{No. of days (DR)} = \frac{\text{Trade creditors value at the end of the year}}{\text{Aggregate amount invoiced by suppliers during the year}} \times 365
\]
This latter figure gives an insight into company practice, to complement the policy statements they might also make. This requirement permits external analysts to use a ratio that is a better proxy of days that the firm takes to pay suppliers, because without this disclosure in the Directors’ Report, the only form to calculate the days is using the annual accounts (Balance Sheet and P&L Account). We have called this Proxy (we have used this variable in our empirical analysis).

\[
\text{No. of days (Proxy)} = \text{Trade creditors value at the end of the year} \times \frac{365}{\text{Cost of Sales}}
\]

*Some companies do not disclose cost of sales because they employ a different reporting format in which case this version of the proxy cannot be calculated.

As we have explained in a previous section there are three payment code versions in UK, although the companies in our sample signed only the two variants existing before 2008: “Prompt payers: in good company” and “Better Payment Practice”.

The focus of the payment codes and the 1997 Regulation relating to the policy on the payment of creditors are closely related. Both are concerned with establishing agreement about payment terms, with giving full and accurate information to suppliers, with making a commitment to pay suppliers on time and with describing conflict resolution steps. Those initiatives are designed to encourage “better” behaviour by companies in dealing with their suppliers.

In this context, we have established the following hypotheses:

| Hypothesis 1a | The number of days (using the Proxy to calculate the payment days) and Signing a Payment Code is independent. |
| Hypothesis 1b | The number of days in the Directors’ Report and Signing a Payment Code is independent. |

| Hypothesis 2a | The similar words (a common but not exhaustive explanation about the policy to complete successfully payment terms with suppliers) used in Payment Policy in the Annual Report (Directors’ Report) about the relationship with suppliers and Signing a Payment Code is independent. |
| Hypothesis 2b | The explanation of the ideas of 1997 Regulation about the relationship with suppliers, explained in Payment Policy in the Annual Report (Directors’ Report), and Signing a Payment Code is independent. |

| Hypothesis 3a | The number of days (using the Proxy to calculate the payment days) and the type of signed code (CBI or DTI) by the company is independent. |
| Hypothesis 3b | The number of days in Directors’ Report and the type of signed code (CBI or DTI) by the company is independent. |

4. DATA AND RESEARCH METHOD

4.1. SAMPLE

This study was conducted on UK firms. The sample used in this study was taken from FTSE All-Share Constituents & Weightings data (31 October of 2007), which shows the:
• FTSE 100 (consisting of the largest 100 UK companies by full market value, i.e. before the application of any investment weightings),

• FTSE 250 (consisting of the next 250 UK companies ranked by full market value, i.e. before the application of any investment weightings)

• and FTSE SmallCap (consisting of the UK companies within the FTSE All-Share which are not large enough to be constituents of the FTSE 100 and FTSE 250).

In our sample we selected 100% of FTSE 100 firms (really there were 102 firms, but we have taken 100; we eliminated Royal Dutch Shell B and Schroders N/V, because we did not have information about them), 20% of FTSE 250 firms and 14% of FTSE SmallCap. The sample for FTSE 250 and SmallCap was selected randomly using systematic method after listing the population in alphabetical order, with no replacement of individuals. Twelve of the firms selected (Dexion Absolute, Ferrexpo, Invesco Property, Merryl Lynch New Energy Technology and Thomas Cook Group of FTSE 250 and Agcert International, Cineworld Group, Cmhyt, F&C Property Investment, The Local Shopping Reit, Sepura and Superglass of FTSE SmallCap) were replaced by the next in the list because they did not have a 2007 Annual Report (in most cases because firms were in liquidation or had merged with other companies) or they had no payment policy in their 2007 Annual Report. The payment policy is the principal focus of our study and it is the reason for replacing these companies with others. A random sample of 200 firms was selected.

