Learning legacy

Lessons learned from the London 2012 Games construction project

Supply Chain Management – Insolvency Management

Abstract

The London 2012 Olympic and Paralympic Games was a critical, constrained and immovable deadline and hence, managing risk was essential, particularly in the supply chain where supplier insolvency can cause significant delays. Therefore, insolvency management was a key part of the Olympic Delivery Authority’s (ODA’s) Supply Chain Management (SCM) strategy.

The SCM strategy was specifically developed to positively influence the delivery of a sustainable 2012 Games and a legacy for East London and the South East beyond 2012. The approach ensured that both horizontal and vertical supply chain dimensions were managed to improve efficiencies and facilitate an integrated and collaborative approach to delivery.

However, at the start of 2009, and in response to the effect of the Credit Crunch within the UK and wider markets, SCM’s remit took on additional emphasis – to manage the potential risk of supplier insolvency.

While an active approach to managing supplier risks was being employed through industry-leading procurement and SCM best practice, the ODA required further assurance and mitigation measures to both understand these emerging risks and their potential impact. In response, the SCM team implemented processes to reduce the impact of contractor insolvency to the programme, and these are outlined in this case study.

Over £640 million of supplier risk was either removed or mitigated from the construction programme. Forty-three supplier insolvencies were avoided with zero impact, and while 11 were realised, their impact was minimised and managed through decisive early actions of the integrated ODA, Delivery Partner and main contractors.

Without industry-leading supply chain management processes, the impact of supplier insolvency would have greatly affected the delivery of the London 2012 construction schedule.

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Introduction
This case study documents the ODA’s approach to avoid and mitigate the impact of supplier insolvency within the construction supply chain associated with the London 2012 construction programme. This includes those contracts procured by the ODA directly and also critical subcontract packages (where delay could affect any aspect of the Programme) procured through the ODA’s Tier One main contractors. However, lower tier, niche or specialist suppliers were also identified and monitored closely as part of the process.

To understand how this was achieved one must consider the original remit of the SCM strategy and team over the period 2006–08, that is ‘pre-recession’.

The ODA’s direct suppliers for construction and engineering packages of work comprised of approximately 150 Tier One contracts and 7,500 Tier Two contracts. Through the whole supply chain there were over 43,000 contracts placed to complete the ODA’s requirements.

A central ODA SCM team supported the procurement and award of Tier One contracts and the ongoing commercial and contract administration duties associated with their Tier One contractors’ critical supply chain.

The role of this team included establishing suitable supply chains and measuring and monitoring supplier capacity, capability and financial standing both during procurement and throughout contract delivery. Tier One delivery contracts tended to be with ‘main contractors’ who coordinated and subcontracted the supply and installation of works; ‘physical delivery’ generally occurred at Tier Two and below.

The SCM strategy was specifically developed to positively influence the delivery of a sustainable 2012 Games and a legacy for East London and the South East beyond 2012. The approach ensured that both horizontal and vertical supply chain dimensions were managed to improve efficiencies and facilitate an integrated and collaborative approach to delivery.

Activities were divided into three interdependent strands:
– Market Intelligence
– Delivering Sustainable Solutions;
and
– Improving Performance

43,000 Contracts placed through the whole supply chain to complete the ODA’s requirements.

Rakers were precast on site and once in place, formed the part of the stadium terracing upon which spectator’s seats were fixed, August 2008

a ‘Critical’ is a contract identified by the integrated ODA, CLM, Main Contractor team which can adversely impact upon the delivery of the programme budget, schedule or quality criteria.
The three-pronged strategy of lessening the chance of any surprises, delivering sustainable solutions and optimising performance played a key role towards ensuring the Games themselves are completed efficiently and that the investment made leaves a long-lasting legacy for many years to come.

To ensure that there were no surprises when it came to delivering the construction programme associated with the Games, the SCM team used detailed forecasting in the form of data gathering, planning and stakeholder engagement. It was essential that SCM engaged with industry and key stakeholders formally and informally at the earliest opportunity.

This ascertained the appetite and capacity of the market to supply the goods and services to the Games. Critically, this allowed the ODA to utilise market intelligence and feedback in developing their procurement strategies, design information, use of innovation and material specification to meet challenging sustainability targets to list a small number of examples.

Through early market engagement, SCM was able to optimise market responses from the most capable contractors (based on experience and financial strength) to forthcoming procurement notices.

