

## **Schedule 22 - Financial Distress**

### **1. Introduction**

- 1.1. This Schedule 22 provides for the assessment of the financial standing of the Contractor and Guarantor, and the establishment of trigger events relating to changes in such financial standing which, if breached, will have specified consequences.

### **2. Financial Ratios**

- 2.1. The Contractor shall monitor the Financial Ratios on an ongoing basis and calculate the following Financial Ratio tests (on the basis of published accounts) as at the end of each Financial Ratios Calculation Period. The Contractor shall confirm to the Authority in writing on the earlier of:

- (a) one (1) month following publication in the public domain of the financial accounts for the Financial Ratios Calculation Period; or
- (b) one-hundred and eighty (180) days of each such Financial Ratios Calculation Period,

that the Financial Ratios fall within the 'Acceptable' Financial Ratio Level as set out in the following tables. In the event that the Contractor is unable to confirm that the Financial Ratios for the Contractor or the Guarantor fall within the 'Acceptable' Financial Ratio Level, the provisions of paragraphs 3, 4 and 5 of this Schedule 22 shall apply (as applicable).

| <b>Test</b>      | <b>Financial Ratio Levels</b> |  |   |                    |
|------------------|-------------------------------|--|---|--------------------|
|                  | <b>Acceptable</b>             | <b>Level 1</b>                                       | <b>Level 2</b>                                    | <b>Level 3</b>     |
| Financial Ratios | Twenty (20) or above          | Less than twenty (20) but not less than fifteen (15) | Less than fifteen (15) but not less than five (5) | Less than five (5) |

| Net Assets                              |         | Score  | Debt Ratio |  | Score | Acid Test           |       | Score | Operating Cash Flow Ratio |          | Score |
|---|---------|--------|------------|--|-------|---------------------|-------|-------|---------------------------|----------|-------|
| £3.0m                                   |         | 5.0    | < 0.3      |  | 10.0  | > 1.4               |       | 15.0  | 10%                       |          | 10.0  |
| £2.7m                                   | < £3.0m | 4.5    | > 0.3      | 0.4  | 9.0   | < 1.4               | 1.3   | 13.5  | 9%                        | < 10%    | 9.0   |
| £2.4m                                   | < £2.7m | 4.0    | > 0.4      | 0.5  | 8.0   | < 1.3               | 1.2   | 12.0  | 8%                        | < 9%     | 8.0   |
| £2.1m                                   | < £2.4m | 3.5    | > 0.5      | 0.6  | 7.0   | < 1.2               | 1.1   | 10.5  | 7%                        | < 8%     | 7.0   |
| £1.8m                                   | < £2.1m | 3.0    | > 0.6      | 0.7  | 6.0   | < 1.1               | 1.0   | 9.0   | 6%                        | < 7%     | 6.0   |
| £1.5m                                   | < £1.8m | 2.5    | > 0.7      | 0.8  | 5.0   | < 1.0               | 0.9   | 7.5   | 5%                        | < 6%     | 5.0   |
| £1.2m                                   | < £1.5m | 2.0    | > 0.8      | 0.9  | 4.0   | < 0.9               | 0.8   | 6.0   | 4%                        | < 5%     | 4.0   |
| £0.9m                                   | < £1.2m | 1.5    | > 0.9      | 1.0  | 3.0   | < 0.8               | 0.7   | 4.5   | 3%                        | < 4%     | 3.0   |
| £0.6m                                   | < £0.9m | 1.0    | > 1.0      | 1.1  | 2.0   | < 0.7               | 0.6   | 3.0   | 2%                        | < 3%     | 2.0   |
| £0.3m                                   | < £0.6m | 0.5    | > 1.1      | 1.2  | 1.0   | < 0.6               | 0.5   | 1.5   | 1%                        | < 2%     | 1.0   |
|   | < £0.3m | 0.0    |            | > 1.2  | 0.0   |                     | < 0.5 | 0.0   |                           | < 1%     | 0.0   |
|   |         |        |            |  |       |                     |       |       |                           |          |       |
| Trend                                   | < 10%   | +/-10% | > 10%      |  |       | Net Assets          |       | 5     |                           |          |       |
| Net Assets                              | 0       | 1      | 2          |  |       | Debt Ratio          |       | 10    |                           |          |       |
| Acid Test                               | 0       | 1      | 3          |  |       | Acid Test           |       | 15    | Acceptable                | 20+      |       |
| Debt Ratio                              | 0       | 1      | 3          |  |       | Operating Cash Flow |       | 10    | Level 1                   | 15 - <20 |       |
| Cash Flow                               | 0       | 1      | 2          |  |       | Trend               |       | 10    | Level 2                   | 5 - <15  |       |
| Trend analysis over 3 years of accounts |         |        |            | 10   |       | Financial Ratios    |       | 50    | Level 3                   | 0 - <5   |       |
| Ratio Calculations:                     |         |        |            |  |       |                     |       |       |                           |          |       |
|   |         |        |            |  |       |                     |       |       |                           |          |       |
| Net Assets                              |         |        |            | As per balance sheet at year-end date              |       |                     |       |       |                           |          |       |
| Debt ratio                              |         |        |            | Total Liabilities / Total Assets                   |       |                     |       |       |                           |          |       |
| Acid test                               |         |        |            | (Current Assets - Inventory) / Current Liabilities |       |                     |       |       |                           |          |       |
| Operating Cash Flow                     |         |        |            | Operating Cash Flow / Revenue                      |       |                     |       |       |                           |          |       |

