No late payment silver bullet

Guest editor Andrew Croft of Beale & Company Solicitors LLP examines the merits of recent steps taken to tackle late payment, and suggests some other possible paths to improvement. The Construction Act is under review, but don’t rely on legislation, he argues.

It is widely acknowledged that late payment is a key issue across the construction industry. For example, a study by the Asset Based Finance Association (ABFA) found that construction and real estate firms had to wait an average of 107 days to receive payment – a longer wait than in any other industry.

Improvements in the payment landscape
The Housing Grants, Construction and Regeneration Act 1996, as amended in 2011 by the Local Democracy Economic Development and Construction Act 2009 (the Act), has significantly improved the payment landscape in the construction industry.

The introduction of adjudication and the requirement for a clear payment process has provided some very useful tools for contractor, consultants and other suppliers (and also for ‘sophisticated’ employers who use adjudication and the payment notices to their advantage).

Downsides to the Act
However, there are some ‘downsides’ to the Act, including:

- to make use of the Act you need to understand how the complex payment processes work, which is not always the case and the Act can be difficult to apply practically;
- the Act may assist the payment process in the short term, but short term gains from any ‘tactical adjudication’ could later be overturned if the matter came before a court, so their effectiveness may be limited;
- whilst some clients respect those who act swiftly following a failure to comply with the Act, a number of suppliers will refuse to take action due to concerns of jeopardising long term relationships; and
- the Act is being exploited, for example by the inclusion of extremely prescriptive contractual payment provisions which seek to circumvent the Act, such as by requiring significant additional requirements and condition precedents to be complied with before payment will be due.

A review of the Act has been commissioned by Parliament and the industry should hope that some of the above concerns are taken into account.

Further legislation in the pipeline
Requirement to report on payment practices and procedures
Further legislation is also in the pipeline in relation to late payment, including a requirement for companies to publish a report on their payment practices and procedures, under the Small Business, Enterprise and Employment Act 2015. Is this really going to assist with late payment?

It is already easy to pinpoint the ‘bad payers’ from information available, but nevertheless having public reporting enshrined into statute must help.

Making this information more freely available may result in a ‘league table’ being produced clearly identifying to the industry those with poor payment records which we would hope will encourage improved payment practices.

It was suggested last year that secondary legislation would be introduced in April 2016 to introduce this requirement, but at the time of writing we are unsure if this will be the case.
Challenging unfair payment terms
Enactment of the Late Payment Directive

Another legislative step aimed at bad payment practices is the introduction of a right for industry bodies to challenge unfair payment terms as part of efforts to enact the Late Payment Directive in the United Kingdom (see Directive 2011/7/EU on Combating Late Payment in Commercial Transactions).

This is a good idea in principle but will industry bodies take the risk of incurring initial time and cost in relation to proceedings which their members may decide not to take forward (for example because the member has reached a commercial agreement with their client)? In the writer’s view it is unlikely.

Legislation can certainly help alleviate late payment, as the Act has shown to some extent and it is hoped that further legislative steps will bolster the position. However, the industry should not rely on legislation alone. To take advantage of any legislation, good credit management is essential. In addition, the industry can itself take steps to improve this issue (and is already doing so).

Other steps taken to address late payment

Project bank accounts

One such step is the use of project bank accounts (PBAs). The public sector, in particular, Highways England (which recently announced that it has awarded £10.4 billion of work using PBAs) and the Environment Agency, has made good use of PBAs and very positive results have been published on projects in which they are used.

This is perhaps a result of the additional certainty and transparency the use of PBAs can provide. PBAs are rarely being used in the private sector and the increased upfront administration could be one explanation for this.

Nevertheless, the Government Construction Strategy 2016–2020 (GCS 2016–20), published on 23 March 2016, proposes the increased use of PBAs in the public sector and hopefully this will encourage their uptake on appropriate private sector projects.

Payment charters

Another useful tool to help tackle late payment is the use of payment charters.

The Prompt Payment Code and the Construction Supply Chain Payment Charter are clearly well intended and set a good benchmark, but have not been used to their full potential to date. For example, there has not been sufficient incentive to become a signatory (there are only ten signatories of the Construction Supply Chain Payment Charter at the time of writing this article) and few consequences of failing to comply. This has meant their effect has been limited.

However, if used properly payment charters can be another helpful tool in tackling late payment. Hopefully the government and the industry as a whole will reconsider the use of charters going forward.

A digital revolution?

One of the key drivers for the difficulties in recovering payment has to be a lack of transparency. The digitisation of the construction industry provides the industry with an opportunity to address this.

The use of digital technology and processes is already changing how services are provided and work carried out, as shown by the significant strides taken in relation to the use of building information modelling (BIM).

Whilst the industry is still adapting to the digital change, applying it to the payment process could help reduce late payment. Issuing payment applications or invoices and pay less notices through a digital system could provide additional certainty, with such a system becoming the ‘one source of truth’ as to parties’ payment entitlement.

Helping improve this industry wide issue could provide greater incentive to the industry to make use of these new digital tools.

How do we therefore alleviate late payment?

There is no silver bullet to tackle late payment. Nevertheless there have been a lot of positive recent developments.

Legislation, wider use of PBAs and stronger payment charters may assist and perhaps the ‘digital revolution’ provides the industry with a real opportunity.

This would be a sensible time to reconsider the payment process and take advantage of these developments to provide additional transparency.

Tackling this industry wide issue will be key to incentivising innovation and helping keep the UK construction industry in a leading position globally – hopefully this opportunity will not be missed. CL