Data were collected by means of annual reports or Financial Analysis Made Easy (FAME) database. The annual report was used principally to obtain the data about payment policy and FAME database was selected as it contained relevant information (e.g. trade creditors, cost of sales).

The following table summarises the technical characteristics of the study:

<table>
<thead>
<tr>
<th>UNIVERSE</th>
<th>UK Firms. FTSE All-Share Constituents &amp; Weightings (100, 250, SmallCap)</th>
</tr>
</thead>
<tbody>
<tr>
<td>SAMPLE</td>
<td>200 firms</td>
</tr>
<tr>
<td>SAMPLING</td>
<td>Systematic random probabilistic sample</td>
</tr>
<tr>
<td>TARGET GROUP</td>
<td>FTSE firms with payment policy in Annual Report (Directors’ Report)</td>
</tr>
<tr>
<td>DATA</td>
<td>The data of firms have been taken of Annual Report of FTSE firms 2007 and FAME Database in 2007</td>
</tr>
<tr>
<td>TECHNIQUE</td>
<td>Review of Annual Reports 2007</td>
</tr>
<tr>
<td>DATE PERFORMED</td>
<td>Field work was carried out on November 2007 (choose sample and collect available 2007 Annual Reports) and November 2008 (collect the rest of 2007 Annual Reports, review data comparing information in Annual Reports and FAME, and clean the sample)</td>
</tr>
<tr>
<td>MARGIN OF ERROR</td>
<td>Em= ± 3.77% with a confidence level of 95%, p=q=0.5, for overall data</td>
</tr>
</tbody>
</table>

The sample is significant at 95% level with an error of 3.77% and it accounts for approximately 85% of the capitalization of UK firms, so this group of firms are a good sample
that represents statistically the UK firm population.

4.2. THE VARIABLES

In this paper we have used information from annual reports and the FAME (UK) database. We have taken the information about payment policy that appears in Directors’ Report of Annual Report. The quantification of this data is realised in the following form (see Table 2):

<table>
<thead>
<tr>
<th>Annual Report</th>
<th>FAME</th>
</tr>
</thead>
<tbody>
<tr>
<td>VARIABLE</td>
<td>CODIFICATION</td>
</tr>
<tr>
<td>Payment Code</td>
<td>No:0, Yes:1</td>
</tr>
<tr>
<td></td>
<td></td>
</tr>
<tr>
<td>Type of Code</td>
<td>CBI:1, DTI:2</td>
</tr>
<tr>
<td></td>
<td></td>
</tr>
<tr>
<td>Similar Words</td>
<td>No:0, Yes:1</td>
</tr>
<tr>
<td>Ideas of the 1997</td>
<td>No:0, Yes:1</td>
</tr>
<tr>
<td>Regulation</td>
<td></td>
</tr>
<tr>
<td>How to obtain the Payment Code</td>
<td>No:0, Yes:1</td>
</tr>
<tr>
<td>Trade Credit</td>
<td>No:0, Yes:1</td>
</tr>
<tr>
<td>Average Trade Credit Days in 2007 (DR)</td>
<td>Number of Days</td>
</tr>
</tbody>
</table>

4.3. METHOD

Methodology is basic in the investigation about ethics in business (Chami et al., 2002) and trade creditors are not an exception. The intention is to determine if signatories of a payment code behave significantly differently in aspects related to payment practices. The proposed hypotheses reflect the different payment behaviour of companies that sign a payment code compared with those that do not sign it. It is also interesting to analyze if the days used to pay suppliers depend on the type of payment code that firms sign.

The empirical analysis that we have used in this study was conducted as we explained in a previous section on UK firms. The total number of firms used was 200, but the sample was reduced to 138 firms because only those firms that use trade credit are of interest. So we have established a constraint: the days to pay suppliers in the directors’ report have to be positive.

