Economic and Financial Standing - Supplier Guide

NHS
Supply Chain

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What is EFS and Why is it Important?

Assessing and monitoring the economic and financial standing (EFS) of suppliers is about understanding the financial capacity of suppliers to perform a contract in order to safeguard supply. At NHS Supply Chain it is the term we use for the standard checks we undertake on a supplier's financial records at tender evaluation, confirmation of award and then as part of our continuous monitoring during the contract term.

We undertake EFS Assessments for the following reasons:

Improved resilience - by understanding supplier capacity to fulfil contractual agreements we can implement mitigation plans early to protect supply.

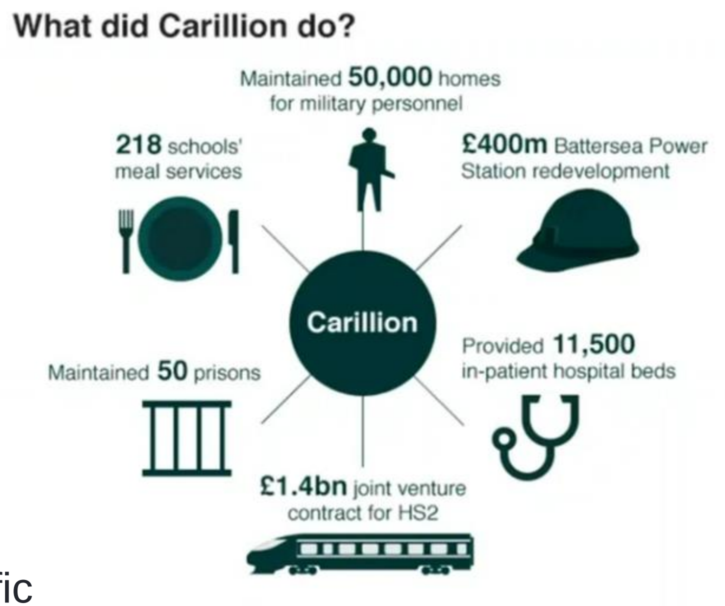
Regulatory compliance - as a public sector authority we are mandated to conduct through assessment and monitoring of our suppliers' financial stability (Procurement Act 2023).

Increased insight - the EFS assessments we undertake allow us to gain a better understanding of our suppliers' common ownership and structure.

Strengthened reputation - we are demonstrating to our customers that NHS Supply Chain is a safe route to market due to robust supplier assurance processes.

Overview of PPN03/24

In June 2023 the UK Cabinet Office published PPN 03/23 (later updated to PPN03/24) which revised the guidance on how public sector authorities should vet suppliers on the grounds of their Economic and Financial Standing. The underlying aim was to protect the public purse from instances such as Carillion who failed and were liquidated in 2018 holding multi million pound Government and other public sector contracts.



Did you know?

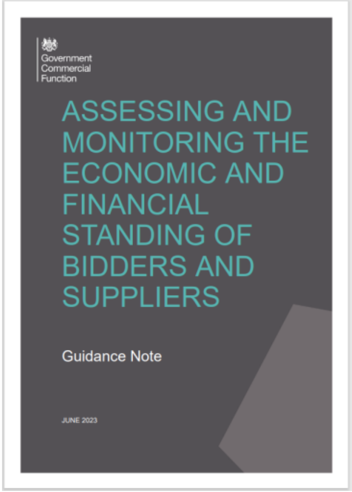
Reports suggested that the collapse of Carillion directly cost the tax payer £148 - £180 million but there were also far reaching impacts in terms of Carillion's supply chain, as well as additional costs to replace them with alternative suppliers.

PPN 03/24 has since been superseded by the Procurement Act 2023 Procurement Specific Questionnaire, however the guidance remains unchanged and details a number of standard checks to be conducted on a supplier at tender evaluation, confirmation of award and then continuously through the contract period to understand their financial capacity to perform the contract in order to safeguard supply.

We had already identified this issue in 2023 prior to our reorganisation, but the PPNs and the Procurement Act 2023 have now given guidance to what is considered best practice.

Overview of the Procurement Act 2023

- The Procurement Act 2023 asks all awarding authorities to undertake as a minimum a number or prescribed checks on the financial records of all our suppliers.
- They primarily test a suppliers
    - Profitability and levels of debt compared to profits.
    - Liquidity and solvency.
    - Ability to service their contractual commitments.



- While the guidance document provides suggested threshold requirements for the financial tests and ratios, we are able to formulate an adapted approach according to the size and nature of the contract, our market knowledge and to not be overly risk averse.
- The regulations also place a heavy emphasis on ongoing financial monitoring to enable early identification of possible problems and the opportunity to test contingency plans before they are needed.
- Monitoring should normally be performed in the first instance by a function or team that is independent of the day-to-day contract management role.
- Ongoing ‘alert’ systems should be established to monitor company announcements and other information sources.

What is NHS Supply Chain’s Approach?

The Supplier Performance and Risk team take primary responsibility for conducting EFS assessments, maintaining EFS records and managing a system of alerts that will highlight any associated issues. Category teams have on demand access to this information.

We will use the information provided as part of your tender submission to obtain an independent report on your organisation’s current financial standing from Dunn & Bradstreet (D&B). This report will include financial data filed at Companies House.

Based on the financial information obtained, a score is determined by applying the formulae detailed on the next slide. These ratios are aligned with the guidance notes to the Procurement Act 2023.

What is NHS Supply Chain's Approach?