2.2. The Contractor warrants and represents to the Authority for the benefit of the Authority that as at the Commencement Date and for the duration of the Contract the Financial Ratios for the Contractor and the Guarantor do and shall fall within the “Acceptable” Financial Ratio Level.

2.3. The Contractor shall regularly monitor the indicators of risk, including without limitation the Financial Ratios relating to the Contractor and the Guarantor, in accordance with this Schedule 22 throughout the Contract Period and shall promptly notify, or shall procure that its auditors promptly notify, the Authority in writing following the occurrence of a Financial Distress Event (and in any event within ten (10) Working Days from the date on which the Contractor first becomes aware of any fact, circumstance or matter which has caused a Financial Distress Event).

### 3. Level 1 – Consequences of a Financial Distress Event

3.1. If the Financial Distress Event consists of:

- (a) the Contractor or the Guarantor having an adverse decline in the Financial Ratios specified in paragraph 2.1 of this Schedule 22 such that the value for the Financial Ratios fall within Financial Ratio Level 1;
- (b) the Contractor or the Guarantor issuing a profit warning to a stock exchange or making any other public announcement about a material deterioration in its financial position or prospects;
- (c) there being a public investigation into improper financial accounting and reporting, suspected Fraud or any other impropriety of the Contractor or the Guarantor; and/or
- (d) the Contractor or the Guarantor committing a material breach of covenants to its lenders,

then, immediately upon notification of the Financial Distress Event (or if the Authority becomes aware of the Financial Distress Event without notification

and brings the Financial Distress Event to the attention of the Contractor), the Authority shall have the rights set out in paragraph 3.2 of this Schedule 22.

3.2. At the request of the Authority, the Contractor shall:

- (a) meet with the Authority (and, if the Financial Distress Event relates to the Guarantor, use all reasonable endeavours to procure that the Guarantor shall meet with the Authority) as soon as is reasonably practicable and in any event within three (3) Working Days to review the effect of the Financial Distress Event upon the continued performance of the Services or of the Guarantee (as the case may be); and
- (b) submit to the Authority for its approval, the draft Financial Distress Event Service Continuity Plan as soon as possible and in any event not later than ten (10) Working Days (or such other period as the Authority may permit and notify to the Contractor in writing) after the initial notification under paragraph 2.3 of this Schedule 22.

3.3. The Authority shall not withhold its approval of a draft Financial Distress Event Service Continuity Plan unreasonably. If the Authority does not approve the draft Financial Distress Event Service Continuity Plan it shall inform the Contractor of its reasons and the Contractor shall take those reasons into account in the preparation of a further Financial Distress Event Service Continuity Plan, which shall be resubmitted to the Authority within five (5) Working Days of the rejection of the first draft.

3.4. If the Authority considers that the draft Financial Distress Event Service Continuity Plan is insufficiently detailed to be properly evaluated, or will take too long to complete or will not remedy the Financial Distress Event complained of, then it may either agree a further time period for the development and agreement of the Financial Distress Event Service Continuity Plan or escalate any issues with the draft using the Financial Distress Event Service Continuity Plan Escalation Process.