The statistical methodology used is Kruskal-Wallis test in the K Independent Samples procedure (2 in this case), available in the Nonparametric Tests procedure. The reason for using this test is that we have studied the shape of each group’s distribution, but the groups are not normally distributed. The statistic of the Kruskal-Wallis test is built from the means of the ranks of the observations across the samples. This approach is similar to that of one-way ANOVA, but Kruskal-Wallis test does not assume normality or equal variances (ANOVA assumes the normal distribution of the sample). As a result it is an appropriate test for this case.

We have used SPSS statistical program in 15.0 and 16.0 versions.
5. PAYMENT CODES: AN EMPIRICAL ANALYSIS

5.1. TRADE CREDIT PRACTICE OF SIGNATORIES OF CODES: A DESCRIPTIVE ANALYSIS.

There are 14 firms that signed a payment code (approximately 10% of the sample). Half of them signed the code supported by CBI and the rest of the firms the code supported by the DTI. Yet, the CBI Payment Code is an old code that finished more than ten years ago, in 1997, which suggests the lack of serious attention paid to payment codes by some firms. More than 80% of the signatories of payment codes are FTSE100 firms, i.e. the largest firms in the UK. The firms that have not signed a payment code total 124 (90%). There are no significant differences between firms that sign a payment code and those that do not sign a payment code in terms of industry.

The main focus of this paper is to analyze if there are differences in terms of days taken to pay suppliers between signatories of payment codes and those firms that do not sign a payment code. To measure the days taken to pay suppliers we could use two different ratios, the ratio required by the 1997 Regulation (DR) and the Proxy. We see in the following table (Table 3) that the days that signatories of payment codes take are close to those taken by non-signatories using the DR ratio, around 30 days. However, firms that sign a code use two days fewer than non-signatories of any payment code. Using the Proxy to make this analysis the difference is bigger, nearly 10 days between signatories (they use 43.22 days) and non-signatories (they use 53.18 days). Considering only those firms that sign a payment code, the CBI signatories use 6 days more to pay suppliers than DTI signatories using DR ratio as indicator in 2007.

In terms of the ideas required by the 1997 Regulation, the differences between signatories and the rest are clearer because more than 90% of firms that sign a payment code explain all of the ideas and only 18% of firms that do not sign a payment code do that. But, there are no differences related to Similar Words and most of the firms use similar phrases to explain their intention and their consideration to the relationship with suppliers, but not specifically all of the ideas required in the law.

Regarding how to obtain the code, nearly 75% of firms that sign a payment code explain in their Annual Report how to obtain the code. Thus more than a quarter of signatories do not follow the 1997 Regulations fully. Obviously, none of the firm that do not sign a payment code explains how to obtain it.

Table 3: Trade Credit practice of Signatories of a Payment Code: Descriptive statistics

<table>
<thead>
<tr>
<th></th>
<th>Signatories of a Payment</th>
<th>Non-signatories of a Payment</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>14 firms</td>
<td>124 firms</td>
</tr>
<tr>
<td>ProxyCS07</td>
<td>DR2007</td>
<td>ProxyCS07</td>
</tr>
<tr>
<td>(days)</td>
<td>(days)</td>
<td>(days)</td>
</tr>
<tr>
<td>Mean</td>
<td>43.22</td>
<td>32.50</td>
</tr>
<tr>
<td>Median</td>
<td>45.00</td>
<td>34.50</td>
</tr>
<tr>
<td>Std. Deviation</td>
<td>22.17</td>
<td>14.78</td>
</tr>
<tr>
<td>Minimum</td>
<td>6</td>
<td>6</td>
</tr>
<tr>
<td>Maximum</td>
<td>83</td>
<td>59</td>
</tr>
<tr>
<td>Similar words</td>
<td>Frequency</td>
<td>Percentage</td>
</tr>
<tr>
<td>no</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td>similar words</td>
<td>14</td>
<td>100</td>
</tr>
<tr>
<td>Total</td>
<td>14</td>
<td>100</td>
</tr>
<tr>
<td>1997 Regulation ideas</td>
<td>Frequency</td>
<td>Percentage</td>
</tr>
<tr>
<td>no 3 ideas of 1997</td>
<td>1 (CBI)</td>
<td>7.10</td>
</tr>
<tr>
<td></td>
<td>101</td>
<td>81.50</td>
</tr>
</tbody>
</table>
As we explain in the methodology section, to test the null hypothesis the Kruskal-Wallis test was selected. The p-value of the Kruskal-Wallis test represented the statistical method used to determine whether differences between the population means were significant. The test was used to consider the null hypothesis at a level of significance of 0.05.

