

**Date:** 21 June 2023

**Item:** Enterprise Risk Update – Efficient and High Performing Supply Chains and Effective Procurement (ER05)

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**This paper will be considered in public**

**1 Summary**

- 1.1 This paper describes Transport for London’s (TfL’s) position on Enterprise Risk 05 (one of ten level 0 risks across TfL) – “Efficient and high performing supply chains and effective procurement” and reflects the risk management approach to the increased scope of the risk, since the previous paper submitted to the Committee on 22 June 2022.
- 1.2 This paper outlines the scope of enterprise risk, current assessment, preventative controls, mitigation activities in place and improvement plans associated with upcoming Procurement and Commercial (P&C) improvement workstreams to reduce TfL’s risk across our procurement, commercial and supply chain activities.
- 1.3 A paper is included on Part 2 of the agenda, which contains exempt supplementary information. The information is exempt by virtue of paragraph 3 of Schedule 12A of the Local Government Act 1972 in that it contains information relating to the business affairs of TfL. Any discussion of that exempt information must take place after the press and public have been excluded from this meeting.

**2 Recommendation**

- 2.1 **The Committee is asked to note the paper and the exempt supplementary information on Part 2 of the agenda.**

**3 Background**

- 3.1 The P&C function (including the ownership of this enterprise risk) has recently transferred from the Chief Capital Officer to Chief Finance Officer (CFO). In parallel, the CFO has undertaken a stocktake of P&C activities and priorities, culminating in a ‘14-point improvement plan’ (Appendix 1) and a refreshed P&C scorecard for 2023/24 (Appendix 2) to monitor performance and associated strategic risks. This 14-point improvement plan covers a range of workstreams linked to TfL’s vision and values - colleague, customer, green, finance and our foundation – and, in conjunction with the refreshed scorecard, links to the strategic risks outlined in this paper. Activities in the Procurement

and Commercial Improvement Programme are contained in separate papers elsewhere on the agenda for this meeting.

- 3.2 TfL relies heavily on contracted goods, works and services to enable safe and reliable journeys for passengers. These goods, works and services are largely provided by our Tier 1 suppliers and their sub-contractors (together comprising the supply chain), many of whom are key to TfL's operation and success across all modes of transport.
- 3.3 Failure to sufficiently identify and appropriately manage risks in our procurement and supply chain functions, could result in impacts on safety, increase costs, cause delays to project delivery and interrupt operational services.
- 3.4 Following the notable increase in scope of ER05, the P&C and Risk and Assurance teams have defined four key risk areas for P&C – Supply chain disruption, Capability (of the P&C function), Compliance, and Value for Money. Any capability risks will be fed into a pan-TfL Level 1 people related risk. The process of re-assessing these risks is currently underway and due to complete by July 2023.
- 3.5 This paper outlines the risks in these four areas, along with their causes, impacts and mitigations (sections 4-6). Aligned to the 14-point improvement plan, a number of actions and activities have been outlined (section 7) to enhance our ability to manage and respond to risk in the medium to long term thereby reducing potential disruption.

## **4 Causes of risks**

### **Capability risk**

- 4.1 Capability risk refers to the potential lack of availability of skills and expertise in P&C, along with sufficient competence, resourcing, knowledge, training, systems and processes to deliver a quality service to our internal and external customers.
- 4.2 The primary risk at present is the challenge in recruitment and retention of staff, leading to a shortage of capacity, necessary expertise and impacting diversity within the P&C team. Current vacancies stand at approximately 140 roles, which represent around 25 per cent of total establishment.
- 4.3 Further capability risks have been identified, including:
  - (a) ineffective, fragmented and sub-optimal deployment of systems and complex processes and procedures across the P&C teams;
  - (b) frequent organisational changes have resulted in change fatigue and a disaggregated approach to learning, skills, development and succession planning in the P&C team; and

- (c) a lack of understanding of diversity and the associated skills and experience makes P&C less able to meet our aspirations on Equality, Diversity and Inclusion (EDI).

### **Compliance risk**

- 4.4 Compliance risk stems from a potential lack of adherence to the necessary guidelines and regulations to achieve fairness and transparency or the ability to demonstrate compliance with the Public Contracts Regulations 2015, Utilities Contracts Regulations 2016 and Concessions Contracts Regulations 2016, TfL's own internal procedures and GLA Group policies.
- 4.5 Further key compliance risks have been identified, including:
  - (a) TfL sourcing being conducted in a manner that does not meet regulatory requirements (non-compliant direct awards) or are non-competitive, due to short term planning, restrictive specifications and/or ineffective communication between internal directorates;
  - (b) P&C colleagues and systems, and wider business stakeholders, not being sufficiently prepared or trained for the introduction of the of the new Procurement Bill (currently expected to be enacted within the next 10 months);
  - (c) ineffective management and/or co-ordination of other legal/regulatory/Mayoral requirements such as the Freedom of Information Act 2000, General Data Protection Regulation (GDPR) and the GLA Group Responsible Procurement Policy; and
  - (d) Cyber Security may be breached within the complex systems used to facilitate the procurement source to pay (S2P) life cycle.

