

ANNEX H – Financial Distress

1 Definitions

1.1 In this Schedule, the following definitions shall apply:

Board means the Contractor's board of directors.

Credit Rating Level means a credit rating level as specified in Appendix A of this Schedule.

Credit Rating Threshold means the minimum Credit Rating Level for the Guarantor as set out in Appendix B of this Schedule.

FDE Group means the Contractor and the Guarantor.

Financial Indicators means each of the financial indicators set out at Paragraph 5.1 of this Schedule.

Financial Target Thresholds means the target thresholds for each of the Financial Indicators set out at Paragraph 5.1 of this Schedule.

Rating Agencies means the rating agencies listed in Appendix A of this Schedule.

2 Warranties And Duty To Notify

2.1 The Contractor warrants and represents to the Authority for the benefit of the Authority that as at the Effective Date:

- (a) the long-term credit ratings issued for the Guarantor by each of the Rating Agencies are as set out in Appendix B of this Schedule; and
- (b) the financial position or, as appropriate, the financial performance of the Contractor satisfies the Financial Target Thresholds.

2.2 The Contractor shall promptly notify (or shall procure that its auditors promptly notify) the Authority in writing if there is any downgrade in the credit rating issued by any Rating Agency for the Guarantor (and in any event within 30 Working Days of the occurrence of the downgrade).

2.3 The Contractor shall:

- (a) Regularly (annually) monitor the credit ratings of the Guarantor with the Rating Agencies;
- (b) monitor and report on the Financial Indicators of the Contractor against the Financial Target Thresholds at least at the frequency set out for each at Paragraph 5.1 (where specified) and in any event, on a regular basis and no less than once a year within one hundred and twenty (120) days after the Accounting Reference Date; and
- (c) promptly notify (or shall procure that its auditors promptly notify) the Authority in writing following the occurrence of a Financial Distress Event or any fact, circumstance or matter which could cause a Financial Distress Event (and in any event, ensure that such notification is made within 10 Working Days of the date on which the Contractor first

becomes aware of the Financial Distress Event or the fact, circumstance or matter which could cause a Financial Distress Event) but only to the extent that disclosure of any further information would be prohibited by any Law or any regulations in the UK or other relevant jurisdiction.

2.4 For the purposes of determining whether a Financial Distress Event has occurred pursuant to the provisions of Paragraphs 3.1(a), and for the purposes of determining relief under Paragraph 7.1, the credit rating of the Guarantor shall be deemed to have dropped below the applicable Credit Rating Threshold if:

- (a) any of the Rating Agencies have given a Credit Rating Level for that entity which is below the applicable Credit Rating Threshold; or
- (b) a Rating Agency that is specified as holding a Credit Rating for an entity as set out at Appendix B of this Schedule ceases to hold a Credit Rating for that entity.

2.5 Each report submitted by the Contractor pursuant to Paragraph 2.3(b) shall:

- (a) be a single report;
- (b) contain a sufficient level of information to enable the Authority to verify the calculations that have been made in respect of the Financial Indicators;
- (c) include key financial and other supporting information (including any accounts data that has been relied on) as separate appendices;
- (d) be based on the audited accounts for the date or period on which the Financial Indicator is based or, where the Financial Indicator is not linked to an accounting period or an accounting reference date, on unaudited management accounts prepared in accordance with their normal timetable; and
- (e) include a history of the Financial Indicators reported by the Contractor in graph form to enable the Authority to easily analyse and assess the trends in financial performance.

3 Financial Distress Events

3.1 The following shall be Financial Distress Events:

- (a) the credit rating of the Guarantor dropping below the applicable Credit Rating Threshold;
- (b) the Guarantor issuing a profits warning to a stock exchange or making any other public announcement, in each case 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 an FDE Group entity;
- (d) an FDE Group entity committing a material breach of covenant to its lenders;
- (e) Not Used;
- (f) any of the following:

