Excessive Payment Terms in Public Sector Supply Chains

A question was raised regarding a supplier that has been offered a subcontracting opportunity but is being required to accept payment terms of up to 120 days.

There are a number of practical steps that suppliers may wish to consider.

Raise the issue through the Public Procurement Review Service (PPRS)

Suppliers can report concerns regarding poor procurement practice, contract management issues and late payment through the Cabinet Office's Public Procurement Review Service (PPRS), which forms part of the Procurement Compliance & Oversight function.

Further information can be found here:

https://www.gov.uk/guidance/procurement-compliance-oversight

The PPRS investigates concerns raised by suppliers and can make recommendations to contracting authorities. It also handles cases involving late payment of valid and undisputed invoices.

However, suppliers should be realistic about the outcome. Such complaints processes are unlikely to provide an immediate remedy to a live commercial negotiation and may take time to influence behaviour. They should be viewed as part of a wider strategy rather than a quick solution to an immediate cashflow problem.

Consider the commercial reality

For many SMEs, the immediate question is whether the opportunity is commercially worthwhile despite the payment terms. In some cases, there may be little practical choice if participation in the supply chain is strategically important. A contract with difficult payment terms may still be preferable to no contract at all, particularly where it provides access to a major customer, valuable experience or future opportunities.

This is often a classic "bird in the hand" decision and suppliers should weigh the cashflow impact against the wider commercial benefits.

Calculate the true cost of the payment terms

Before accepting extended payment periods, suppliers should calculate the actual financial impact on their business. A contract that appears profitable on paper can become significantly less attractive when the costs of financing, overdrafts, invoice discounting or additional working capital are taken into account.

Understanding the true cost of waiting 120 days for payment provides a much stronger basis for negotiation. Rather than simply arguing that the terms are unreasonable, suppliers can explain the measurable impact on pricing, cashflow and delivery risk. In some cases, this analysis may support a request for shorter payment terms, staged payments, mobilisation payments or revised pricing.

Suppliers should also consider the wider risks associated with delayed payment, including increased exposure to changes in scope, contract disputes, inflation and the financial health of the customer. The longer the payment period, the greater the working capital burden being carried by the supplier.

Understand the role of Payment Spot Checks

For contracts awarded under the Procurement Act 2023, contracting authorities may include provisions requiring prime contractors to demonstrate that they are paying subcontractors in accordance with the government's expectations on prompt payment.

The Cabinet Office's Payment Spot Checks Policy Note (PPN 021) provides a mechanism through which contracting authorities can examine payment practices within the supply chain and seek evidence of compliance from their suppliers.

Further information can be found here:

https://www.gov.uk/government/publications/ppn-021-payment-spot-checks-in-public-sub-contracts

This means that payment practices are no longer viewed solely as a matter between a prime contractor and its suppliers. Where the relevant provisions have been incorporated into a Procurement Act 2023 contract, contracting authorities may take an interest where there is evidence of poor or unreasonable payment behaviour within the supply chain.

It is also worth remembering that many public procurements include commitments relating to SME participation, social value, responsible business conduct and supply chain management. Contracting authorities may reasonably question whether very long payment terms support those commitments in practice.

Suppliers should therefore review the prime contract requirements where possible. If payment spot check provisions apply, concerns raised by subcontractors may be of interest to the contracting authority as part of its ongoing contract management activities.

Engage carefully with the contracting authority

There have been occasions where contracting authorities have become aware of problematic supply chain practices through direct engagement with subcontractors. However, suppliers should proceed carefully.

Whilst raising concerns may prompt questions from the authority about why extended payment terms are being imposed, it can also risk damaging the relationship with the prime contractor. Suppliers should therefore consider both the potential benefits and the commercial consequences before escalating concerns.

A sensible first step may be to seek clarification from the prime contractor itself. Understanding the reason for the extended payment terms may reveal whether they are driven by genuine project requirements, internal processes or simply established commercial practice.

Where concerns remain, suppliers may wish to ask whether the contracting authority is aware of the payment arrangements being applied within its supply chain and whether those arrangements are consistent with the authority's expectations and contractual requirements.

Key Message

Suppliers facing excessive payment terms have several options available, including raising concerns through government channels and drawing attention to the issue through contracting authority oversight mechanisms. However, the decision should be taken in the context of the commercial opportunity, the importance of the relationship and the practical likelihood of achieving a change in behaviour.

Ultimately, suppliers should make a conscious commercial decision. Some opportunities may justify accepting difficult payment terms in the short term, while others may expose the business to an unacceptable level of cashflow risk. Understanding the true financial impact is often the first and most important step.

The fact that a large contractor can impose 120-day payment terms does not necessarily mean it should. Increasingly, contracting authorities are taking an interest in whether the behaviour of their supply chains reflects the commitments made during the procurement process and supports a healthy and sustainable supplier market.

For many suppliers, the most effective approach is often to combine commercial pragmatism with a clear understanding of the mechanisms available to challenge poor practice. Knowing when to accept a position, when to negotiate and when to escalate is an important part of operating successfully within public sector supply chains.

The reference to PPRS reflects the current Cabinet Office structure for supplier complaints and late payment issues under Procurement Compliance & Oversight. The service investigates supplier complaints and late-payment matters and can escalate systemic concerns where appropriate. (GOV.UK)

Finally, of course, is the MODs own Office for Small Business and they said during the meeting that they were starting to investigate this type of thing and putting in a meessag to them is of value.