

## **PROMPT PAYMENT BY GOVERNMENT SUPPLIERS**

A consultation on how Government should take account of a supplier's approach to payment in the procurement of major contracts

## **Purpose of consultation**

The Government wishes to gather views on whether it would be appropriate to exclude suppliers from major government procurements if they cannot demonstrate a fair, effective and responsible approach to payment in their supply chain management.

## **Scope**

The measures proposed in this consultation apply to all Central Government Departments, their executive agencies and Non-Departmental Public Bodies when undertaking procurements under the Public Contracts Regulations 2015. We welcome responses to this consultation from suppliers to government, their representatives, public bodies, and those otherwise involved in public procurement.

**Issued:** 10th April 2018

**Respond by:** 5th June 2018

**Enquiries to:** Crown Commercial Service, Rosebery Court, St. Andrew's Business Park, Norwich, NR7 0HS

**Email:** [paymentconsultation@crownccommercial.gov.uk](mailto:paymentconsultation@crownccommercial.gov.uk)

The consultation can be found on GOV.UK

## **Confidentiality and data protection**

Information provided in response to this consultation, including personal information, may be subject to publication or disclosure in accordance with the access to information legislation (primarily the Freedom of Information Act 2000, the Data Protection Act 1998 and the Environmental Information Regulations 2004).

If you want information that you provide to be treated as confidential please say so clearly in writing when you send your response to the consultation. It would be helpful if you could explain to us why you regard the information you have provided as confidential. If we receive a request for disclosure of the information we will take full account of your explanation, but we cannot give an assurance that confidentiality can be maintained in all circumstances. An automatic confidentiality disclaimer generated by your IT system will not, of itself, be regarded by us as a confidentiality request.

We will summarise all responses and place this summary on the GOV.UK website. This summary will include a list of names or organisations that responded but not people's personal names, addresses or other contact details.

## **Quality assurance**

This consultation has been carried out in accordance with the Government's Consultation Principles.

## **What happens next**

An analysis of the consultation responses will be produced in accordance with best practice guidance.

The consultation analysis, as well as wider engagement, will help inform the Government's next steps.

The consultation outcome will be published within 12 weeks of the close of the consultation or an explanation if this is not possible.

## Introduction

The Government understands the importance of prompt, fair and effective payment in all businesses, and that it is particularly important for small and start-up companies. Being paid promptly for work done ensures businesses have a healthy cash flow. This is especially important for small and medium sized enterprises (SMEs) who may not have the reserves of larger companies.

The Government has already taken action to improve payment practices in its supply chains:

- The Public Contract Regulations 2015 require many public sector bodies to pay their suppliers within 30 days and to mandate 30 day payment terms down the supply chain in new public sector contracts
- The Prompt Payment Code<sup>1</sup> has been strengthened and signatories commit to pay suppliers within 60 days and work towards 30 day terms. By July 2017 all major government suppliers signed up to the Code.
- The use of Project Bank Accounts is the preferred option in relevant government construction projects and over £10bn has been spent through this fast, transparent payment mechanism.
- Subcontractors are encouraged to report cases of late payment in public sector supply chains to the Crown Commercial Service's Mystery Shopper team who will then investigate on their behalf.
- The Small Business Commissioner role was created by the Enterprise Act 2016 to tackle late payment and poor payment practices in the private sector.

In its 2017 Manifesto, the Government stated that it would 'use our buying power to ensure that big contractors comply with the Prompt Payment Code both on government contracts and in their work with others'. This commitment has been examined in the context of the UK's procurement rules, the Public Contracts Regulations 2015. Through this consultation, the Government is now testing options that would operate in accordance with those rules.

The Government now wants to consider how it should take account of a supplier's record on prompt payment in the procurement of major government contracts, and when it is appropriate to exclude suppliers which cannot demonstrate a fair, effective and responsible approach to payment in their supply chain management.

This consultation aims to gather views and information on the effectiveness of the Government's proposed approach.

## Policy Rationale

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<sup>1</sup> [promptpaymentcode.org.uk](http://promptpaymentcode.org.uk)

The Government proposes that when suppliers are bidding for government contracts above a specific financial threshold, their approach to payment of their subcontractors should be assessed as part of the selection process. Efficient mechanisms to ensure that suppliers comply with contractual obligations as to payment of their subcontractors are important for the overall delivery of major contracts. As such, it is appropriate to consider a supplier's evidence that it demonstrates a fair, effective and responsible approach to payment in its supply chain management.

This policy would apply to all Central Government Departments, their executive agencies and Non-Departmental Public Bodies when undertaking procurements under the Public Contracts Regulations 2015.

The proposed financial threshold would be contracts over £5 million per annum. Contracts of this size are more likely to involve a supply chain. Assessing contracts by their value (rather than, for example, size of the supplier) should support a consistent application of the policy across different suppliers.

Wherever relevant, existing benchmarks and mechanisms for reporting a supplier's payment performance should be taken into account. Contracting authorities should be able to verify a self-declaration by a bidder by reference to these benchmarks and mechanisms.