- (i) commencement of any litigation against the Contractor with respect to financial indebtedness greater than [Information Redacted] or obligations under a service contract with a total contract value greater than [Information Redacted];
- (ii) non-payment by the Contractor of any financial indebtedness greater than [Information Redacted];
- (iii) any financial indebtedness of the Contractor becoming due as a result of an event of default;
- (iv) the cancellation or suspension of any financial indebtedness in respect of the Contractor; or
- (v) the external auditor the Contractor expressing a qualified opinion on, or including an emphasis of matter in, its opinion on the statutory accounts of the Contractor;

in each case which the Authority reasonably believes (or would be likely reasonably to believe) could directly and materially adversely impact on the continued performance and delivery of the Services in accordance with this Contract; and

Any one of the Financial Indicators set out at Paragraph 5 (Financial Indicators) for the Contractor failing to meet the required Financial Target Threshold

4 Consequences Of Financial Distress Events

4.1 Immediately upon notification by the Contractor of a Financial Distress Event (or if the Authority becomes aware of a Financial Distress Event without notification and brings the event to the attention of the Contractor), the Contractor shall have the obligations and the Authority shall have the rights and remedies as set out in Paragraphs 4.3 to 4.6.

4.2 Not Used

4.3 The Contractor shall (and shall procure that where applicable the Guarantor shall):

- (a) at the request of the Authority, meet the Authority as soon as reasonably practicable (and in any event within 3 Working Days of the initial notification (or awareness) of the Financial Distress Event or such other period as the Authority may permit and notify to the Contractor in writing) to review the effect of the Financial Distress Event on the continued performance and delivery of the Services in accordance with this Contract; and
- (b) where the Authority reasonably believes (taking into account the discussions and any representations made under Paragraph 4.3(a) that the Financial Distress Event could impact on the continued performance and delivery of the Services in accordance with this Contract:
 - (i) submit to the Authority for its approval, a draft Financial Distress Remediation Plan as soon as reasonably practicable (and in any event, within 10 Working Days of the initial notification (or awareness) of the Financial Distress Event or such other period as the Authority may permit and notify to the Contractor in writing); and

- (ii) to the extent that it is legally permitted to do so and subject to Paragraph 4.8, provide such information relating to the Contractor and/or the Guarantor as the Authority may reasonably require in order to understand the risk to the Services, which may include forecasts in relation to cash flow, orders and profits and details of financial measures being considered to mitigate the impact of the Financial Distress Event.
- 4.4 The Authority shall not withhold its approval of a draft Financial Distress Remediation Plan unreasonably. If the Authority does not approve the draft Financial Distress Remediation Plan, it shall inform the Contractor of its reasons and the Contractor shall take those reasons into account in the preparation of a further draft Financial Distress Remediation Plan, which shall be resubmitted to the Authority within 5 Working Days of the rejection of the first draft. This process shall be repeated until the Financial Distress Remediation Plan is approved by the Authority or referred to the Dispute Resolution Procedure under Paragraph 4.5.
- 4.5 If the Authority considers that the draft Financial Distress Remediation Plan is insufficiently detailed to be properly evaluated, will take too long to complete or will not ensure the continued performance of the Contractor's obligations in accordance with the Contract, then it may either agree a further time period for the development and agreement of the Financial Distress Remediation Plan or escalate any issues with the draft Financial Distress Remediation Plan using the Dispute Resolution Procedure.
- 4.6 Following approval of the Financial Distress Remediation Plan by the Authority, the Contractor shall:
 - (a) on a regular basis (which shall not be less than fortnightly unless otherwise agreed):
 - (i) review and make any updates to the Financial Distress Remediation Plan as the Contractor may deem reasonably necessary and/or as may be reasonably requested by the Authority, so that the plan remains adequate, up to date and ensures the continued performance and delivery of the Services in accordance with the Contract; and
 - (ii) provide a written report to the Authority setting out its progress against the Financial Distress Remediation Plan, the reasons for any changes made to the Financial Distress Remediation Plan by the Contractor and/or the reasons why the Contractor may have decided not to make any changes;
 - (b) where updates are made to the Financial Distress Remediation Plan in accordance with Paragraph 4.6(a), submit an updated Financial Distress Remediation Plan to the Authority for its approval, and the provisions of Paragraphs 4.4 and 4.5 shall apply to the review and approval process for the updated Financial Distress Remediation Plan; and
 - (c) comply with the Financial Distress Remediation Plan (including any updated Financial Distress Remediation Plan) and ensure that it achieves the financial and performance requirements set out in the Financial Distress Remediation Plan.
- 4.7 Where the Contractor reasonably believes that the relevant Financial Distress Event under Paragraph 4.1 (or the circumstance or matter which has caused or otherwise led to it) no longer exists, it shall notify the Authority and the Parties may agree that the Contractor shall be relieved of its obligations under Paragraph 4.6.

