

**Manchester City Council
Report for Information**

Report to: Resources and Governance Scrutiny Committee – 6 October 2020

Subject: Steps being taken to mitigate the risk of supplier failure

Report of: Deputy Chief Executive and City Treasurer

Summary

This report outlines the steps normally taken by the Council to mitigate the risk of supplier failure for major capital projects and larger revenue contracts and the additional measures that have been in operation due to the increased pressure on suppliers as a result of the Covid-19 pandemic.

Recommendations

The Scrutiny Committee is asked to note the contents of the report.

Wards Affected: All

Environmental Impact Assessment - the impact of the issues addressed in this report on achieving the zero-carbon target for the city
Resilience of the Council's suppliers to continue to contribute towards achieving carbon reduction strategies

Our Manchester Strategy outcomes	Summary of how this report aligns to the OMS
A thriving and sustainable city: supporting a diverse and distinctive economy that creates jobs and opportunities	Resilience of suppliers has a direct effect on employment opportunities given that over 60% of the Council's spend is with Local companies.
A highly skilled city: world class and home grown talent sustaining the city's economic success	Resilience of suppliers is key to providing job opportunities for local residents
A progressive and equitable city: making a positive contribution by unlocking the potential of our communities	Contribution of suppliers to the Council's Social Value principles provides significant support to communities.
A liveable and low carbon city: a destination of choice to live, visit, work	Suppliers selected through robust procurement practices are expected to deliver against low carbon targets - if suppliers are adversely impacted, replacement suppliers may not

	provide similar commitments
A connected city: world class infrastructure and connectivity to drive growth	

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Background documents (available for public inspection):

Not applicable.

1.0 Introduction

- 1.1 This report outlines the various measures that are implemented to safeguard the council against the consequences of supplier failure in major capital projects and for significant revenue contracts.
- 1.2 An additional emphasis has been placed on mitigating supplier failure as a result of the Covid-19 pandemic and several measures have been taken in accordance with government procurement guidance and supplementary to the national Coronavirus Job Retention Scheme.
- 1.3 Whilst the emphasis on high value contracts is noted, the measures outlined in the report also apply to contracts that may have a low overall spend but carry a high risk in relation to an interruption to a service through supplier failure, for example in Social Care or Children's Services where safeguarding is an issue.

2.0 Background

- 2.1 Whilst the Council makes every effort to ensure due diligence and the robustness of suppliers to undertake contracts, there will be instances of supplier failure whilst working on council contracts. Over the last two years the stability of the construction market, in particular, has been significantly challenged and the Council has been affected. The most significant recent instance was in March 2019 when Dawnus went into administration whilst working on the Manchester and Salford Inner Relief Road.
- 2.2 In the period since this incident, there have also been other failures within the construction sector with, for example, Cruden Construction appointing administrators in July this year after having been awarded two schemes by the Council at Ghyl Head and Mauldeth Rd Primary School via the North West Construction Hub Framework.
- 2.3 The Procurement Regulations provide for economic and financial standing to be assessed and taken into account to assess a company's financial capacity before a contract is let. These assessments are restricted to adequacy of turnover (limited to twice the annual value of the contract) and the ratio between assets and liabilities but these measures must be proportionate to the contract and "transparent, objective and non-discriminatory".
- 2.4 The current approach is to request details of recent accounts with submitted tender documents and, prior to awarding a contract, include carrying out an assessment of the supplier's credit rating. This applies whether the award is for a place on a framework or for an actual contract awarded as a standalone or as a call-off under a framework. The Council undertakes this assessment using Dun and Bradstreet credit reports which are considered the industry standard being drawn from a worldwide database of business records which are used widely to inform investment decisions. The Dun and Bradstreet subscription is around £8k pa.

- 2.5 A potential problem with this approach is that the credit rating can be based on accounts that relate to the previous financial year and may not provide a true reflection of the company's current trading position. In addition other factors that are not covered by the data collated by Dun and Bradstreet may affect a company's stability – for example, the financial stability of creditors. This is especially relevant given the current disruption created by the Covid-19 pandemic.
- 2.6 Following the Dawnus incident, a review was carried out into the approach to Due Diligence for significant contracts which concluded that a range of indicators should be used with key suppliers on an ongoing basis and not just at the point of award of a contract.
- 2.7 As part of the developing improved approach to Contract Management, the Integrated Commissioning and Procurement Unit has developed a system of categorisation for contracts based on how critical they are (Gold, Silver, Bronze) and how they are performing (Red, Amber, Green). This system helps to provide an initial guide as to which contracts may require more intensive financial scrutiny linked to risk rather than just value.
- 2.8 The Contract Management approach includes monitoring financial standing to varying standards according to the nature of the project, levels of risk, potential reputational and operational losses, value of contract and cost of remedial action plus the state of the market. This is in line with best practice generally and is advocated in the Government Commercial Function guidance on contract management.
- 2.9 Having identified the Critical contracts a range of tools are now in use to inform those involved in management of contracts about the financial stability and any specific risks relating to a key supplier. These include
- Industry related publications – e.g. Construction News and other bulletins published regularly (weekly or daily) and include information on how the specific market is performing, including for example details of significant contract awards or termination and therefore provide insight into whether a company is currently successful or otherwise.
 - “Category intelligence” picked up through professional networks, whether formal or informal, across GM and wider. This can provide anecdotal but reliable information from inside sources.
 - The AGMA Procurement Hub provides free access to the “FAME” database which is similar to Dun & Bradstreet but includes some wider determinants of a company's financial including recent contract awards and losses, changes of director, positive and negative press articles etc. The system provides a service which send “alerts” to users in relation to changes of status of any companies that are of interest and one of the Integrated Commissioning and Procurement team members has signed up to receive alerts for all suppliers that are considered key to the Council – for example, those with high risk contracts or that hold places on long term frameworks.

