

# Mitigating Global Supply Chain and Customer Insolvency Risk

# Protecting your business from exposure to supplier and customer insolvency

There is no doubt that the economic environment in 2019, hampered by global trade wars and political uncertainty, made for a challenging year for many companies across a diverse range of sectors. This presents an inevitable counterparty risk heading into 2020, and additional global challenges in Q1 have already emerged with potential for significant economic impact, at least in the short term.

Financial distress and failure, through insolvency of customers or key suppliers, exposes business to substantial financial loss (through irrecoverable debts due from the insolvent customer/loss of on-going trade) and/or can cause major business interruption if an element of the supply chain suddenly and unexpectedly ceases production in circumstances where an alternative supplier cannot be readily sourced. With increasingly globalised operations, implementing legal and operational protection effective within the jurisdictions in which the operations and supplies take place, can provide valuable protection against exposure to financial distress in a business' structure and supply chain.

These risks are prevalent across sectors and industries and the implementation of specific legal and operational planning and on-going monitoring processes, tailored to the jurisdictions in which the operations/exposure may arise, will significantly mitigate the risk and effect of customer or key supplier insolvency, increase optionality from an early stage and thereby enable resulting business costs to be minimised.

Outlined here are some key warning signs and a number of solutions within the legal and operational toolkit available to improve a business' resilience to customer and key supplier financial distress.



## WARNING SIGNS

- Delayed payment/stretching of supplier credit.
- Re-negotiated payment terms sought/requests for deposits and upfront payments.
- Deteriorating service levels.
- Spurious/unjustifiable claims.
- CCJs, late filing of accounts, withdrawal of credit insurance, pending winding up proceedings.
- Auditor's report subject to qualifications.
- New/additional security being granted to an alternative funding provider.
- Market rumour/industry specific challenge/external shock.
- Over-leveraged business.
- Significant changes in management.

# Options to protect your goods/exposure



## CUSTOMER RISK

- Retain title to goods supplied until all payments due from the customer are made (key legal provisions properly incorporated in supply contracts can be very valuable).
- Periodic on-going monitoring:
  - are customer accounts filed on time?
  - any CCJs/winding up proceedings commenced?
  - audit of stock segregation conditions at customer premises if holding goods supplied which are not yet paid.
  - is credit insurance available?
- Review of financial position and payment terms.
- Monitor and review level of credit exposure.
- Are you an essential supplier (of utilities/certain IT services) which may be compelled to continue supply after the consumer enters an insolvency process?



## SUPPLIER RISK

- Is the supplier key to your supply/production operations?
- If the supplier ceased trading, what alternatives would be available and within what time frame?
- Monitor potential knock on impact on your ability to deliver an onward supply contract.
- In the event of supplier distress, would that provide an opportunity to acquire assets/bring part of production required for your business in-house?



## Early action to recover assets/ obtain payment

- Where concern is identified with regard to a customer or supplier, early action is key to avoiding potentially large exposure as an unsecured creditor upon an insolvency.
- At an early stage, key steps can be taken, including:
  - enhancement of protective provisions in your terms and conditions of trade (for example retention of title clauses and early insolvency triggers);
  - diversification of the supply of key goods and services;
  - audit and inventory of stock held by customer where title has been retained;
  - recovery action in respect of stock/suspension of credit terms absent payment of debts being made up;
  - written reminders of directors' duties/potential personal liability for directors acting in breach of duties to creditors and/or threat of early enforcement action/commencement of insolvency proceedings to apply immediate pressure for payment;
- procuring payment on account/guarantee from third party for continued supply;
- the taking of security and guarantees to elevate and enhance creditor rights;
- securing provision of pertinent financial information;
- if potential "essential supplier" obligations, early action and termination of arrangements may enable a supplier to extract itself from being subsequently compelled to supply if customer enters insolvency;
- early engagement with a key supplier in financial distress will enable optionality to be identified to secure continuing supply (with/without financial support to the current supplier or by procuring continued supply from an alternative).

# Key contacts

Our Restructuring team has significant experience in mitigating customer or supply chain risk in jurisdictions across the globe.



**Chris Roberts**

Partner, UK

+44 161 235 4265

chris.roberts@dlapiper.com



**Jamila Justine Willis**

Partner, US

+1 212 335 4969

jamila.willis@dlapiper.com



**Francesco De Gennaro**

Partner, Italy

+39 0668 880 509

francesco.degennaro@dlapiper.com



**Dietmar Schulz**

Partner, Germany

+49 89232 372 230

dietmar.schulz@dlapiper.com



**James Iremonger**

Partner, Middle East

+97 144 386 253

james.iremonger@dlapiper.com



**Caroline Texier**

Partner, France

+33 140 152 524

caroline.texier@dlapiper.com



**Egil Hatling**

Partner, Norway

+47 24 131 633

egil.hatling@dlapiper.com

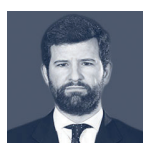


**Amelia Kelly**

Partner, Australia

+61 292 868 412

amelia.kelly@dlapiper.com



**Álvaro Cid-Luna**

Of Counsel, Spain

+34 91 788 7353

alvaro.cid-luna@dlapiper.com



**Peter Manley**

Senior Associate, London

+44 207 796 6056

peter.manley@dlapiper.com

