Improving payment practices and the thorny issue of retentions

Payment remains a hot topic in the construction industry. Many SMEs are still feeling the pinch from Carillion’s administration while larger firms are trying to balance the growing calls for fairness in payment provisions with tighter margins.

In my April blog I updated on the draft Construction (Retention Deposit Schemes) Bill which had been introduced as a Private Members Bill by Peter Aldous MP. Since that time there have been some developments of interest, which I will briefly cover below.

Where are we on the Aldous Bill?

The 2nd reading has been delayed – it will now take place on 26 October 2018. However, that in itself could be beneficial in securing that the Bill passes. It is understood that 120 MPs are already in support of the Bill and the aim of those driving its addition to the Statute books is to gain more support in the months leading up to the 2nd reading.

So, there is hope that the Bill will pass. But will it assist in solving the payment issues rife in the construction industry?

Reaction to the Aldous Bill

The construction industry is aware payment procedures have to change – the demise of a company as large as Carillion and its impact on hundreds if not thousands of sub-contractors, consultants and clients cannot be ignored.
Losing a percentage value of sums rightly due can impact on cash flow. A party must be able to have assurances that those sums are protected. It is for this reason that major bodies inside the industry have come out in support of the Bill, including ECA and BESA, and in June those bodies petitioned the government for reform on behalf of their 335,000 members. In addition bodies outside the industry are supportive of the Bill. The Association of Accounting Technicians and the British Chambers of Commerce (who have over 575,000 members) are behind the proposed changes.

However some major trade bodies have come out against, including Build UK and CECA. But their position is not seeking to preserve the status quo on retentions or challenge the likely addition to the administrative burden on a project but to end retentions altogether. After all, retentions are taken from contractors’ interim payments by clients just as they retain retentions from their subbies.

Leading the way

There has been talk on changes to retentions but the first major client to take the lead has been Network Rail, who in June announced that they would be insisting on 28 day payment periods with no retentions.

There is understandably some trepidation as to this step, including which other major clients will follow, what impact will it have on cash flow down the chain and how will Network Rail (and other clients) monitor and enforce these provisions.

Retentions not the only key to unlocking payment issues

While recovering retentions or not having such deductions made in the first payment is important – losing typically 5% of sums due and being at risk that the company holding that sum could go into administration cannot be understated – there remains the need for all members of the construction industry to aspire to prompt payment of all sums due.

On 31 July Build UK published data related to the payment performance of 24 of its main contractor members. Not one of these contractors has an average payment time to its supply chain of less than 30 days, with time periods stretching from 33 days to 66 days. The data also shows a wide % range of payments not made in accordance with the applicable contractual terms, with the highest being 83%.
Although addressed as a “bold first step” by the chief executive of Build UK, the results highlight the considerable issues smaller firms are facing to obtain payments in good time and in accordance with their contractual terms.

Having come out in support of Network Rail’s announcement, the data published indicates that Build UK and its members could and should be doing more to drive better payment practices in the industry.

Conclusion

The Aldous Bill is a good first step (on the basis that it passes) and will provide safeguards for those who enter into contracts with retentions included. However given Network Rail’s recent announcement and the position of Build UK and CECA there remains the growing call for retentions to be abolished altogether.

That may improve the financial health of and reduce the risk to SMEs but what is key to cash flow is securing payment in good time. The industry still has a lot of work to do on that front.

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