### **Supply chain disruption risk**

- 4.6 Supply chain disruption risk arises from the possibility of any event that causes disruption or delay in TfL's receipt of products, goods, works or services from its suppliers, and risks that may arise from supplier financial distress and wider economic and/or political issues which adversely affect our ability to manage our supply chain.
- 4.7 Further key supply chain risks have been identified, including:
  - (a) following Brexit and the subsequent Windsor Framework some supply chain disruptions remain, including delays to goods and services resulting from complex import arrangements and changes to customs procedures;
  - (b) the Russia-Ukraine conflict, where various factors continue to cause disruption to the supply chain, including the reduced availability of raw materials. Imports of iron and steel make up a large proportion of the material imported from Ukraine and are widely used in TfL's construction of roads, railways and other infrastructure;

- (c) China/ Taiwan tensions may threaten trade, particularly the trade in semiconductors, which are crucial to modern electrical and transportation systems used for a wide range of operations across the TfL network;
- (d) climate change increasing the risk of disruption to access to raw materials, manufacturing, transportation and logistics; and
- (e) macroeconomic headwinds including high inflation and interest rates within the UK and global economies.

### **Value for money risk**

- 4.8 Value for money risk stems from failing to maximise our commercial leverage when sourcing goods, works and services together with potential sub-optimal commercial management practices and the consequences of historical strategic sourcing decisions.
- 4.9 The risks include not being able to fully leverage our economies of scale or disaggregation of our spending power, ineffective long term planning, generating complex specifications, and supplier-owned intellectual property for key components limiting our ability to compete.
- 4.10 Further key value for money risks have been identified, including:
  - (a) historical sourcing decisions leading to TfL being dependent on original equipment manufacturers (OEM) suppliers which are extremely difficult and highly costly to unwind;
  - (b) insufficiently detailed pipeline of procurement activities and future requirements across TfL;
  - (c) production of overly complex or non-generic specifications and the use of local and/or out of date product specifications and standards; and
  - (d) failure of TfL to show third party auditors that TfL is achieving good value for money.

### **Other associated risks**

- 4.11 P&C recognises that it has key relationships with: Safety Health and Environment 'Inability to deliver safety objectives and obligations' (ER01); IT and Cyber 'Significant security incident' (ER04); and Finance 'Financial resilience' (ER07), are other Enterprise risks reported at Executive Committee Level. Any relevant P&C risks that are identified shall be shared with the other Enterprise risk teams to ensure all risks are captured and appropriately managed.

## **5 Impacts**

- 5.1 There are a wide range of risks which exist in both tactical and strategic sourcing and the management of our supply chain which could negatively impact TfL. As outlined below, these could manifest in adverse safety, operational, commercial, and reputational impacts.

### **Capability impacts**

- 5.2 High vacancy rates and a challenging recruitment environment result in increased workloads, negative impacts to the health and wellbeing of colleagues. This may lead to a reduced ability to meet TfL's sourcing requirements on time and to budget further driving higher costs via the need for non-permanent labour.
- 5.3 The lack of a centrally co-ordinated P&C learning, ethics and development plan increases the risk of error and potential fraud, negatively impacts staff retention and results in difficulty in recruiting the right type and caliber of staff. Combined, this has the potential to reduce the overall skill level of P&C.
- 5.4 Insufficient understanding of diversity and inclusion may adversely affect colleague engagement, wellbeing and retention, leading to a diversion from TfL's values.

### **Compliance impacts**

- 5.5 A breach of current regulation, legislation or ethical standards could lead to TfL being subject to financial penalties, compensation claims, procurement challenges, contracting delays, negative political/public perception and increased costs of operation.
- 5.6 Non-compliant procurement may cause TfL's governance or Mayoral standards or policies to be breached and failure to demonstrate best value for public funds, giving the opportunity for error and fraud.
- 5.7 Failure to deliver social value and/or our sustainable procurement objectives may impact TfL's ability to compete in the labour market to secure diverse and best in class talent.
- 5.8 Data may be accessed or abused by way of a cyber intrusion resulting in, for example, theft of sensitive data.

### **Supply chain disruption impacts**

- 5.9 Logistic and imports disruption impact lead times and costs for goods deliveries to TfL, particularly those directly sourced from EU suppliers. This affects important suppliers such as Alstom, Matisa, Siemens, CAF and SKF which all rely upon supplies from Europe for key parts and components to maintain and support our rolling stock, infrastructure and rail systems.

- 5.10 High inflation and significant fluctuations in commodity and utility prices impact supplier financial sustainability, potentially leading to insolvencies, contractual disputes and increased costs to TfL.
- 5.11 Unavailability of materials, commodities, finished products and skilled labour caused by geopolitical disruption may lead to project delays and reduce operational availability, impacting the performance of TfL services and the associated revenue. The China-Taiwan tensions have the potential to impact operational systems such as track to train control, signalling, rolling stock and power control systems due to the reliance on semiconductors as Taiwan is a significant supplier of these components and currently produces around 92 per cent of the world's most sophisticated chips. Additionally, South-East Asia, in particular South Korea and Japan, are significant suppliers of related technologies. Any conflict in this region therefore poses the risk of a significant detrimental effect on related supply chains and trade routes.
- 5.12 Impacts of climate change may lead to local and global manufacturing and logistic disruptions, increased sourcing costs, reduced access to raw materials and fuel price fluctuations.