3.5. The Contractor shall comply with any Financial Distress Event Service Continuity Plan following its approval by the Authority.

#### **4. Level 2 – Consequences of a Financial Distress Event**

4.1. If the Financial Distress Event consists of:

- (a) The Contractor or the Guarantor having an adverse decline in the Financial Ratios specified in paragraph 2.1 of this Schedule 22 such that the value of those Financial Ratios falls within Financial Ratio Level 2;
- (b) A Key Sub-contractor notifying the Authority that the Contractor has not satisfied any material sums properly due under a specified invoice and not subject to a genuine dispute; and/or
- (c) The Contractor failing to notify the Authority of a Financial Distress Event that falls within paragraph 3 of this Schedule 22,

then, immediately upon notification of the Financial Distress Event (or if the Authority becomes aware of the Financial Distress Event without notification and brings the Financial Distress Event to the attention of the Contractor), the provisions of paragraphs 3.2 to 3.5 of this Schedule 22 shall apply to the extent applicable and the Authority shall also have the rights set out in paragraph 4.2 of this Schedule 22.

4.2. The Authority may:

- (a) Without cost to the Authority, require the Contractor to establish a Financial Distress Escrow Account;
- (b) Pay any undisputed Fees due to the Contractor in respect of each month during which Services have been received (less any deductions made in accordance with this Contract) into the Financial Distress Escrow Account;
- (c) Require the Contractor to provide (and, if applicable, use all reasonable endeavours to procure that the Guarantor provides) such financial information relating to the Contractor or Guarantor (as the case may be) as the Authority may reasonably require; and
- (d) Require any sums properly due to a Key Sub-contractor to be paid (without set-off or deduction) directly from the Financial Distress Escrow Account to the relevant Key Sub-contractor.

4.3. The Authority shall, prior to exercising its rights under paragraphs 3.2 and/or 4.2 of this Schedule 22 (as the case may be):

- (a) Where the Financial Distress Event relates to the issue of a profit warning by the Contractor or Guarantor pursuant to paragraph 3.1(b), give the Contractor a period of not more than ten (10) Working Days to demonstrate to the Authority's reasonable satisfaction that the profit warning relates to a general reduction in trade in the relevant industry sector and that it will not result in the Contractor becoming unable, within the next twelve (12) months, to pay Key Sub-contractors or the Guarantor becoming unable, within the next twelve (12) months, to be able to perform the Guarantee (as the case may be); and
- (b) Where the Financial Distress Event relates to the non-payment of Key Sub-contractors pursuant to paragraph 4.1(b), give the Contractor a period of not more than ten (10) Working Days in which to rectify that non-payment or to demonstrate to the Authority's reasonable satisfaction that there is a valid reason for non-payment.

4.4. Monies paid into the Financial Distress Escrow Account by the Authority shall be held on trust by the approved bank and shall be paid out on the joint instructions of the Parties in the following order:

- (a) The payment in full of any Key Sub-contractors;
- (b) The payment in full of any other Sub-contractors;
- (c) The payment of any other liabilities of the Contractor that have a direct impact on the performance of the Contract; and

- (d) Subject to paragraphs 4.5 and 4.6 of this Schedule 22, repayment of the balance to the Contractor.
- 4.5. The Contractor shall demonstrate its compliance with paragraphs 4.4(a), (b) and (c) of this Schedule 22:
  - (a) By the production of valid invoices against which payments from the Financial Distress Escrow Account have been made to the relevant Key Sub-contractors, other Sub-contractors and any other liabilities (as applicable); or
  - (b) At the Authority's sole discretion and notified in writing to the Contractor, by the certification by the nominated representative of the Contractor that the Key Sub-contractors, other Sub-contractors and any other liabilities (as applicable) have been paid from the Contractor's general account.
- 4.6. The Parties shall instruct the bank to withhold an amount in the Financial Distress Escrow Account in respect of:
  - (a) Any amount payable to a Key Sub-contractor or other Sub-contractor under the relevant Sub-contract that is subject to a dispute between the Key Sub-contractor or other Sub-contractor (as applicable) and the Contractor until the resolution of that dispute; and
  - (b) Which the Authority requires further details of the satisfaction of any relevant Key Sub-contractor's or Sub-contractor's invoices and/or any other liability.

