

Committees:	Dates:
Finance Committee Finance Committee of the Barbican Centre Board (for information)	21 July 2015 30 September 2015
Subject: Chamberlain's Financial Appraisals of Third Party Entities	Public
Report of: The Chamberlain	For Decision

Summary

The Chamberlain's Department undertakes financial appraisals on potential commercial tenants, suppliers and service providers. Such appraisals have been undertaken based on practical experience and knowledge using an internally developed procedure guide. In February 2015 new procurement regulations were transposed into UK law with an increased requirement on transparency and compliance in respect of selection criteria. The new regulations also require a 'light touch' regime for low value contracts below the OJEU threshold. Consequently, the procedure guide was amended to incorporate selection criteria required by the new regulations, and the assessment methodology is disclosed to suppliers up front to ensure transparency. Pre-Qualification Questionnaires (PQQ) now include, where relevant, explicit financial criteria from the procedure guide, against which potential tenderers can assess their own suitability on a pass/fail basis. For contracts below the OJEU threshold, the procedure guide was revised to allow a proportional approach based upon the risk of the contract. Ensuring the procedure guide has official status represents a logical development that protects the City from external challenge, and makes the procurement process more accessible to SMEs.

This report presents this procedure guide for formal adoption by the City Corporation. The new regulations will require modest changes to the working practices of the appraisals team, however it is expected that this can be accommodated within existing resources.

Recommendations

Members are asked to:

- a) Note the report
- b) Adopt the financial appraisal procedure guide
- c) Delegate authority to the Chamberlain to amend the guide as necessary to comply with United Kingdom and European Community procurement law and any other legal and accounting requirements which may arise in due course.

Main Report

Background

1. The City Corporation has a diverse range of commercial and business interests which require it to interact financially with the wider world, which exposes its financial resources to risk, either by losing income or by incurring excessive expenditure when interacting with third parties. Financial appraisals are a means of mitigating that risk in some part.
2. The main areas of risk are retail and commercial leases, property developments, contracts for goods or services and the Approved List of Caterers for Guildhall functions.
3. In February 2015, the Public Contract Regulations 2015 (PCR 2015) were transposed into UK law, with increased requirements on transparency and compliance in respect of selection criteria used in financial appraisals. The new requirements have resulted in financial appraisals coming under more scrutiny as they represent a visible and important facet of the procurement process. As such they are exposed to challenge, particularly where an adverse financial appraisal is given.
4. Members of the Barbican Board have queried the appropriateness of financial appraisal procedures applied and the Chairman of Finance Committee has agreed that a review of the procedures should be undertaken.
5. This report seeks Members' approval for the formal adoption of the current financial appraisal procedure guide to be used when undertaking financial appraisals of third party entities.

Current Position

6. Financial appraisals are undertaken on third party entities which are:
 - a. taking tenancies of City commercial and retail properties;
 - b. undertaking developments of City property holdings;
 - c. being shortlisted for City Corporation contracts with a value in excess of £172,000 for goods and services or £400,000 for works;
 - d. being retained on the Approved List of Caterers for Guildhall functions.
7. A procedure guide has been developed from existing documentation, current working practices and practical experience. The intention has been to codify City practice, ensure robust assessment procedures to mitigate financial risk, and demonstrate compliance with Regulation 58 (Selection Criteria – Economic and Financial Standing) of PCR 2015. The guide is a living document which continues to be amended as necessary in the light of experience and in response to changing statutory requirements. It currently has no formal status, being an internal working document used to ensure that all financial appraisals are undertaken to the same standards of analysis.

8. During 2014 the financial appraisal practices in nine other local authorities were benchmarked against the City's current practice. Within these nine examples practice ranged from one instance of sole reliance on Credit Reference Agency (CRA) to sole reliance on analysing company accounts (three instances). Four authorities analysed company accounts supplemented by CRA. One authority was implementing an on-going project to move away from financial appraisals in favour of risk based assessment. There appeared to be no standard model or guidance for financial appraisals in use.
9. The City uses company accounts supplemented by the background information provided in Credit Reference Agency reports for financial appraisals. This compares favourably to those authorities that only used information from a single source, and would accord with the practices of the majority of those authorities included in the benchmarking.

Proposals

10. It is proposed that the procedure guide should be adopted as the City's standard procedure to be applied for all financial appraisals undertaken by the Chamberlain's Research and Technical section.
11. It is also proposed that authority should be delegated to the Chamberlain to amend the guide as necessary, once adopted, in order to reflect the continuing development of procurement policy under PCR 2015 and any other legal and accounting requirements which may arise.
12. The main change to existing procedures is to incorporate mandatory assessment criteria required by PCR 2015, such as those relating to turnover thresholds. The revised procedures are more transparent, with the financial criteria and method of assessment communicated to prospective suppliers up front. This enables them to undertake a measure of self-assessment to determine whether they have the financial and economic standing to perform the contract.
13. The procedures also incorporate the requirements of PCR 2015 relating to low value contracts below the OJEU threshold. For these tenders, contractors submit a self-assessment against the City's evaluation criteria and the financial appraisal process is only applied to the winning bidder. The revised procedures allow a proportional approach to the appraisal criteria based upon the size of the contract, and the pool of likely contractors.
14. The procedure guide is attached at Appendix 1 and incorporates the financial appraisal criteria used in the Pre-Qualification Questionnaire (PQQ) for contracts being let by City Procurement e.g. the calculation of turnover requirements, standard accounting ratios, and Altman's Z- Score.

Implications

15. With the advent of PCR 2015 it is imperative that the procurement process should demonstrate transparency and compliance with the new regulations. The financial appraisal of potential tenderers is a part of the procurement process which does come under scrutiny and challenge by external parties exercising their rights to challenge contract awards in accordance with regulations 88-104

(Chapter 6 Applications to the Court) of PCR 2015. Adopting the procedure guide and its PQQ criteria will underpin the already robust procurement procedures in place.

16. The procedures are compliant with regulation 111 (Assessing suitability – Chapter 8 Below threshold contracts) of PCR 2015, which requires a light touch procurement regime for low value contracts. Compliance with the new regulations reinforces the City's support for SME's, making it easier for them to engage with the procurement process and ensuring that any appraisal undertaken is proportionate to the risk of the contract.
17. Should the procedure guide and its PQQ criteria *not* be adopted, the financial appraisal elements of procurement projects will potentially breach statutory requirements and also leave such projects open to challenge by external parties. In addition the current unofficial status of the procedure guide detracts from the robustness of the actual procedures themselves and the validity of a strong corporate response to challenge.
18. It is not expected that adoption of the procedure guide will result in any adverse financial or HR implications. The revised procedures will require modest changes to the working practices of the appraisals team, however these changes can be accommodated within existing resources.

Conclusion

19. The financial appraisals of third party entities are coming under greater scrutiny as a result of PCR 2015. The adoption of the procedure guide and associated PQQ criteria will give formal status to what is currently an internal departmental working document and will also present the opportunity to demonstrate transparency and compliance as procurement practices develop.

Appendices

- Appendix 1 – Chamberlain's Financial Appraisals: Procedure Guide and Manual, including Pre-Qualification Questionnaire financial criteria.

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