4.8 The Contractor shall use reasonable endeavours to put in place the necessary measures to ensure that the information specified at Paragraph 4.3(b)(ii) is available when required and on request from the Authority and within reasonable timescales. Such measures may include:

- (a) obtaining in advance written authority from the Guarantor authorising the disclosure of the information to the Authority and/or entering into confidentiality agreements which permit disclosure;
- (b) agreeing in advance with the Authority, and/or the Guarantor a form of confidentiality agreement to be entered by the relevant parties to enable the disclosure of the information to the Authority;
- (c) putting in place any other reasonable arrangements to enable the information to be lawfully disclosed to the Authority (which may include making price sensitive information available to Authority nominated personnel through confidential arrangements, subject to their consent); and
- (d) disclosing the information to the fullest extent that it is lawfully entitled to do so, including through the use of redaction, anonymisation and any other techniques to permit disclosure of the information without breaching a duty of confidentiality.

5 Financial Indicators

5.1 Subject to the calculation methodology set out at Appendix C of this Schedule, the Financial Indicators and the corresponding calculations and thresholds used to determine whether a Financial Distress Event has occurred in respect of those Financial Indicators, shall be as follows:

Financial Indicator	Calculation	Financial Target Threshold:	Monitoring and Reporting Frequency
1 Operating Margin	<i>[Operating Margin = Operating Profit / Revenue]</i>	<i>[Information Redacted]</i>	<i>[Information Redacted]</i>

2 Net Debt to EBITDA Ratio	<i>[Net Debt to EBITDA ratio = Net Debt / EBITDA]</i>	<i>[Information Redacted]</i>	<i>[Information Redacted]</i>
3 Acid Ratio	<i>[Acid Ratio = (Current Assets – Inventories) / Current Liabilities]</i>	<i>[Information Redacted]</i>	<i>[Information Redacted]</i>

Key: 1 – See Appendix C of this Schedule which sets out the calculation methodology to be used in the calculation of each Financial Indicator.

6 Termination Rights

6.1 The Authority shall be entitled to terminate this Agreement under Clause 19.1 (*Termination by the Authority*) if:

- (a) the Contractor fails to notify the Authority of a Financial Distress Event in accordance with Paragraph 2.3(c);
- (b) the Parties fail to agree a Financial Distress Remediation Plan (or any updated Financial Distress Remediation Plan) in accordance with Paragraphs 4.3 to 4.5; and/or
- (c) the Contractor fails to comply with the terms of the Financial Distress Remediation Plan (or any updated Financial Distress Remediation Plan) in accordance with Paragraph 4.6(c).

7 Primacy Of Credit Ratings

7.1 Without prejudice to the Contractor's obligations and the Authority's rights and remedies under Paragraph 2, if, following the occurrence of a Financial Distress Event pursuant to any of

Paragraphs 3.1(b) to 3.10, the Rating Agencies review and report subsequently that the credit ratings for the Guarantor do not drop below the relevant Credit Rating Thresholds specified for those entities in Appendix B of this Schedule, then:

- (a) the Contractor shall be relieved automatically of its obligations under Paragraphs 4.3 to 4.6; and
- (b) the Authority shall not be entitled to require the Contractor to provide financial information in accordance with Paragraph 4.3(b)(ii).