## **5. Level 3 – Consequences of a Financial Distress Event**

- 5.1. If the Financial Distress Event consists of:
  - (a) The Contractor or Guarantor having an adverse decline in the Financial Ratios specified in paragraph 2.1 such that the value of those Financial Ratios falls within Level 3;
  - (b) Commencement of any litigation against the Contractor or the Guarantor with respect to financial indebtedness or any obligation under a service contract, non-payment of any financial indebtedness, any financial indebtedness becoming due as a result of an event of default, the cancellation or suspension of any financial indebtedness, which will directly impact upon the Contractor's ability to deliver the Services;
  - (c) An Insolvency Event; and/or
  - (d) The Contractor failing to notify the Authority of a Financial Distress Event that falls within paragraph 4 of this Schedule 22,

then immediately upon notification of the Financial Distress Event (or if the Authority becomes aware of the Financial Distress Event without notification and brings the Financial Distress Event to the attention of the Contractor), the provisions of paragraphs 3.2 to 3.5 and 4.2 to 4.6 of this Schedule 22 shall

apply to the extent applicable and the Authority shall also have the rights set out in paragraph 5.2 of this Schedule 22.

5.2. The Authority may:

- (a) Require the Contractor's chief financial officer to update the Authority as to its and/or the Guarantor's financial standing on a monthly basis and, if applicable, require the Contractor to use all reasonable endeavours to procure that the Guarantor directly provides monthly updates to the Authority;
- (b) Provide the Contractor with a draft Financial Distress Event Service Continuity Plan setting out how the Contractor will ensure the continuity of provision of the Services in the event that the Contractor or the Guarantor becomes subject to the occurrence of an Insolvency Event; and
- (c) Instruct the bank where the Financial Distress Escrow Account is held to retain in that Financial Distress Escrow Account, for the benefit of the Authority, such part of the Fees as the Authority shall specify (which the Parties acknowledge shall be a substantial part of the Fees after making payments in accordance with paragraphs 4.4(a), (b) and (c) and agree shall not constitute a breach of this Contract under clause H2 (Termination by the Contractor) for six (6) consecutive months.

5.3. The Authority shall not exercise its right under paragraph 5.2(c):

- (a) without first notifying the Contractor in writing of its intention to do so; and
- (b) where requested by the Contractor, within three (3) Working Days of the date of the paragraph 5.3(a) meeting, and without first considering any representations made by the Contractor.

**6. Termination Rights**

6.1. The Authority shall be entitled to terminate this Contract under clause H1 (Termination by the Authority) if:

- (a) The Contractor fails to notify the Authority in accordance with paragraph 4 and/or 5 in respect of a Financial Distress Event;
- (b) The Parties fail to agree a Financial Distress Event Service Continuity Plan in accordance with paragraphs 3.2 to 3.4 of this Schedule 22;
- (c) The Contractor fails to comply with the terms of the Financial Distress Event Service Continuity Plan in accordance with paragraph 3.5 of this Schedule 22; and/or
- (d) The Contractor fails to establish the Financial Distress Escrow Account and/or otherwise comply with its obligations in accordance with paragraph 4 or 5 of this Schedule 22; and/or

## **7. Consequences of an Improvement in Financial Distress**

7.1. Following the occurrence of a Financial Distress Event pursuant to paragraph 4 of this Schedule 22 then (as applicable):

- (a) If the Guarantor's Financial Ratios subsequently rise and are maintained above Level 2 pursuant to paragraph 4 of this Schedule 22 for a period of five (5) consecutive months; and/or
- (b) The relevant Key Sub-contractor withdraws its claim that the Contractor has not satisfied any material sums properly due and invoices or the Contractor has demonstrated to the Authority's reasonable satisfaction that there is a valid reason for non-payments,

then, subject to any subsequent Financial Distress Event, the Contractor may request that the Authority pay the Fees direct to the Contractor and that the Authority gives its consent to the closure of the Financial Distress Escrow Account and the Contractor's withdrawal of any sums standing to the credit of that account, and the Authority shall not unreasonably withhold or delay its agreement and consent in response to such request.

## **8. Sub-Contractor Payment**

8.1. The Contractor shall ensure that all Key Sub-contract include an obligation on the Key Sub-contractors to report to the Authority, within ten (10) Working Days of the due date for payment, any material non-payment or late payment of any sums due to it from the Contractor under the provision of the Key Sub-contract.