

1. Executive Summary

Raymond Chabot Grant Thornton (RCGT) was mandated by the *Coalition against payment delays in the construction industry* (the “Coalition”) to carry out a study on the issue of payment delays in the construction industry.

The Coalition, representing a group of more than 20 associations involved in the Quebec construction industry, is concerned about the impacts of late payments on their respective members.

The construction industry is characterized by a high number of stakeholders for a single construction project: clients, general contractor, subcontractors, sub-subcontractors, etc. A construction project can often be seen as a multi-tiered stakeholder pyramid, with payments passing from one tier to another. Unwarranted payment delays have a multiplier effect in this payment chain and cause cash flow issues for many players, particularly those at the bottom of the pyramid who often serve as a buffer zone when delays occur. However, these same companies must pay certain costs promptly in order to be paid themselves (CCQ, Department of Revenue, wages, CSST, etc., to obtain the necessary certificates of compliance to trigger a payment) and this puts tremendous pressure on their cash assets. If they are not paid on time, these companies and their suppliers are the ones who feel the pinch.

Depending on their position in the payment pyramid, companies are at the mercy of stakeholders in the payment chain who can manipulate this system, which creates inequity in the construction industry. Companies that suffer the negative consequences of this system can be pushed to the point of bankruptcy depending on the length of delays and the number of construction sites they are operating on simultaneously.

The consultations and survey conducted as part of the study helped to identify the main causes of payment delays in the Quebec construction industry:

- Delays in the release of holdbacks;
- Failure to respect contract payment clauses;
- Administrative red tape required by clients;
- Delays in the approval of changes (changes orders);
- Payment authorizations by consultants.

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Impact Study on Payment Delays in the Quebec Construction Industry

Furthermore, the analysis of the data gathered during the study enabled us to assess the economic impacts of payment delays on the Quebec construction industry. The impacts identified, including quantifiable economic and other impacts on Quebec, are as follows:

- Cash flow management:
 - an annual sum of more than \$7.2 billion that companies are being deprived of beyond the usual payment period of 30 days, representing nearly 15% of all construction expenses;
 - loss of potential annual return on fixed capital in accounts receivable beyond the usual period is more than \$709 M;
- Financing costs: interest charges from accounts receivable beyond 30 days account for more than \$137 M annually;
- Company productivity: loss in productivity due to late payment recovery representing more than \$132 M annually;
- Competition within the construction industry: additional costs included in bid prices are close to \$25 M annually;
- Delays in payment to suppliers (i.e., “pay-when-paid”);
- Limitation in the number of contracts companies can bid on;
- Limited growth of businesses.

The total quantifiable impact is in excess of \$1 billion annually.

Moreover, in the past several years, a number of laws have been adopted throughout the world (United States, European Union, United Kingdom, etc.) to regulate payment delays in the construction industry. It seems that laws alone do not solve the overall problem, but they do help to shorten payment delays. The lessons learned based on the experience of other countries makes it possible to put forward recommendations for ways to reduce payment delays in the Quebec construction industry, namely:

- Consultation with stakeholders;
- Strict legal framework;
- Measures that are both punitive and incentive;
- Establishing legal procedures that foster a quicker, less costly and more effective resolution in the case of breaches to rules;
- The government must set a good example;
- Consideration of factors causing payment delays that cannot be resolved by simply applying prompt payment legislation.

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It is in this context that the Coalition launched a joint reflection process on the parameters proposed for dealing with payment delays, based on the results of this study.

The aim was to conduct a serious exercise and determine to what extent the proposals put forward could reduce current payment delays in the Quebec construction industry. The exercise demonstrated that the proposed parameters would be valid and would have positive economic impacts.

The key parameters proposed are prescribed timeframes for monthly payments and payment of holdbacks, the possibility of suspending work when monthly payments are late (going as far as terminating the contract) and implementing a stakeholder-decision maker model for the prompt resolution of disputes.

The fundamental impacts of the proposed parameters are:

- Better balance of power among stakeholders;
- Shorter timeframes for the approval of progress of work and payment authorizations;
- Decrease in the value and age of accounts receivable;
- Decreased use of line of credit;
- Reduction in project costs.

The quantifiable positive economic impact resulting from the application of the proposed parameters was evaluated at more than \$448 M. Another proposed parameter that consists of implementing the stakeholder-decision maker model for dispute resolution would also have a considerable positive impact although not easily quantifiable at this stage.

Factor	Economic impact
Negative economic impact	(\$1,002,884,190)
Portion excluded from the scope of the proposed parameters	\$416,927,224
Positive economic impact of the proposed parameters	\$448,124,883
Residual economic impact	(\$137,976,438)