At the start of 2009, and in response to the effect of the Credit Crunch within the UK and wider markets, SCM’s remit took on additional emphasis – to manage the potential risk of supplier insolvency. Note: SCM resources remained as the original remit required, however, the team took on supplementary monitoring and reporting functions to manage the programme insolvency risk.

With over 43,000 anticipated supply chain contracts required to deliver the Games programme, a number of supplier insolvencies were deemed inevitable under ‘normal economic conditions’. It was thought the UK recession would lead to an increased likelihood of insolvency in the construction supply chain and possible impact to the London 2012 programme. The most significant impact would be insolvency (or other financial trauma) within one of the critical elements of the construction and engineering supply chain, resulting in a significant delay to overall project/programme delivery combined with a consequential increase in budget.

While an active approach to managing supplier risks was being employed through industry-leading procurement and SCM best practice, the ODA required further assurance and mitigation measures to both understand these emerging risks and their potential impact. In response, the SCM team successfully implemented processes to reduce the impact of contractor insolvency to the programme, and these are outlined in this case study.

Early engagement with industry and key stakeholders helped ascertain the appetite and capacity to supply goods and services to the programme.

Building works showing new underground platform at Stratford Regional station
Methodology – SCM approach to supplier insolvency risk management

In the event of a supplier failure, the ODA identified three key risks that needed to be managed closely:

- **Schedule performance**: ensuring continuation and availability of key resources (including staff, plant, equipment and materials) meant that site works could progress with minimal overall delay, and recovery plans were instigated to deliver the original contract completion dates.

- **Cost impact**: made certain that in the event of supplier failure there was minimal overall cost impact. Such mitigating actions included (but this list is not exhaustive): full ownership rights protected for all materials purchased, Tier One contractors not overpaid for goods and services, and communications and negotiations with the appointed insolvency practitioners (Administrator) focused on the continual operation of site works as a priority.

- **Quality performance**: reduced quality performance of the works and limited contractual remedy for latent defects.

SCM’s approach had three steps. Figure 1 shows the activities carried out at each step of the process:

- **Prevention and protection** throughout the procurement selection processes
- **Awareness and planning** during the delivery phase
- **Recovery** and impact mitigation in the event of an insolvency

There was a risk that the UK recession would lead to an increased likelihood of insolvency in the construction supply chain.

Figure 1: Three-step process to supplier insolvency risk management
Procurement and supplier selection

The overall focus of Step 1 of the ODA's insolvency mitigation and recovery was to ensure that throughout the supply chain a rigorous process of selection and approval of Tier One and Tier Two (plus specialist suppliers where identified) contracts was in place, robust financial data was utilised to gauge and monitor the stability of the London 2012 supply chain, and that the necessary protection was contained within the supply chain contracts including New Engineering Contract – version 3 (NEC 3).

The ODA procurement process had a number of measures in place to ensure financially secure suppliers are selected and that appropriate safeguards were included in the contract. Principally, the ODA used NEC 3 (standard clauses and the accompanying 'Work Information' within part one of the Contract Data) which offered some protection for both their Tier One and Tier Two suppliers.

Supplier selection and Tier Two approvals

Under the terms of the NEC 3 contracts (including detail within part one of the Contract Data) that the ODA have executed with their Tier One suppliers, the Project Manager (CLM) had to approve all Tier Two contracts prior to award.

A check was also kept at programme level of the value of contracts placed across the programme with individual suppliers to limit the total exposure the ODA had to a single supplier. A limit of 30 per cent of turnover (capacity) was recommended by the Office of Government Commerce (OGC) and set as the default total maximum value of contracts for any individual supplier across the programme.

Suppliers bidding for work over this threshold were requested by the ODA to have a mitigation strategy in place stating how they would deliver in addition to existing (and pipeline) commitments.

Credit and financial checks were made prior to the engagement of suppliers.

Limit of turnover (capacity) recommended by the OGC as a default total maximum value of contracts for an individual supplier across the programme.
The D&B reports/indicators were also utilised during the delivery phase to monitor the ongoing financial stability of Tier One and critical Tier Two/Three suppliers and provide an early indication of the likely financial distress being experienced.

D&B financial indicators and collated trend data were used to facilitate discussion at project and programme level, and set mitigating actions in response to potential risk(s) if required.

