

Date: 4 July 2018

Item: TfL Management of Risk of Insolvency of Major Suppliers

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**This paper will be considered in public**

## **1 Background**

- 1.1 TfL spends approximately £5.8bn annually with third party suppliers and contractors who provide much of the infrastructure and services which TfL uses day to day. There are approximately 6,200 suppliers in the portfolio although a significant proportion of the spend (more than 76 per cent) is spent with a core group of 60 suppliers.
- 1.2 As part of TfL's recently launched Supplier Management Programme, which is part of TfL's wider supplier engagement activity, these suppliers are split into two core groups; Strategic (six suppliers) and Critical (54 suppliers). Strategic suppliers generally interface across a number of areas in the organisation and are typically high spend, complex service or product providers. Each Strategic supplier has a member of TfL's Executive Committee appointed to lead senior engagement with them.
- 1.3 A number of measures exist to assure visibility of the risk of financial failure and to implement appropriate contingency measures should a supplier failure occur.
- 1.4 The recent failure of Carillion plc, and subsequent media stories relating to other large outsource providers (i.e. Interserve, Capita) have led to an increasing focus on the measures in place to provide both assurance and contingency.
- 1.5 In the case of Carillion plc, TfL had a limited exposure having identified a particular financial risk emerging in the summer of 2017 and putting appropriate contingency arrangements in place.

## **2 Recommendation**

- 2.1 **The Committee is asked to note the paper.**

## **3 Assessing Third Party risk**

- 3.1 There are a number of measures which are in place to continually evaluate and assess the risk of supplier failure across our 60 core suppliers. These measures can be categorised as follows:
  - (a) financial assessment;
  - (b) negative press reviews;
  - (c) category management; and

- (d) ongoing supplier management.

### **Financial Assessment**

3.2 Financial assessments of suppliers are carried out through a number of stages in the commercial lifecycle:

- (a) all suppliers are checked for financial strength as part of the selection process. An assessment is made, depending on the role they are going to be performing and the subsequent risk profile appropriate for that activity. This means a number of suppliers do not pass the minimum criteria as defined in the initial selection process and are removed as a result;
- (b) ongoing financial strength analysis is carried out, including via Creditsafe, TfL's company reporting credit tool. A portfolio of our key suppliers on Creditsafe also alerts us to any changes in risk and credit score;
- (c) this process is supported by the internal circulation of other relevant credit rating information held on suppliers. We also monitor share price developments on an ongoing basis and significant share movements are flagged both internally and to the relevant supplier manager. These changes are notified to the Executive Committee through a quarterly supplier report. The supplier report also covers issues such as supplier performance, HSEQ performance and risk; and
- (d) through any of our procurement processes, supplier financial security is assessed which gives a "updated point in time" overview of the supplier's current position which can then be shared across multiple projects should any concerns be raised.

### **Negative Press**

3.3 As part of our overall view of supplier stability, we monitor press on an ongoing basis to get an understanding of how suppliers are performing outside TfL, which contracts they are winning and losing and what the potential impact of these changes might be. This is circulated in a periodic supplier bulletin, which might provide an early indication of any financial difficulty that a supplier might find themselves in. This is also supported by the circulation of news on the core suppliers from Bloomberg every day. Using this information, relevant Commercial teams are alerted to potential risks.

### **Category Management**

3.4 We have moved to a "Category Management" model which requires the team to deliver an increased expertise in the external market. This is useful both in improved management data, but also in broadening conversations with additional providers in the market to deliver a whole market view. This assists in providing views of overall market profitability and which suppliers are performing well. Equally, peer company discussions help to inform this debate further.

## **Supplier Management**

- 3.5 Each of our Strategic and Critical suppliers has a TfL lead who is responsible for the management of that relationship. These enable direct conversations with the supply chain. These have been used successfully across a number of suppliers recently to understand recovery business plans which can be tracked jointly in the future. This role is also responsible for tracking supplier performance on a quarterly basis. Performance dips can sometimes be a wider symptom of an issue within a supplier and so can be addressed accordingly.
- 3.6 Within the suppliers not captured under the Strategic or Critical supplier scheme (which is less than 10 per cent), we are currently assessing where we may have any single points of failure despite relatively low spend. This analysis is likely to take until the autumn of 2018 to be completed.

## **4 Contingency Planning**

- 4.1 Despite our best efforts, there will still be instances where a supplier may fail due to a number of different reasons outside of TfL's direct control. Our Supplier Strategy team makes an assessment of suppliers and the approach we have to contingency planning may be addressed in a number of different ways depending on some core circumstances. We think about potential supplier failures in the following ways:
- (a) non critical products or services for which there are many market alternatives;
  - (b) critical products or services for which there are many market alternatives;
  - (c) non critical products or services for which few market alternatives exist; and
  - (d) critical products or services for which few market alternatives exist.

Our approach to establishing contingency arrangements in each of these scenarios is different.

- 4.2 We review our existing supplier base along the following criteria in the table below, with a focus of activity on goods and services which are critical to the operation of the organisation.



- (b) **macroeconomic drivers:** A wider piece around the macro-economic drivers that could adversely affect our key suppliers. This exercise will look to review drivers such as Brexit, commodity prices, economic activity fluctuations, geopolitical influences etc.; and
- (c) **commercial guidance:** We are reviewing our existing Commercial Guidance on “Supplier Financial Checks and Dealing with Insolvency” to ensure that the guidance is up to date and robust enough to manage contingency planning.

## **Appendices to this report**

Appendix 1: Example of supplier report

## **Background papers**

None

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## Appendix 1: Example of Supplier Report

Supplier A		Overall Quarter Performance			TfL spend in YTD	Creditsafe Rating	Credit agency rating	Credit agency outlook
					£179m	61	Baa2	Stable
Contract Title	Val (£)	Comm Area	Delivery	Safety	Value	Responsible Procurement (RP)	Average Rating	
Contract 1	£121.0m	Surface Ops						
Contract 2	£35.0m	Surface Ops						
Contract 3	£23.0m	Surface Ops						