For example, the Small Business, Enterprise and Employment Act 2015 introduced a statutory duty for large businesses to report on their payment practices. The Department for Business, Energy and Industrial Strategy (BEIS) has recently introduced a payment reporting system<sup>2</sup>, which requires the UK's largest companies and Limited Liability Partnerships to report on a six monthly basis on their payment practices, policies and performance. The Prompt Payment Code sets a standard for its signatories of paying 95% of undisputed invoices within 60 days unless there are exceptional circumstances.

The Government proposes that paying 95% of undisputed invoices within 60 days, over two consecutive six month periods, provides an appropriate benchmark of payment performance.

### **Proposed options and their legal base**

We have identified two options where an assessment of whether the bidder demonstrates a fair, effective and responsible approach to payment in its supply chain management might be appropriate under the Public Contract Regulations 2015 (PCRs). Neither are without potentially additional burdens

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<sup>2</sup> [gov.uk/check-when-businesses-pay-invoices](https://www.gov.uk/check-when-businesses-pay-invoices)

on contracting authorities and bidders. We wish to use this consultation to better understand the risks and benefits of each option.

### ***Option 1***

The assessment of whether the bidder demonstrated a fair, effective and responsible approach towards payment would form part of the selection criteria assessing the bidder's technical and professional ability. Regulation 58 of the PCRs allows contracting authorities to impose certain requirements on bidders for participation in a procurement where these are related and proportionate to the subject-matter of the contract.

Regulation 60(9)(d) of the PCRs allows contracting authorities to ask bidders for an indication of their supply chain management and tracking systems they can apply when performing the contract being procured.

Following this approach a contracting authority would apply a relevant criterion on effective payment systems in supply chain management at the selection stage of the procurement. It would ask a bidder to provide evidence of its payment systems and whether these are effective. This assessment would form part of the test of the bidder's technical and professional ability.

A contracting authority would need to be satisfied the requirement to demonstrate an effective approach to supply chain management is related and proportionate to the subject-matter of the contract. The Government would provide guidance to contracting authorities setting out a framework the contracting authority could use to identify relevant criteria and categories of relevant evidence. A contracting authority would be able to select their own criteria and evidence base, taking account of what was appropriate. This framework might include information from the bidder on:

- its standard payment terms and how it ensures 30 day payment terms are passed down its public sector supply chains;
- the robustness of its systems and processes for scrutinising and paying invoices and how it resolves disputed invoices promptly and effectively;
- whether poor payment practices in the past have impacted on the resilience and reliability of its supply chain;
- whether it has had to pay significant compensation or interest on late payments under late payment legislation;
- its historic performance on paying invoices, including against its standard payment terms, and percentage of payments made within specific time frames such as 60 days.

Bidders would then be assessed against this evidence. A contracting authority could assess the effectiveness of the bidder's supply chain management

against relevant benchmarks, for example, the standards in the Prompt Payment Code on paying 95% of undisputed invoices within 60 days.

It would be for the contracting authority to decide on the appropriate evaluation methodology and the outcome of the selection stage, including whether the evidence warranted the bidder being excluded from proceeding to the next stage.

***Question 1: What evidence do you consider contracting authorities would need to request from a bidder to assess the effectiveness of supply chain management payment practices?***

***Option 2***

Regulation 57 of the PCRs allows contracting authorities to exclude bidders from a procurement process under mandatory or discretionary grounds. Grave Professional Misconduct is a discretionary ground.

The Government considers that certain behaviours around a supplier's payment systems, in particular where there is a systematic failure to pay suppliers in accordance with specific obligations to do so, could be sufficiently serious to amount to Grave Professional Misconduct.

Contracting authorities would need to assess whether a bidder's past record of paying its suppliers indicated a systemic problem of non-payment of invoices. This could include poor performance against a common benchmark such as the Prompt Payment Code's principle that 95% of payments should be made within 60 days. Contracting authorities would then need to investigate whether the bidder's actions constituted a serious, culpable, systemic approach that demonstrated Grave Professional Misconduct.

This would have to be assessed on a case by case basis, taking account of the bidder's circumstances and the facts of the procurement. However, the Government would provide guidance to contracting authorities on appropriate evidence that could call into question the integrity of the bidder and demonstrate Grave Professional Misconduct. This might include evidence on:

- unfair practices such as knowingly delaying the raising of purchase orders or disputing invoices unnecessarily;
- failure to communicate honestly and effectively with subcontractors about payment issues and practices;
- failure to pay valid claims for interest or compensation under late payment legislation.

The decision to exclude a bidder would be for each contracting authority to decide on case by case basis. It would need to identify why the bidder had not

paid its invoices promptly and assess whether the bidder's overall behaviour demonstrated Grave Professional Misconduct.

If the contracting authority concluded that the bidder's behaviour demonstrated Grave Professional Misconduct, the bidder would have the opportunity to show whether it had 'self-cleaned' within the meaning of the PCRs. Self-cleaning could involve paying compensation in respect of any damage caused by the misconduct, collaborating with the investigating authority to clarify the facts and circumstances in a comprehensive way, or taking technical, organisational and personnel measures that would prevent future misconduct. A bidder that shows sufficient evidence of self-cleaning to satisfy the contracting authority it is reliable to carry out the contract, should not be excluded from the procurement process.