The information from D&B enabled the SCM team to monitor critical suppliers and track changes in financial parameters that might indicate areas of concern. The following information was monitored by the SCM team on a daily basis:

- **Capacity**: of suppliers to deliver the contract based on the contract value as a proportion of turnover. Visibility was achieved across both the horizontal (programme-wide) and vertical (project-specific) dimensions of the London 2012 supply chain including the Athletes’ Village projects.

- **Tender status**: identified whether the supplier had been awarded the contract and if not, the ODA was able to inform the Tier One supplier of an unfavourable change in financial position and suggest alternatives where appropriate.

- **Lead time**: looked at the industry standard lead-in time for the package and tested it against the procurement programme.

The following D&B Risk Ratings\(^b\) were continually used to calculate a metric for the overall risk of failure for the critical contracts (suppliers):

- **Failure Score**: gave the likelihood that a company would cease operations without paying its creditors in the next 12 months. The score was marked out of 100 with a low score indicating a higher likelihood of ceasing operations. For example, a company with a score of 10 indicated that it was more likely to cease operations than 90 per cent of UK companies.

- **Risk Indicator**: linked directly to the Failure Score, segmenting all businesses into one of four broad categories as follows:
  - Minimal risk
  - Low risk
  - Above average risk
  - Significant risk.

- **Delinquency Score**: predicted the likelihood that a company would pay its bills in a severely delinquent manner based on the information held by D&B. A ‘severely delinquent firm’ was defined as a business with less than 75 per cent of its trade experiences paid in a satisfactory manner (prompt or within 30 days) and at least 10 per cent of its payments 90 days or more past due or one or more events classified as leading to failure.

- **Financial Strength**: based on the net worth of a company from the most recent financial information available.

A poor assessment score/rating using D&B ratings did not in itself mean a supplier would not be considered but it did give the opportunity for the ODA to obtain additional assurances by:

- undertaking a detailed financial audit of the company by the ODA (or its appointed advisors) to determine, in greater detail, the financial stability of the company;

- obtaining confirmation from the CFO/FD/bank/etc;

- requesting parent company guarantees, where applicable, if not already in place;

- requesting a performance bond if not already in place;

- requesting a material vesting certificate for key assets-manufactured products, such as structural steel and rebar for major venues and bridges, Velodrome external cladding (timber), precast concrete beams for the Aquatics Centre F10 pedestrian bridge, etc.

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\(^b\) A schedule of all current (contracted or prospective) Tier One and Tier Two critical suppliers was maintained, with D&B reports refreshed daily against selected parameters to alert the SCM team and by exception, to procurement and project management teams (approximately 3,000 suppliers). Ref Appendix A. Supplier Matrix template.
Critical packages and monitoring process
Some packages were more critical to the programme than others and not necessarily in proportion to cost.

Therefore, several other criteria were considered to define and identify critical packages on the programme including the:
- criticality of the package in relation to delay to the programme;
- supplier sits on the critical path of the programme and/or contract;
- specialisation of suppliers, such as: the number of alternatives and ease of replacement;
- use of proprietary systems and component suppliers with implications for technical performance or non-availability and the potential need for re-design;
- number of contracts engaged in across the programme including, where identifiable, throughout the supply chain;
- status of materials relative to the contract; and
- size and value of the contract and the value remaining to complete.

SCM maintained a central register of all critical packages which was continually updated as new contracts were awarded across the Park and Athletes’ Village (Tiers One, Two and below where relevant).

This register was also used to manage the financial stability and overall insolvency risk for each package with data updated on a daily basis (source data D&B).

Figure 2 sets out the steps of critical package selection during the Tier One procurement process, SCM monitoring and assurance/mitigation confirmation.
Accelerated buying and delivery to site of key components where availability was at risk reduced the potential impact of insolvency.

The resulting data obtained via the monitoring process was collated and input to the SCM Contractor Matrix. This document was dynamic and changed daily in response to the data alerts and emerging intelligence. The Contractor Matrix held extensive data containing information on 95 projects programme-wide. This represented over 2,900 lines by 42 columns of data – a total of 105,667 data elements (Ref. Appendix A. An extract from the Contractor Matrix).

SCM integrated their resource within the major contractor’s project teams to assist their respective procurement processes with a unique, Park-wide visibility of the collective supply chain (both vertical and horizontal) to identify potential opportunity and risk mitigation. Where supplier risks were identified, SCM were able to raise awareness of these and identify alternative suppliers for consideration that demonstrated available capacity or unbeknown specialisms, for example.