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The assessment criteria used in this model explained in more detail:

Turnover Ratio to assess a bidder's reliance on NHS Supply Chain and ability to accommodate additional contracts.
Turnover Ratio = Bidder Annual Revenue / Transactional NHS Supply Chain Last NHS Financial Year

Net Debt to EBITDA Ratio measures entity's ability to service its debt. Low ratio indicates entity is better.
Net Debt to EBITDA ratio = Net Debt / EBITDA

Net interest Paid Cover Ratio measures how easily an entity can service interest on its debits out of its profits. Higher number indicates entity is better able to service interest on its debt.
Net interest paid cover = EBIT / Net Interest Paid

Acid Ratio measures entity's ability to meet its short-term liabilities as and when the they fall due. Low ratio may raise doubts over ability to meet liabilities as they fall due.
Acid Ratio = (Current Assets – Inventories) / Current Liabilities

Net Asset Value provides a basic view of whether an entity's assets exceed its liabilities. Hence overall solvency. Negative value may suggest the entity is less sustainable in event of performance deterioration.
Net Asset Value = Total Assets – Total Liabilities

In order to give a broader-based final outcome, the D&B Failure Score will be integrated into the overall assessment. The D&B Failure Score is designed to help predict a business's potential for failure. It uses a range of Dun & Bradstreet information, including financials, comparative financial ratios, payment trends, public filings and demographic data to provide predictive insight. We will take the D&B Failure Score (of 1 – 100) along with the financial ratio scores (as detailed above) to arrive at a combined final risk rating and score for your organisation.

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What is NHS Supply Chain's Approach?

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The score that each supplier obtains for each criterion is translated into a mark of between 0 and 2 for the criterion.

This is dependent on whether the score is above or below the benchmark for the criterion set - see the table showing 'Scoring Matrix' on this slide for details of the benchmark.

A maximum Score of 12 marks is available.

Test	Thresholds	Score
D&B Failure Score	>50	2
	30 to 50	1
	<30	0
Turnover Ratio	> 2.0	2
	1.5 to 2.0	1
	< 1,5	0
Net Debt/EBITDA	< 2.5	2
	2.5 to 3.5	1
	> 3.5	0
Interest Cover	> 4.0	2
	2.5 to 4.0	1
	< 2.5	0
Acid Ratio	> 0.8	2
	0.7 to 0.8	1
	< 0.7	0
Net Worth	> £0	2
	< £0	0

What is NHS Supply Chain's Approach?

Each supplier's mark out of 12 is then converted into a risk rating, as detailed on this slide.

For the majority of our framework awards, there is no intention to exclude a supplier on the grounds of their financial standing, instead we will take a risk-based approach to identify areas of concern so that as a business we make an informed decision and mitigate any risks to protect supply.

Awarded suppliers with moderate to high-risk scores may not be invited to participate in any competition or other activity under the framework agreement if this presents an unacceptable level of risk of the Applicant not being able to discharge its obligations, or to meet its liabilities, under the Agreement or call-off contract.

The Performance and Risk Team will maintain this data ensuring it is updated at least once a year and when new financial data or insight becomes available.

Any high-risk cases will be escalated to the Category teams.

Score	Risk Rating	Indications of Financial Score and Risk Rating*
11+	Low	Strong condition with fundamentally strong financial standing across all metrics Based on the predicted risk of failure: high likelihood of continued operations
8-10	Low - Moderate	Stable condition with no major financial issues across assessed metrics Based on the predicted risk of failure: high likelihood of continued operations
6-7	Moderate	Stable condition with some risks across key financial metrics Based in the predicted risk of failure: continued operations probable
3-5	Moderate - High	Stability risk across multiple financial metrics Based on the predicted risk of failure: potential for operational failure
0-2	High	No financial information provided, or a stability risk across most or all financial metrics Based on the predicted risk of failure: going concern of operational fulfilment

I Have Been Rated as High Risk - What Should I Do?

- The Supplier Performance and Risk team will advise if any specific information is required, and if so, the Category Manager, or Supplier Relationship Manger for suppliers who are part of the formal SRM programme, will contact you to facilitate this.

- Having additional information may mean that the risk rating can be reevaluated to a more acceptable level which may allow you to continue accessing all competitive activities.

- Some examples of the types of additional information / actions that might be asked for include:
    - Provision of a full set of latest Financial Accounts.
    - Insight into the levels of safety stock you hold in your organisation to protect the continuity of supply in the short term, which may need to be increased to provide us with additional confidence.
    - Visibility of your KPIs / metric reporting for transparency and early insight of challenges / your mitigation plans.
    - Visibility of your Business Continuity Plans, or an ask to create one if not currently in place.
    - Enhanced audit access in collaboration with your key process owners.

Parent Company Guarantees

NHS Supply Chain

NHS Supply Chain reserves the right to request the provision of a Parent Company Guarantee (PCG), or similar surety, from any awarded supplier under the following circumstances:

1. The bidding entity is newly formed, has been trading for less than 12 months, and is therefore unable to provide its first year of accounts records.
2. The bidding entity has been trading for any period of time, but its financial year-end Balance Sheet records indicate that it is insolvent (liabilities exceed assets).
3. The bidding entity is solvent or insolvent but relies on the financial support of another entity.

Provision of a Parent Company Guarantee would not be a condition of award at the point of tender.

However, we will monitor any risk presented as part of active contract management. If a PCG is deemed appropriate but not provided, your EFS risk rating would remain high, and customers would be informed that a risk to continuity of supply is present. You would also be unable to partake in any competition resulting in a commitment from customers.

Parent Company Guarantees

In the event that there is no parent company ownership structure, alternative surety can be provided. This includes, but is not limited to:

- Guarantees by a third party related to the business, for example another company that is related to, but does not control, the bidding entity.
- Director’s Personal Guarantees.
- Bank Guarantee or a similar “bond” from a suitable financial institution.

Any Guarantee provided would be contract-specific and would not extend to all awards held by you across other framework agreements.

Contact Us

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