If a bidder is excluded from a procurement on grounds of Grave Professional Misconduct there would be a three year period of exclusion from the contracting authority's procurement opportunities unless it could later demonstrate adequate self-cleaning. Contracting authorities would therefore need to make a robust assessment on the basis of clear evidence that such an exclusion was warranted.

***Question 2: What evidence do you consider contracting authorities would need to request from a bidder to demonstrate Grave Professional Misconduct in payment practice?***

### **Appropriate evidence and benchmarks of a bidder's payment practice**

As explained above, under both the proposed approaches contracting authorities would ask bidders to provide evidence on prompt payment. We wish to use this consultation to better understand the nature of the evidence and benchmarks that should be considered.

Wherever relevant, existing benchmarks and mechanisms for reporting a supplier's payment performance should be taken into account. Contracting authorities should be able to verify a self-declaration by a bidder by reference to these benchmarks and mechanisms.

The Small Business, Enterprise and Employment Act 2015 introduced a statutory duty for large businesses to report on their payment practices. BEIS has recently introduced a payment reporting system, which requires businesses in scope to report their payment practices and performance (six monthly, starting with their first full financial year that starts on or after 6 April 2017).

These reports must include:



- Narrative descriptions of:
  - the business' standard payment terms;
  - the business' process for resolving disputes related to payment.
  
- Statistics on:
  - average number of days taken to make payments in the reporting period;
  - percentage of payments made within the reporting period which were paid in 30 days or fewer, between 31 and 60 days, and in 61 days or longer;
  - percentage of payments due which were not paid within the agreed payment period.
  
- Statements (ie a tick box)
  - whether suppliers are offered e-invoicing;
  - whether supply chain financing is available to suppliers;
  - whether the business' practices and policies cover deducting sums from payments as a charge for remaining on a supplier's list;
  - whether the business is a member of a payment code and the name of the code.

This information must be published through an online service provided on GOV.UK and will be publicly available for contracting authorities to search, for example, to verify any self-declaration by a bidder about how quickly it pays its suppliers. It is a criminal offence if a business fails to publish a report containing the necessary information within the specified filing period of 30 days. Anyone who knowingly publishes a report which is misleading, false or deceptive, commits a criminal offence.

The Prompt Payment Code sets standards for payment practices between organisations and their suppliers. It is a voluntary code of practice for businesses, administered by the Chartered Institute of Credit Management (CICM) on behalf of BEIS. Signatories to the code undertake to pay suppliers within a maximum of 60 days (met by paying 95% of undisputed invoices unless there are exceptional circumstances), and to work towards adopting 30 days as the norm.

The Government proposes that paying 95% of undisputed invoices within 60 days, over two consecutive six month periods, is an appropriate benchmark of payment performance.

The Government recognises that not all suppliers will be covered by the payment reporting requirement or will be signatories to the Prompt Payment Code. No bidder should be disadvantaged in these circumstances.

In addition, this policy should not disadvantage a new economic operator that reasonably does not have previous payment performance that could be taken into account. And if a consortium or separate legal entity such as a Special Purpose Vehicle had been created to bid, then the contracting authority would need to consider the constituent members and take account of their conduct and evidence of technical and professional ability where relevant.

***Question 3: Do you agree that failure to pay 95% of payments within 60 days over two consecutive six month periods is an appropriate benchmark of payment performance? Are there other benchmarks that should be considered?***

### **Financial threshold to apply the measure**

The Government proposes using contract value at an appropriate threshold for application of this measure to ensure it is targeted and proportionate.

We have undertaken analysis to identify an appropriate level at which to set this financial threshold. This suggests that £5 million per annum per contract (rather than total contract value) means the contract would likely involve a supply chain element and therefore the use of subcontractors, helping to ensure the policy would be relevant to such contracts. It also assesses contracts by considering their value, rather than the size of the supplier carrying them out. We believe this would support a consistent application of the measure across all suppliers.

***Question 4: Do you agree that applying this measure to contracts valued above £5 million per year is an appropriate threshold? If not, what threshold should apply and why?***

### **Other measures**

We are interested in hearing about proposals that could be delivered through central government procurement to support the Government's overarching policy objective of fostering a culture of prompt payment across the economy.

The Government encourages businesses to report poor payment practice and instances of late payment in public sector contracts in breach of contract terms, including late payment in the supply chain, to its Mystery Shopper service. Mystery Shopper will then investigate.

But we know subcontractors on public contracts are often nervous about escalating complaints when they experience payment issues with a prime supplier and that they often do not know how to contact the contracting authority. It might be more powerful for subcontractors to be able to raise

concerns with a contracting authority and for prime suppliers to be required (through an appropriate contract condition) to provide their contact details.

***Question 5: Would there be benefit in giving subcontractors greater access to the contracting authority (as described above) to make them aware of significant payment issues?***