Step 2: Awareness, planning and risk reduction

Once a contract had been awarded, intelligence gathering, monitoring and contingency planning was carried out between the ODA, Delivery Partner and the Tier One main contractor to monitor the ongoing health of their critical Tier Two suppliers. It also focused on ensuring all intellectual property (IP) that the ODA had full rights to under the terms of the contract was secured, so that in the event of insolvency, minimal operational disruption occurred from the inability to progress site works. Key IP included (but was not limited to): drawings, method statements, key personnel, test plans, commissioning plans, etc.

A key focus was placed on reducing the impact of insolvency by identifying opportunities to accelerate buying and delivery to site of key components whose availability was at risk because of the economic climate. For example: SCM directly engaged with Tata Steel Europe (formerly Corus) in response to market reactions in 2008 that they were to reduce crude steel production in Europe by up to 20 per cent.

The project teams (including Tier One and Tier Two fabricators) accurately mapped and coordinated the delivery of structural and weathering steel requirements for major venues, structures, bridges and highways. As a result, Tata Steel Europe was able to identify available materials, create production schedules and deliver materials through the supply chain on a time critical or ‘priority’ basis. This activity also incorporated the requirements of the immediate neighbouring schemes (Athletes’ Village and Stratford Retail developments) and also considered major projects across the UK and Europe.

Steel cross beam for the Olympic Park Site. The ODA engaged with Tata Steel Europe following reports that they were to reduce crude steel production in Europe
Intelligence gathering and monitoring
As described previously, SCM used D&B reports to monitor the financial health of all construction and engineering Tier One main contractors and critical Tier Two suppliers pre-, during and post-contract.

The criteria and ratings listed in Step 1 were used to assess the financial stability of each supplier. The frequency with which the information was updated depended on the criticality of the contract, however, given the concerns associated with the economic climate, critical suppliers and packages were monitored daily, with relevant alerts escalated to ODA and Delivery Partner Executive teams (via the Delivery Partner Commercial Director).

Monthly risk and insolvency tracking meetings were held by the Executive team as an additional level of supplier assurance to identify possible trends in intelligence and performance.

Intelligence was also sought from other industry sources such as material and component suppliers, trade press and the workforce. This approach tended to be an ad hoc, but useful, source of information, however, it was very important that rumour and speculation were not encouraged.

The key indicators for Tier One and Two were reviewed on a weekly basis by SCM and alerts raised within the business if an increased risk of supplier insolvency occurred. On a monthly basis the overall trends were reviewed by the ODA Commercial and Procurement Board (part of the ODA’s governance structure).

Mapping of critical materials and intellectual property
A key element of being able to continue the works with minimum disruption and cost was the location and status of materials, supplies and sub-contracts. Through the contract the ODA had measures in place to ensure materials and supplies were vested and ownership clearly labelled to enable possession if needed. For example, these measures were successfully deployed for the securitisation of critical bridge components where the ODA took full ownership rights (through vesting and off-site material bonds) prior to delivery to the Games site.

The ODA and SCM undertook a review of all Tier One main contractors’ plans for insolvency and to assure its vesting and retention policies were being adhered to. Note: while ownership was established through vesting, immediate release of the asset was not, and additional measures may be required to ensure continued progress of the works.

Monthly risk and insolvency tracking meetings were held by the Executive team as an additional level of supplier assurance.

View of steel worker, working on steel prior to its transportation to the IBC from the Severfield Reeve steel works in Thirsk, North Yorkshire
Further measures were undertaken to ensure all critical IP which the ODA had full rights to under the contract was stored and easily accessible to the Delivery Partner.

The information that was collated and stored for all critical Tier One contracts included: drawings, method statements, construction methodology statements, test plans, commissioning plans, Tier Two collateral warranties, insurance arrangements (particularly Tier Two), key site staff, plant hire agreements, labour agency agreements, etc. The range of information was such that, in the event of insolvency, the ODA could instruct the Delivery Partner to step in as ‘contractor of last resort’ to minimise disruption to site progress from a lack of IP availability.

Advanced purchase of commodity components (risk reduction activity) In reducing the impact of insolvency on delivering the Park infrastructure, venue build programme and the Athletes’ Village the build was considered in two stages:
– Stage 1: off-site fabrication of systems and components (such as steel bridge sections, pipes, ducts, precast concrete sections, pumps, electrical equipment, seats);
– Stage 2: on-site installation, testing and commissioning of works.