- The Cabinet Office's Government Commercial Function provides weekly Strategic Supplier bulletins on the principal suppliers in Business Process Outsourcing, ICT, Construction and Facilities Management, Professional Services and Telecoms. This provides additional market intelligence for these service areas and Integrated Commissioning and Procurement have advised client departments to subscribe to the weekly newsletters that are issued. The unit also monitors the bulletins each week and provides updates to other service units as relevant.

2.10 In response to the Covid-19 outbreak, the Integrated Commissioning and Procurement Unit has subscribed to an application "Company Watch" which, as well as providing information on a suppliers' financial position, provides an additional "Covid Scenario Forecast H-Score" which provides additional rating on how susceptible a supplier may be to issues created as a result of the pandemic. Again, alerts can be set that indicate when a company's rating changes and the Integrated Commissioning and Procurement Unit monitors key suppliers.

2.11 The subscription was taken out in July for a 3-month trial in which procurement, finance, capital programmes, highways and commercial governance service units have participated. If adopted, the system costs would be approx £7500 pa. The trial finishes at the end of September and the results will then be assessed.

3.0 Coronavirus related issues

3.1 As mentioned in paragraph 1.2, the Coronavirus pandemic has created an additional layer of risk in relation to supplier failure with many small and large companies adversely impacted.

3.2 In March 2020, the Cabinet Office issued a Procurement Policy (PPN) guidance note (PPN: 02/20) for public bodies regarding payment of suppliers to ensure service continuity during and after the coronavirus (COVID-19) outbreak. The guidance recommended that authorities:

- Urgently review their contract portfolio and inform suppliers who they believe are at risk that they will continue to be paid as normal (even if service delivery is disrupted or temporarily suspended) until at least the end of June.
- Put in place the most appropriate payment measures to support supplier cash flow; this might include a range of approaches such as forward ordering, payment in advance/prepayment, interim payments and payment on order (not receipt).
- If the contract involves payment by results then payment should be on the basis of previous invoices, for example the average monthly payment over the previous three months.
- Ensure invoices submitted by suppliers are paid immediately on receipt (reconciliation can take place

- 3.3 To qualify, suppliers should agree to act on an open book basis and make cost data available to the contracting authority during this period. Suppliers are also expected to continue to pay employees and flow down funding to their subcontractors.
- 3.4 These payments, in essence, amounted to councils being expected to pay suppliers in advance for goods and services with an expectation that unrecoverable costs would be reimbursed by the Treasury.
- 3.5 In June 2020, further guidance was issued that extended these arrangements until the end of October 2020. It was made clear in the revised guidance issued in June that suppliers in receipt of funding from other Coronavirus Job Retention Scheme support (eg where staff have been furloughed) would have this taken into account when support under the procurement guidance was taken up.
- 3.6 These “PPN arrangements” are currently under review by the Cabinet Office and not expected to be further extended.
- 3.7 Integrated Commissioning and Procurement provided guidance to all service units on these arrangements in March and again in June. The unit also established a centralised database for recording details of all arrangements made with suppliers under this initiative.
- 3.8 The Council has signed up to the “Prompt Payments Code” (a BEIS Standard) and commits to payment of any undisputed invoices within the terms set out in the contract which are typically within 30 days of receipt of the invoice. In 2019, BEIS appointed a “small business tsar” who reported that this is considered to be a strong contributory factor towards any supplier’s financial wellbeing, and that local authorities perform at a much higher level than private sector organisations against this standard.
- 3.9 One final point to note is that the Council recently established a Due Diligence Working Group with representation from Audit, Finance, Development and Shared Services that is reviewing current Due Diligence arrangements in respect suppliers, various partners and other organisations that are commercially involved with the council. The group was set up in March and is benchmarking our approach to due diligence with other similar councils as part of the review process.

4.0 Recommendations

- 4.1 The recommendations appear at the front of this report.