Hypotheses 2b, 3a and 3b are rejected with a significance level higher than 95%, but hypotheses 1a, 1b and 2a are not rejected (see Table 4). The differences between signatories and non-signatories of payment codes are reflected in the ideas required by the 1997 Regulation (signatories explain correctly all of the ideas). The differences in terms of number of days to pay suppliers (using DR or Proxy) and similar words between signatories and non-signatories of codes are not clear. We can not say that there are statistically significant differences between firms that sign payment codes and those that do not sign payment codes in terms of days taken to pay suppliers. However, signatories of payment codes are more likely explain the ideas required in 1997 Regulation (settle the terms of payment with suppliers when agreeing the terms of each transaction, ensure that those suppliers are made aware of the terms of payment, and abide by those terms) and of course are more likely to state how to obtain the payment code that they sign. Although the statistical representation of the firms that sign CBI and DTI is doubtful, the test of the hypotheses suggest that the differences between firms that sign CBI and firms that sign DTI payment codes in terms of used days to pay suppliers (DR or Proxy ratios) are significant.

Table 4: Trade Credit practice of Signatories of a Payment Code: Test of Hypotheses

| H1a: The number of days (using the Proxy to calculate the payment days) and Signing a Payment Code is independent. | The probability of the Kruskal-Wallis statistic is 0.878, which is greater than the level of significance of 0.05. | H1a is not rejected: |
|---|
| Signatories (7 firms) | Signatories (7 firms) |
| Mean | Mean |
| ProxyCS07 (days) | 33.16 | 63.33* |
| DR2007 (days) | 35.85 | 29.14 |

*The result is not representative of all of 7 firms because the ratio is calculated with the information of only 3 firms.
We do not reject the null hypothesis and conclude that the analysis supports the research hypothesis that average number of days using the Proxy to calculate the payment days is not different for firms that sign a Payment Code and for firms that do not sign a Payment Code.

The probability of the Kruskal-Wallis statistic is 0.941, which is greater than the level of significance of 0.05. 

H1b is not rejected:

We do not reject the null hypothesis and conclude that the analysis supports the research hypothesis that average number of days using Directors’ Report to calculate the payment days is not different for firms that sign a Payment Code and for firms that do not sign a Payment Code.

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The probability of the Kruskal-Wallis statistic is 0.941, which is greater than the level of significance of 0.05. 

H1b is not rejected:
CONCLUSION

Payment to suppliers is an important aspect of the financial situation of firms. Public policy initiatives in the UK have encouraged firms to improve in this area. For example, the 1997 Regulation required UK large firms to establish their Payment Policy in their annual report (Directors’ Report), describing their relationship with suppliers, showing if they sign a Payment Code and how to obtain that Code as well as disclosing the days that they use to pay suppliers using the total invoiced by suppliers, an inaccessible variable for external analysts.