The delivery of the Park build programme could have been severely impacted (both time and cost) from insolvencies to off-site component and system suppliers.

In such instances, significant delay could have occurred as a direct consequence of re-phasing assembly operations in factories or finding alternative capacity. In addition, Administrators might impose a price premium on stock supplies in an attempt to secure optimum value for their shareholders and creditors, impose additional costs for ongoing facility production, etc.

Such factors were realised with the failure of Trent Concrete and EJ Badekabiner on the Athletes’ Village which saw cost increases of up to 60 per cent above the original contract value (see the Analysis section for further details).

To reduce the impact of such occurrences, SCM worked with all Tier One main contractors to identify critical material and commodities whose risk of supply can be reduced from advanced buying ahead of the current schedule requirements.

In such instances, items would be stored on the Games site in advance of installation, or at suppliers’ sites accompanied by the appropriate securities (vesting certificates and off-site material bonds).

Figure 3 highlights the elements and steps of the SCM strategy for supplier selection and insolvency monitoring as described above.
Developing detailed contingency plans for critical contract packages helped the ODA/CLM teams to understand the contractor’s approach to mitigating the insolvency risk and to gauge their readiness to respond in the event of failure.

Plans to limit the impact of potential insolvency included (but were not limited to) the following considerations:
– identification of critical Tier Two and Three suppliers and/or packages;
– identification of alternative suppliers and resources, contact with lower tier suppliers to maintain progress and securing the site;
– contingency plans in the event of any subcontractor liquidation;
– processes in place to control/understand material movements;
– the level of advance payments and off-site payments;
– lower tier suppliers’ ‘corporate’ approach to insolvency management.

The Tier One main contractors whose performance and supply chains were critical in progressing the build programme were engaged in this exercise and asked to complete a Critical Contracts Register containing details including: the value and dates of the contract, the cost to complete, the value of materials vested, criticality rating, and package contingency.

Areas of concern were identified, together with areas of good practice with all parties to ensure a consistent approach was adopted which in turn promoted learning and good practice across the vertical project and horizontal programme supply chain.

**Step 3: Recovery (in the event of insolvency)**

In the event of insolvency within the supply chain, the ODA and Delivery Partner developed a Recovery Plan, including a Recovery team, to ensure the continuation of construction with the least impact to the programme.

The Recovery Plan comprised five main elements: Security, contract termination, communications, Recovery team and contingency plans. A breakdown of these elements follows:

**Security:** The site should be secured as quickly as possible to prevent vandalism or theft of materials and equipment. Off-site materials (vested and secured by bonds) should be secured and arrangements made for immediate removal from the affected parties’ premises. Expert advice would be made available and arranged through the ODA Legal team’s Framework Legal Partners to ensure full access rights to off-site secured materials occurs.

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In the event of insolvency within the supply chain, the ODA developed a Recovery Plan including a Recovery team.

View of construction of the MPC building, November 2009
Contract termination: Under the terms of the NEC 3 contract, termination at the point of insolvency is not automatic, but notice could be given by the ODA if it was decided, after consideration with all stakeholders (including defaulting parties, administrator, etc), that termination was the best course of action. In such an eventuality, and to ensure the terms of the contract are fully complied with, the Delivery Partner’s Project Manager would have 13 weeks to certify a final payment to the contractor/administrator for works completed up to the point of termination.

The key activities that the Delivery Partner would be required to undertake to protect the clients’ interests included:
- full valuation of all works up to the point of termination (photographic evidence to support valuation and site status will be required);
- an itemised list of all known defects. The Delivery Partner would be required to obtain quotes for rectification;
- ensuring procedures were in place and adopted so that all communications and negotiations are via the administrator and not directly with any subcontractor for works related up to the point of termination;
- ensuring all compensation events were up-to-date, and issuing a Project Manager’s assessment (if applicable);
- ensuring all cost verification findings were fully documented (including disallowed cost) and considered in the overall final certified payment;
- certifying sectional completion, and imposed damages allowed under the contract if completion was beyond the dates in the contract;
- forecasting the additional cost to the client of completing the works and deducting costs from outstanding payments as allowed under the contract.

