Late Payment – Improving an Industry Wide Issue

In February 2016, Beale & Company hosted a Round Table event at Capital House, 85 William Street, London, EC4N 7BL, with a cross section of the construction industry to discuss the perennial issue of late payment.

The purpose of this paper is to report on the key points discussed at the Round Table and consider how this issue might be improved. In due course we will be sending a version of this paper to key industry bodies, including the Construction Industry Council (CIC), the Association of Consulting Engineers (ACE), Civil Engineering Contractors Association (CECA), Building Engineering Services Association (BESA) and the Chartered Institute of Highways and Transport (CIHT), to encourage proactive steps to be taken across the industry and through legislation to address this key issue.

(The key findings in this paper will also be published in the May 2016 edition of Construction Law.)

An industry wide Issue

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. We held the Round Table event to discuss the merits of recent steps taken to date to tackle late payment, including existing legislation and proposed legislation, other steps which have been taken to seek to alleviate late payment, and ways this issue may be improved going forward.

Legislation

It was generally agreed at the Round Table that 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 contractors, consultants and other suppliers (and also for “sophisticated” employers who use adjudication and the payment notices to their advantage). However, attendees highlighted a few “downsides” to the Act, including that:

- to make use of the Act you need to understand how the complex payment processes work - not everyone understands these processes and the Act can be difficult to apply practically;
- the Act may assist the payment process in the short term, but an adjudicator’s award can later be overturned in court or arbitration, so any gains from a “tactical adjudication” may be lost;
- 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, for example: 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. We all welcome this.

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 was suggested at the Round Table that it is already easy to pinpoint the “bad payers” from information available but nevertheless having public reporting enshrined into statute would help. This was considered to particularly be the case if making this information more freely available results in a “league table” being produced clearly identifying to the industry those with poor payment records, which one 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 the Round Table we were unsure if this would be the case.

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 UK. During the Round Table, this was thought to be a good idea in principle but queries were raised as to whether industry bodies would want to take the risk of incurring initial time and cost in relation to proceedings which their member may decide not to take forward (for example because the member has reached a commercial agreement with their client)? This was considered to be something which would limit the effectiveness of this legislation.

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, attendees discussed at the Round Table that the industry should not rely on legislation alone. To take advantage of any legislation, good credit management is essential. In addition, the industry, from top to bottom, can itself take steps to improve this issue (and is already doing so).

Other steps taken to address late payment

We discussed that one such step to address late payment is the use of project bank accounts (“PBAs”). The public sector, in particular, Highways England (which recently announced that it has awarded £10.4bn 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. Attendees spoke positively about the use of PBAs and agreed that they had a role in improving late payment.

However, 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 proposes the increased use of PBAs in the public sector. Hopefully this will encourage their uptake on appropriate private sector projects.
Another useful tool to help tackle late payment is the use of payment charters. We discussed at the Round Table that the Prompt Payment Code and the Construction Supply Chain Payment Charter are clearly well intended and set a good benchmark, but they have not been used to their full potential to date. For example, there was not considered to be sufficient incentives to become a signatory (there are very few signatories to the Construction Supply Chain Payment Charter) and the consequences of failing to comply are minor. This has meant their effect has been limited. However, it was agreed that, 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.

It was generally agreed that one of the key drivers for the difficulties in recovering payment has to be a lack of transparency. We discussed that 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 BIM. Whilst the industry is still adapting to the digital change, applying it to the payment process could help reduce late payment. Attendees considered that 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 was thought to be key to providing greater incentives 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.

Practical Steps

Practical steps Beale & Company will take following the Round Table to seek to improve the issue of late payment include:

1. **circulate the key findings** - issuing this paper to attendees, publishing the key findings in Construction Law and sending this note to a wider audience;

2. **encourage action** – based on the findings of the Round Table and as outlined in this paper, engage with key decision makers/influencers such as the Department for Business Innovation and Skills, which is assisting with the review of the Act, and industry bodies such as the CIC, ACE, BESA, CIHT and CECA to consider steps which could improve this issue; and

3. **align payment process with other key industry developments** – consider the alignment of steps to alleviate late payment with other key changes in the industry, such as the digitisation of construction (and the opportunities this provides), through, amongst other things, Beale & Company’s Digital Network (http://www.beale-law.com/digital-network.php).

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If you would like further information on the matters discussed in this note or assistance in relation to late payment or your payment processes please contact the Beale & Company attendees to the Round Table:

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