There are different points that could help suppliers to identify “better” payers; signing a Payment Code could be one such indicator. Specifically, in the UK three different payment codes have been developed in recent years, each being clearer and more detailed than the previous one; “Prompt payers code” from 1991 to 1997 developed by Confederation of British’s Industry (CBI), “Better Payment Practice Code” from 1997 to 2008 developed by the Department of Trade and Industry (DTI), and in December 2008 “Prompt Payment Code” supported by the Institute of Credit Management on behalf of Department for Business, Enterprise and Regulatory Reform (the DTI’s successor). These payment codes as most of business codes are focused on ethical guidelines in terms of payment to suppliers. Our results in this sense show that there are some notable differences between payment codes and business codes. The writers are external, but there is a close relationship between decision-makers who sign a payment code and the staff that are to carry it out, so implementation – once a commitment has been – should be relatively straightforward. Furthermore, the content is clear and brief, being focused on paying suppliers on time; payment codes do not directly affect all stakeholders, only suppliers.

Using UK data for 2007 in our empirical analysis, we find that the hypothesis that links signing a payment code with being a better payer is not supported by statistical evidence. More specifically, we show that firms that sign a payment code are more exhaustive comparing with the rest of firms in terms of complete the requirements in 1997 Regulation. Although they give in Annual Report correct explanations about the form to make relationships with suppliers it is not possible to say that sign a payment code implicates a quick payment to suppliers, at least
But, there is evidence that suppliers can have confidence in firms that sign a payment code that they will be paid within clearly defined terms, and that there is a proper process for dealing with any payments that are in dispute. In addition, although CBI and DTI signatories do not represent statistically the population, the explanatory analysis suggests that the DTI signatories are better payers than CBI signatories. This may be because the CBI Code officially ceased some years ago, and any firm still claiming to be a signatory might therefore not be committed to good payment practice.

In sum, the results show that signing a Payment Code is enough to complete correctly the requirements of the 1997 Regulation, but not for being a better payer and paying suppliers quickly. These findings raise a doubt related to the use of payment codes as indicators to identify better payers. However, but only as an exploratory suggestion, the type of payment code signed by the firms could be used as an approximation variable to recognize “better” payers.

LIMITATIONS AND FUTURE RESEARCH DIRECTIONS

Our results were based on the analysis of second data information (annual reports of firms and FAME database), so the data have been collected from a single source at a single time. While our results were supported, we relied on cross-sectional data. Future research should aim to test our results using longitudinal data drawn from both UK and other firms.
Appendices

Appendix 1: Payment Codes in UK

CBI (1991)

Prompt payers Code
The prompt payment of bills contributes towards ensuring a healthy, efficient and competitive economy. To delay payment beyond the due date, when goods have been received or services provided to a satisfactory standard, is not only a breach of contract, it is plain bad business as it can jeopardise the viability of valued suppliers. To assist companies to fulfil their obligation to honour contract payment terms, the CBI has set out the following Code of Practice for Buyers.

Responsible companies should:

• Have a clear, consistent policy that they pay bills in accordance with contract.
• Ensure that the finance and purchasing departments are both aware of this policy and adhere to it.
• Agree payment terms at the outset of a deal and stick to them.
• Not extend or alter payment terms without prior agreement.
• Provide suppliers with clear guidance on payment procedures.

Ensure that there is a system for dealing quickly with complaints and disputes and advise suppliers without delay when invoices, or parts of invoices, are contested.

DTI (1997)
The Better Payment Practice Code
The Better Payment Practice Group urges all firms to adopt a responsible attitude to paying on time.
By adopting the following four point code you can apply to use the Better Payment Practice logo. The use of this logo will send a clear signal to your suppliers and customers of your responsible position on prompt payment.

As a business you must promise to:

• Agree payment terms at the outset of a deal and stick to them;
• Explain your payment procedures to suppliers;
• Pay bills in accordance with any contract agreed with the supplier or as required by law; and
• Tell suppliers without delay when an invoice is contested, and settle disputes quickly.

You can apply online by visiting www.payontime.co.uk or by detaching and completing the coupon below* and returning it to us. To use the logo simply detach the logo* … and pass it to your stationery supplier to be printed onto your letterhead or other materials.

*B Not reproduced here.