Communications: The Recovery team would establish communications with the key stakeholders including the Administrator, Tier One main contractor, employee representatives and other contractors. It was important that any formal commercial discussions and agreements involved the Administrator appointed by the company or court and that the Project Manager does not deal directly with subcontractors without their full knowledge, unless the client has indicated the intention to ‘step in’.

The core purpose was to segregate the duties of dealing with the Administrator and mitigating the commercial (time and cost) impact of the insolvency on the one hand and ensuring the continuation of site delivery on the other. The development of construction recovery plans was also intended to limit the impact of any subsequent delays.

The Recovery team: The Recovery team could comprise key executive parties from the client or contractor who were empowered, with the appropriate delegated levels of authority, to ensure a swift outcome to all negotiations with the Administrator and minimal impact to site delivery.

Ultimately, the Recovery team, through the SCM team, would also determine the extent of the impact on the programme as a result of interfaces with other projects or involvement with other contracts or suppliers.

Recovery teams comprised key executive parties from the client or contractor who were empowered to negotiate with the Administrator to minimise impact to site delivery.
Analysis – Interventions and achievements

Through comprehensive supply chain processes, the Delivery Partner monitored over 80 Tier One main contracts and 2,700 ‘critical’ packages of work across the Park and Athletes’ Village for indicators of both risk and opportunity. The degree of supplier visibility was possible as a result of a joint initiative by the ODA, Delivery Partner and Tier One main contractors to identify and register critical packages and components (refer to above and Appendix A. Supply Chain Management Contractor Matrix).

Based on the intelligence gained from engaging with the market and suppliers, interventions were considered and continually reassessed with respective project teams. Supplier interventions took different forms, occurred at different stages of delivery and within various tiers of the supply chain.

As part of the daily monitoring process, the Delivery Partner identified 25 Tier One main contracts, representing ODA spend in excess of £2 billion that had an increased level of potential risk within their supply chains, and needed to take action. Examples of these interventions and their resultant effects are classified as follows:

1. **Indirect** – it was probable that the Tier One main contractor would have removed supplier risk as part of their own procurement and supplier selection process, or the supplier was unsuccessful for other reasons, for example failed to submit a competitive or compliant tender, D&B High Risk or ‘out of business’ Indicator, over-capacity risk.

2. **Direct** – the Delivery Partner made a recommendation to mitigate a potential risk which was achieved to protect the programme, manufacturing process and ultimately, the asset required by the ODA. Such interventions included requests for Parent Company Guarantees, performance bonds, accelerated or supportive payment patterns (from the ODA directly or via the main contractor), material vesting, etc.

3. **Positive-Negative** – the Delivery Partner identified an increased supplier risk and made recommendation(s) through interventions, however, the Tier One main contractor appointed the contract in light of the intelligence available and took a view on risk exposure/failure probability.

4. **Unavoidable** – supplier insolvency that was not tracked or predicted through Delivery Partner daily monitoring processes or that of the Tier One main contractor’s in-house systems.

Through early detection, intervention and collaborative working between the Delivery Partner and main contractor, 73 per cent of supplier risks were removed pre-tender.

SCM cannot prove or disprove their influence was decisive in the removal of the risk, therefore these interventions represent the Indirect effect (see Figure 4). The remaining 27 per cent of interventions (Direct, Positive-Negative and Unavoidable) were communicated during tender and award periods in response to increased levels of supplier risk, or even insolvency.
SCM’s objective was to identify and remove potential supplier threats at the earliest opportunity to protect every aspect of the programme, for example procurement delays would ultimately impact on start-on-site milestone dates. 403 interventions were recorded in response to an increased level of supplier risk at a combined value of £640 million, with £433m removed at tender alone.

Early intervention by SCM allowed the Tier One main contractor to investigate, develop a mitigation strategy, or identify suitable alternative companies. The resultant effect removed considerable risk at the tender stage, ensured risk, or potential threats were acknowledged by the project teams during procurement and mitigation plans developed to protect the programme in the event of failure (such as financial audit, material vesting, Parent Company Guarantee confirmed). Once the contract had been placed, interventions were made to retrospectively protect the ODA’s assets and programmes.

Figure 4: Total number of supplier interventions against critical packages from early risk identification and removal pre-procurement to managing exposure post contract award.
Following five unavoidable failures, quick intervention aided the recovery of the individual projects with limited periods of inactivity.

Figure 5 shows the total number of critical packages associated with supplier insolvency.