Appendix A – Rating Agencies and their Standard Rating System

- Rating Agency 1 (e.g Standard and Poors)
 - Credit Rating Level 1 = AAA
 - Credit Rating Level 2 = AA+
 - Credit Rating Level 3 = AA
 - Credit Rating Level 4 = AA-
 - Credit Rating Level 5 = A+
 - Credit Rating Level 6 = A
 - Credit Rating Level 7 = A-
 - Credit Rating Level 8 = BBB+
 - Credit Rating Level 9 = BBB
 - Credit Rating Level 10 = BBB-
 - Etc.
- Rating Agency 2 (e.g Moodys)
 - Credit Rating Level 1 = Aaa
 - Credit Rating Level 2 = Aa1
 - Credit Rating Level 3 = Aa2
 - Credit Rating Level 4 = Aa3
 - Credit Rating Level 5 = A1
 - Credit Rating Level 6 = A2
 - Credit Rating Level 7 = A3
 - Credit Rating Level 8 = Baa1
 - Credit Rating Level 9 = Baa2
 - Credit Rating Level 10 = Baa3

Appendix B – Credit Ratings and Credit Rating

Entity	Credit Rating (long term) (insert credit rating issued for the entity at the Effective Date)	Credit Rating Threshold <i>(insert the actual rating (e.g AA-) or the Credit Rating Level (e.g Credit Rating Level 3))</i>
Guarantor	Moody's – [Information Redacted]	Moody's – [Information Redacted]
	Standard & Poors – [Information Redacted]	Standard & Poors – [Information Redacted]

Appendix C – Calculation Methodology for Financial Indicators

The Contractor shall ensure that it uses the following general and specific methodologies for calculating the Financial Indicators against the Financial Target Thresholds:

General methodology

- 1 **Terminology:** The terms referred to in this Appendix are those used by UK companies in their financial statements. Where the entity is not a UK company, the corresponding items should be used even if the terminology is slightly different (for example a charity would refer to a surplus or deficit rather than a profit or loss).
- 2 **Groups:** Where the entity is the holding company of a group and prepares consolidated financial statements, the consolidated figures should be used.
- 3 **Foreign currency conversion:** Figures denominated in foreign currencies should be converted at the exchange rate in force at the relevant date for which the Financial Indicator is being calculated.
- 4 **Treatment of non-underlying items:** Financial Indicators should be based on the figures in the financial statements before adjusting for non-underlying items.

Specific Methodology

Financial Indicator	Specific Methodology
1 Operating Margin	<p>[The elements used to calculate the Operating Margin should be shown on the face of the Income Statement in a standard set of financial statements.</p> <p>Figures for Operating Profit and Revenue should exclude the entity's share of the results of any joint ventures or Associates.</p> <p>Where an entity has an operating loss (i.e. where the operating profit is negative), Operating Profit should be taken to be zero.]</p>
2 Net Debt to EBITDA Ratio	<p>Net Debt = Bank overdrafts + Loans and borrowings + Finance leases + Deferred consideration payable – Cash and cash equivalents</p> <p>EBITDA = Operating profit + Depreciation charge + Amortisation charge</p> <p>The majority of the elements used to calculate the Net Debt to EBITDA Ratio should be shown on the face of the Balance sheet, Income statement and Statement of Cash Flows in a standard set of financial statements but will otherwise be found in the notes to the financial statements.</p>

Financial Indicator	Specific Methodology
	<p><u>Net Debt</u>: The elements of Net Debt may be described slightly differently and should be found either on the face of the Balance Sheet or in the relevant note to the financial statements. All interest bearing liabilities (other than retirement benefit obligations) should be included as borrowings as should, where disclosed, any liabilities (less any assets) in respect of any hedges designated as linked to borrowings (but not non-designated hedges). Borrowings should also include balances owed to other group members.</p> <p>Deferred consideration payable should be included in Net Debt despite typically being non-interest bearing.</p> <p>Cash and cash equivalents should include short-term financial investments shown in current assets.</p> <p>Where Net debt is negative (i.e. an entity has net cash), the relevant Financial Target Threshold should be treated as having been met.</p> <p><u>EBITDA</u>: Operating profit should be shown on the face of the Income Statement and, for the purposes of calculating this Financial Indicator, should include the entity's share of the results of any joint ventures or Associates. The depreciation and amortisation charges for the period may be found on the face of the Statement of Cash Flows or in a Note to the Accounts. Where EBITDA is negative, the relevant Financial Target Threshold should be treated as not having been met (unless Net Debt is also negative, in which case the relevant Financial Target Threshold should be treated as having been met).</p>
<p>3</p> <p>Acid Ratio</p>	<p>All elements that are used to calculate the Acid Ratio are available on the face of the Balance Sheet in a standard set of financial statements.</p>