22 May 2019

White Paper Public Procurement Conference 2019
Distressed Contractors and the Procurement Regulations

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250 YEARS

Introduction

- The Questions:
  - Distressed Contractors:
    - *What are the warning signs of a contractor in financial distress?*
    - *What can you actively do to ensure that your service is continued and delivered within the rules?*

Warning signs of a Contractor in Distress

- Main Contract level:
  - poor performance and late delivery at main contract level
  - requests for early or advance payments
  - Triggering of financial distress provisions
  - high or increased levels of staff turnover
  - late delivery of statutory accounts

Warning signs of a Contractor in Distress

- Supply Chain issues:
  - late delivery or requests for payment up front
  - requests for Off Site Materials/Supply Agreements with suppliers
- Adverse press coverage, negative financials and changing ratings
  - clearly not definitive but can be an early warning

What can you do at this stage?

- Have you received all relevant contractual deliverables e.g.
  - Collateral Warranties and Direct Agreements
  - Product Guarantees
  - Service Keys for Software
  - Are any documents stored and available in Escrow (e.g. software codes or materials design information)

- Do you have access to Performance Security e.g.
  - Parent Company Guarantees
  - Bonds

Actively ensuring continuing service delivery within the rules

- Insolvency prior to Contract Award:
  - MT Højgaard/Zublin Case
  - Some practical considerations

- Insolvency during Contract Term:
  - Consider existing contractual protections and provisions
  - What do the Procurement Regulations allow?

Insolvency prior to contract award

- What if insolvency occurs during the tender process?

- Case of MT Højgaard A/S and Zublin A/S v Banedanmark (C-396/14)
  - Consortium member entered insolvency
  - Remaining Consortium member was entitled to continue….
    - provided that it alone still meets the requirements laid down by the Contracting Entity; and
    - the continuation of the single entity does not place others at a competitive disadvantage

Insolvency prior to contract award

- Some practical considerations around changes to consortia prior to contract award:
  - Can the single bidder meet the financial requirements of your ESPD process?
  - Can the single bidder meet the technical requirements of the ESPD process?
  - Are any key individuals or teams pertinent to the technical evaluation lost as a result of the change?
  - Including a right to rerun the ESPD in your procurement documentation

Insolvency during the term of the Contract

- Some things to consider in advance of insolvency:

  – Does the contract contain provisions around insolvency:
    - What is the definition of insolvency and when does it bite?
    - Does insolvency trigger an automatic right to terminate?
    - Do the payment obligations cease on Insolvency?

  – Is it the counterparty to the contract that is insolvent or is it another group entity?

Insolvency during the term of the Contract

- Once insolvency occurs:
  - Ensuring service continuity is usually the prime consideration.
  - Can the services be taken back in house (even in the short term)?
  - If not do you have appropriate termination or step in rights and can you call on Performance Securities?
  - Are there Funders involved who may have prior ranking rights in an insolvency scenario (e.g. Direct Agreements pursuant to PPP Contracts)

Insolvency during the term of the Contract

- Ensuring continuity - what do the Procurement Regulations allow?

  - Regulation 72(1)(d) (Modification of contracts during their term):

    "(d) where a new contractor replaces one to which the contracting authority had initially awarded the contract or framework as a consequence of—

    (i) an unequivocal review clause or option in conformity with sub-paragraph (a); or

    (ii) complete or partial succession into the position of the initial contractor, following corporate restructuring, including takeover, merger, acquisition or insolvency, by another economic operator that fulfils the criteria for qualitative selection initially established, provided that this does not entail other substantial modifications to the contract or framework and is not aimed at circumventing the application of this Part;"

Insolvency during the term of the Contract

- Considering the regulation further – there are three key strands:
  - Change in contractor has to follow a corporate restructuring, including takeover, merger, acquisition or insolvency (insolvency is specifically mentioned)
  - The new contractor must fulfil the criteria for qualitative selection from the original procurement, therefore an ESPD or similar process must be undertaken; and
  - There must be no other substantial modifications to the contract
- The Authority would need to be careful that all three limbs are met. Be wary of incoming new contractors looking to alter the risk profile of the contract due to the urgency of the requirement.

Insolvency during the term of the Contract

- Are there any other options under the Regulations?
  - Below threshold contracts?
  - If above threshold, could you use the negotiated procedure without prior publication?

    (1) A contracting authority may award a public contract following negotiated procedure without prior publication of a contract notice or prior information notice in any of the following cases— […]

    (c) where (but only if it is strictly necessary) for reasons of extreme urgency brought about by events unforeseeable by the contracting authority, the time limits for open procedure, restricted procedure or competitive procedure with negotiation cannot be complied with.

Insolvency during the term of the Contract

- Are there any other options?

  - For the purposes of Regulation 33(1)(c) reasons cannot be attributable to the contracting authority

  - The insolvency would also need to have been unforeseeable, and even then Authority would be prudent to consider what action is proportionate in the circumstances e.g.
    - If it is a new contract what is the value and are you entering into a short term contract to give you sufficient time to run a new fully compliant procurement?
    - Are you novating existing contracts and if so, what is the unexpired term and are any modifications required?

Questions?

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