66 packages failed at tender stage and were removed with zero impact to the programme – those packages were associated with 43 different insolvent suppliers, at a combined value of £63m.

There were nine packages – awarded to seven suppliers with an approximate value of £20m – with realised insolvencies, that occurred during the contract. However, all were monitored by the Delivery Partner from tender stage until their demise, meaning all had a mitigation strategy in place to accelerate steps to minimise project and programme impact.

It was widely accepted by the ODA and Delivery Partner that a small number of insolvencies would be inevitable, especially within the Tier One main contractors’ supply chains given there were no contractual links for the Delivery Partner to act directly but through the contracting organisation.

Again, all of the five unavoidable package failures (or four individual supplier insolvencies valued at £6.5m) were included within SCM’s critical package monitoring. This meant quick intervention aided the recovery of the individual projects with limited periods of inactivity through immediate appointment of alternative suppliers and installers from within the existing Games supply chain.

Figure 5: The total number of critical packages associated with supplier insolvency
Retrospective investigation into these failures ultimately established that business debt and the refusal of lenders to extend terms further impacted cash-flow.

Financial institutions unable to recover their investments called in administrators to maximise returns where possible, mainly through land acquisition. Such matters are not detectable through any form of supplier or financial monitoring solution in the market place, therefore adding to the benefit of ensuring an accurate register of critical packages and mitigation strategies certainly minimised the impact financially and protected the ultimate goal of the ODA construction programme.

The following examples of two insolvencies from the point of early risk identification, to intervention through to the realisation of failure demonstrate how the combined efforts of the main contractor and Recovery teams minimised the impact of failure on the Games’ construction programme, yet highlights the financial implications of failure and inflation associated with an appointed administrator.

**Example A: SJW Civil Engineering Ltd**

SJW Civil Engineering Ltd was identified by the Delivery Partner as being a high financial risk. They were associated with two Tier One main contractors across four projects and listed against seven commercially competitive tenders totalling a combined works value of £3.5m (should they have been successful on all). Further financial deterioration of both the parent and subsidiary was tracked by the Delivery Partner through D&B daily monitoring which led to Project team alerts (individual and parent company alerts). Interventions and mitigations identified alternative suppliers and an in-house capability to undertake works.

Through early engagement with both the supplier and the main contractors, D&B daily monitoring, clear communication of concern and recommendations made to mitigate risk or remove the supplier, the supplier remained on six bid lists. Efforts to confirm parent company linkages and organisational structure directly with the supplier were not successful in securing additional assurances to explain and underwrite financial and capacity risks.

SJW Civil Engineering Ltd was awarded one package at Eton Dorney Rowing facility. The main contractor had included the supplier based on ‘previous experience’ and competitive tender returns, however, acknowledgement of the potential risks were not deemed sufficient to remove them from the procurement process, for example the main contractor was prepared to manage the risk and mitigation in the event of failure. Note: the contracting form in this case was NEC 3 Option A.

SJW Civil Engineering Ltd was subsequently awarded one reinforced concrete package valued at £500,000 which represented approximately five per cent of the total Eton Dorney project value.

At the point of insolvency £300,000 had been spent, however, the failure is reputed to have cost the main contractor about £250,000 in additional fees (50 per cent of the original contract value). Quick actions taken by the ODA, Delivery Partner and main contractor to reschedule the delivery programme, procure additional materials, retain and employ the labour of the failed supplier, and mobilise in-house capacity protected the agreed completion milestones.
Example B: EJ Badekabiner (UK) Ltd

EJ Badekabiner (UK) Ltd was identified by the SCM team on two Athletes’ Village projects. They were listed against three commercially competitive tenders for the manufacture and installation of bathroom pods totalling works to a value of £10m (should they have been successful on all).

The Athletes’ Village team was made aware of the potential risk of insolvency early in the pre-tender stage through supply chain monitoring processes. Suitable assurances and guarantees were recommended by the Delivery Partner to mitigate the financial and capacity risks highlighted through supplier interventions. Two contracts were awarded in light of these potential risks, without confirmation the Parent Company Guarantee and an investigation into the aforementioned matters had been undertaken.

