

Suppliers' Financial Stability

What LUPC does to help mitigate the risk of supplier insolvency

LUPC takes the issue of supplier solvency very seriously. Assessing the financial standing and capability of a supplier is a key factor in the supplier selection and procurement process, and it is equally important to monitor financial stability in managing the supplier post-award.

That said, Members are reminded that it is their own responsibility to protect their own interests in the light of their individual sensitivity to the risk of key supplier insolvency. Full Members have free access to the Creditsafe service as a key Member benefit.

What we do at the procurement stage

LUPC uses the service offered by Creditsafe in order to monitor the financial stability and the risk of failure of all current suppliers. Credit rating is not, however, employed in the supplier selection process as the undisclosed algorithms employed by agencies such as Creditsafe may contravene transparency requirements.

Instead, a combination of the following information (a minimum of two of these options) is used in the process:

- Comparative industry-specific data, such as 'acid-test' ratio figures, allowing a lower-quartile or some other cut-off to be employed;
- Bidders' latest filed accounts for the last two years, remembering that this can give an outdated view. A satisfactory explanation shall be sought if a bidder has not yet filed accounts with Companies House more than 9 months after the accounting period;
- Bidders' business forecasts including budget planning for both the current and the following year; and/or
- The bidder's most recent management accounts.

Care is also be taken to assess and understand each agreement or contract for specific risks, e.g. where advance payments may be customary. In such cases the risks are set out for Members clearly in the Buyers' Guide for the agreement or contract, together with measures available to Members to mitigate such risks, e.g. a Parent Company Guarantee, a Banker's Guarantee or escrow account.

Assessing and monitoring the financial standing and capability of a *parent company* may be necessary to substantiate the 'true' standing of a supplier. Care is taken to cover risks in these instances with the use of appropriate safeguards such as a Parent Company Guarantee.

The credit rating for each 'successful' supplier is then reviewed prior to the 'standstill' period to check that it is advisable to proceed with the award. This rating, at that time, is then used as the basis for future monitoring.

What we do during the term of the agreement

LUPC also uses the Creditsafe service in order to monitor the financial stability and the risk of failure of all suppliers. In order to ensure that the service is used to its full potential, all our suppliers are monitored on a regular basis.

The Creditsafe service includes a *Risk Tracker* facility. This means our contracts professionals receive instant notifications when things change - email alerts are generated if any of the default criteria are triggered, i.e.:

- Any change in credit rating
- Any change in credit limit
- Changes in company status
- Media Search
- County Court Judgement added
- Directors' details changed
- Writ added.

Our contracts professionals also ensure that similar arrangements are in place such that suppliers on agreements in their portfolios led by other consortia (including the Crown Commercial Service) are also monitored.

In the event that a supplier:

- Suffers a drop in credit rating by 30 points or more; or
- Suffers a drop in credit rating to below 30 ("high risk"); or
- May be indicated as being in potential financial difficulty by substantive information received from another credible source;

then the Senior Contracts Manager for the category will contact the supplier to identify the nature of the risk:

- Where that risk is identified as 'short term' and supporting financial information is provided by the supplier, then monitoring will continue without further action unless matters deteriorate.
- Where that risk is identified as 'medium term', then the Senior Contracts Manager will inform the Director, who will decide an appropriate course of action, which may include advising Members and other consortia. The Senior Contracts Manager shall liaise closely with the supplier to maintain communication and obtain regular updates.
- Where that risk is identified as 'immediate' then the Senior Contracts Manager will inform the Director, who will decide an appropriate course of action, which will include advising Members and other consortia. The Senior Contracts Manager will liaise closely with the supplier to maintain communication and obtain regular updates.

In all these cases, the Senior Contracts Manager will also use search tools such as Google News to obtain wider information available concerning any matter indicating a potential financial difficulty for a supplier.

Members are also be invited to report issues and/or rumours to LUPC about suppliers, on a confidential basis.

What Members need to remember

LUPC's purpose is to help our Members obtain better value from their procurement of goods and services. In doing this, we arrange framework agreements and contracts for goods and services so that Members can contract with suppliers without each going through the complexities and costs of a full tender process.

It is important that Members remember that the use of any LUPC framework agreement or contract to acquire goods or services is neither obligatory nor exclusive. Where special arrangements to protect Members from supplier insolvency are made, then these will be set out in the Buyers Guide for that agreement.

We particularly recommend that Members seek their own legal advice:

- before making advance payments to suppliers; and
- if they negotiate their own contractual terms rather than utilise the model terms in the agreement.