BERR (2008)

Prompt Payment Code
The Prompt Payment Code is sponsored, hosted and administered by Institute of Credit management (ICM) on behalf of BERR and supported by RBS (Royal Bank of Scotland) and NatWest. (12 December 2008)
Recently, is supported by Barclays and HSBC too.

1. Pay suppliers on time
within the terms agreed at the outset of the contract
without attempting to change payment terms retrospectively
without changing practice on length of payment for smaller companies on unreasonable
grounds

2. **Give clear guidance to suppliers**
providing suppliers with clear and easily accessible guidance on payment procedures
ensuring there is a system for dealing with complaints and disputes which is communicated to suppliers
advising them promptly if there is any reason why an invoice will not be paid to the agreed terms

3. **Encourage good practice**
by requesting that lead suppliers encourage adoption of the code throughout their own supply chains

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1997 No. 571 COMPANIES

The Companies Act 1985 (Directors’ Report) (Statement Payment Practice) Regulations 1997

**PART VI**

**POLICY ON THE PAYMENT OF CREDITORS**

12.—(1) This Part of this Schedule applies to a report by the directors of a company for a financial year if—

(a) the company was at any time within the financial year a public company, or
(b) the company did not qualify as small or medium-sized in relation to the financial year by virtue of section 247 and was at any time within the year a member of a group of which the parent company was a public company.

(2) The report shall, with respect to the financial year immediately following that covered by the report, state—

(a) whether in respect of some or all of its suppliers it is the company’s policy to follow any code or standard on payment practice and, if so, the name of the code or standard and the place where information about, and copies of, the code or standard can be obtained,
(b) whether in respect of some or all of its suppliers it is the company’s policy—

(i) to settle the terms of payment with those suppliers when agreeing the terms of each transaction,
(ii) to ensure that those suppliers are made aware of the terms of payment, and
(iii) to abide by the terms of payment,
(c) where the company’s policy is not as mentioned in paragraph (a) or (b) in respect of some or all of its suppliers, what its policy is with respect to the payment of those suppliers.

(3) If the company’s policy is different for different suppliers or classes of suppliers, the report shall identify the suppliers or classes of suppliers to which the different policies apply.

(4) For the purposes of this Part of this Schedule a supplier is any person whose claim on the reporting company in respect of goods or services supplied would be included under "trade creditors" within "Creditors; amounts falling due within one year" in a balance sheet drawn up in accordance with balance sheet format 1 in Schedule 4.
(6) Schedule 9 to the 1985 Act (form and content of accounts of banking companies and groups) is amended in accordance with Schedule 4 to these Regulations.

(7) Schedule 9A to the 1985 Act (form and content of accounts of insurance companies and groups) is amended in accordance with Schedule 5 to these Regulations.

(8) Schedule 11 to the 1985 Act (modifications of Part VIII where company’s accounts prepared in accordance with special provisions for banking or insurance companies) is amended in accordance with Schedule 6 to these Regulations.

http://www.opsi.gov.uk/si/si1996/Uksi_19960189_en_1.htm
Notes
References


737-44.


[i] In this model the core is the content, but other parts of the process to develop an effective business code are important, such as establishing expected results and the objectives of the code, implementation and administration, characteristics and conduct of management and employees, and corporate effects.

[ii] The web pages of the payment codes are the following: www.cbi.org for “Prompt Payers Code”, www.payontime.co.uk for “Better Payment Practice Code” and www.promptpaymentcode.org.uk for “Prompt Payment Code”.


[v] The “Better Payment Practice Code” started in 1997, but some firms still say that the code that they have signed the previous one. In December 2008, another code, “Prompt Payment Code” was introduced, but our analysis is for 2007, so this new code is not considerate in our empirical analysis.

[vi] There are other three firms (Resolution, Umbro and Scottish and Newcastle) without access to their annual report 2007 for different reasons: the acquisition by others (Umbro has being acquired by Nike and Scottish and Newcastle by Heineken) or due to the fact that they are no longer a listed company and are not required doing so.