At the point of the insolvency, the combined Project team (including the ODA, Delivery Partner and main contractors) immediately contacted the Administrator and was able to agree and implement mitigation measures to reduce potentially disastrous impacts. The team was able to secure the bathroom pod ‘shells’ delivery to site, excluding complete interior fit-out, so minimising the impacts to increased retrofit works on-site or the requirement to pay an administrator to keep the factory open or procure an alternate bathroom pod supplier. Although delays resulted from this insolvency, the speedy action by the Project team ensured that the plot could be ‘closed up’ in the timeliest manner and mitigated major delays.

The ODA and Delivery Partner’s Athletes’ Village team coordinated with Lend Lease to develop a mitigation strategy that determined the most economical and schedule effective approach for responding to this incident. The cost, which equates to approximately 60 per cent of the original contract value, includes the procurement of a third party to fit out the bathroom pods on-site and negotiations with other trade contractors to reschedule programmes.

The combined Project team was able to agree and implement mitigation measures to reduce potentially disastrous impacts.
Lessons learned and conclusions

While the ODA has proven that this method of managing and mitigating supplier insolvency risk is effective at both project and programme level, it is impossible to entirely mitigate all the risks associated with failure in the supply chain.

With the very real probability that the full extent of the recession has not yet manifested itself and with 2012 works drawing to a conclusion, the following steps should be considered when implementing a SCM Insolvency Risk strategy:

- Encourage potential and contracted suppliers to regularly take an interest in their own financial rating – include this as part of the pre-procurement market engagement activities.
- Undertake detailed risk analysis of ‘project, programme or organisational’ risks to inform risk mitigation and management, programme contingency assessment and set realistic financial provisions.
- Develop detailed contingency plans for ‘critical contract packages’ which will help to understand the contractor’s approach to mitigating the insolvency risk and to gauge their readiness to respond in the event of failure, regardless of the supplier’s financial classification.
- For contracts executed, work with supply chains to ensure ‘critical suppliers’ have been identified and that increased financial monitoring of critical suppliers and a view of liquidity through the supply chain, together with contingency plans for supplier insolvency/failure, are in place.
- Understand critical suppliers’ risk management strategies. Make recommendations for additional assurance in relation to supply chain risks (where required).
- Consider the need for, and prepare standard templates of, the financial information required monthly from critical suppliers and the standard processes for executing reviews of financial standing.
- Review and update processes and procedures for the selection and management of the supply chain to reflect the emerging increased risks, including procurement strategies, identification of critical suppliers, contingency planning and supplier auditing.
- Deliver ‘what if’ scenario planning with all project teams to raise the profile and management of insolvency risk at a delivery level and to inform risk management and contingency provisions.
- Develop clear operational and financial procedures on the actions following supplier insolvency – the formation of an Insolvency Recovery team and/or key ‘action owners’.
- Get legal expertise in the event of insolvency in the supply chain to determine the actions that can be taken by the contracting body (client/main contractor) or its representatives. Access to such advice should ensure compliance with the Insolvency Rules within the specific contracting form.
- Establish an Insolvency Recovery team whose purpose is to coordinate and manage insolvency situations across the programme.
- The Client/Project team should undertake a multifunctional (Project Management, Commercial Management, legal, finance, etc) workshop simulation to ‘model’ how the team would respond to an insolvency. Training outputs should help to formalise the strategy/approach to manage supplier risk.
- Once the overall insolvency plan has been finalised, further awareness and training sessions are required/advised by the client/contracting organisation to ensure key staff are aware of:
  1. commercial and contract administration insolvency terms and conditions, and liabilities within contract variations/types;
  2. those steps/activities that should be undertaken to protect IP and prepare the Project team to mitigate the impact of insolvency on delivery operations;
  3. the processes and procedures that need to be implemented in the event of a Tier One main contractor or Tier Two insolvency and;
  4. the vesting and other provisions within the contracts to protect the client and project stakeholder in the event of insolvency.
Conclusion

Further improvements in the insolvency management processes are possible through increased awareness and education of how to identify a failing business, wider understanding of contractual terms and conditions within the Project team, etc but ultimately, next time, such supply chain management processes will be supported by a proven and successful track record of removing project and programme level insolvency risk.

The following supportive quotation is taken from the January 2012 National Audit Office Value for Money Report: ‘While risks inevitably remain, good practice and lessons for other public bodies are evident in how the ODA’s monitoring and active intervention in its supply chains has protected its delivery programme from delays through contractor financial distress and insolvency.’

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Further improvements in the insolvency management processes were possible through increased awareness and education.