### **Value for money impacts**

- 5.2 Failing to consider the long-term effects of sourcing decisions impacts the ownership of intellectual property and increases whole life costs which affect TfL's ability to deliver best value, retain flexibility of supply and optimise lead times.
- 5.3 The ineffective planning of procurement may cause TfL to disaggregate spend, reducing our ability to consolidate our supply chain and leverage economies of scale, resulting in potential overspend and sub-optimal strategic supplier relationship management.
- 5.4 Macroeconomic challenges including increased inflation and interest rates affect the UK economy, increasing the risk of supplier insolvencies and leading to shortages of goods or services and additional costs in sourcing alternative suppliers, causing possible instability in service delivery and leading to public relations concerns, political risk and poor media representation.
- 5.5 Using non-generic, out of date or overly complex specifications reduces our ability to maximize competition, value for money and/or deliver innovative, safe and efficient solutions. This also increases demand on internal engineering resource, leading to longer product assurance and approval timescales.

## **6 Current Mitigations**

- 6.1 The following mitigation measures, inclusive of the recent CFO stocktake and implementation of the 14-point P&C improvement plan, will serve to reduce our risk exposure across ER05. The strategic management of the risk will be

supported via regular senior risk reviews and an enhanced P&C scorecard to maintain visibility, direction, and delivery of targets.

### **Capability risk mitigations**

- 6.2 P&C has improvement workstreams to increase its capability and performance. As part of that activity P&C is planning a number of targeted recruitment campaigns to fill critical vacancies e.g. in the Technology and Data and Capital teams. This will involve improving P&C's marketing to potential candidates and being more active in the candidate market for procurement and commercial resources.
- 6.3 Improving awareness of EDI, including mandatory inclusion of EDI objectives in personal development plans, provision of training and e-learning and the promotion of colleague network groups to help create environments where people feel empowered and engaged.
- 6.4 Increased training availability by establishing a learning and development plan to improve commercial competence, including the provision of training on ethics, fraud prevention, environmental matters, carbon literacy and modern slavery including training for the upcoming procurement regulations.
- 6.5 Cabinet Office and Department for Transport (DfT) engagement and collaboration to leverage central best practice sharing and training provision. The P&C team regularly engages with the DfT, attending their Strategic Supplier Working Group and working collaboratively to share non-confidential information on suppliers' financial standing and best practice.
- 6.6 SAP Ariba, an end-to-end procurement software solution, has been implemented across P&C including a risk management tool that has provided a consistent approach and workflow to activities.

### **Compliance mitigations**

- 6.7 The P&C Governance, Risk and Assurance (GR&A) team is being developed to enhance assurance activities (including lower value activities where fraud and error is more likely) and co-ordinate the management of a P&C strategic risk register to drive targeted improvements. The GR&A team will have additional headcount resource secured over the current financial year, to support delivery (one additional headcount in each of Risk and Assurance).
- 6.8 Increased compliance via further support and guidance on SAP Ariba and use of the Management Framework, to provide a clear vision of our methodology for procurement and commercial activities, to improve performance and to support P&C to achieve best value for money.
- 6.9 Simplifying our governance templates to streamline process, reduce administration and provide greater visibility of sourcing decisions, including establishing the root causes for single source requests, so that they can be addressed via continuous improvement.

- 6.10 Develop our security approach to appropriately address our cyber security requirements over the S2P lifecycle.

### **Supply chain disruption mitigations**

- 6.11 Monitoring the financial health of 251 suppliers who are critical to TfL's operations. Thirty-four of the 251 monitored suppliers are currently considered to be at high financial risk. Failure to monitor and respond appropriately to poor supplier financial health could result in significant disruption to TfL.
- 6.12 The P&C Supplier Relationship and Capability team are delivering improvements to supplier relationship management and intelligence, with a particular focus on our key and critical suppliers. The team consolidates our supplier intelligence information, manages supplier segmentation, and promotes effective relationships with our suppliers to reduce the impacts of disruption in the supply chain.
- 6.13 Macroeconomic market awareness will enable procurement strategies to consider less complex supply chains, prioritizing UK and local supply chains (where possible) which could support the growth of UK industries and reduce the risk from global disruptors. In particular with regard to the emerging situation between China and Taiwan and its possible impacts on global trade and shipping, P&C will use appropriate guidance/advice from government departments and other relevant bodies to manage and mitigate supply chain risk.
- 6.14 Establish a refreshed P&C supply chain risks and issues register which also records mitigation plans. The register is an important tool for liaising with business stakeholders to help with the planning and control of mitigations being undertaken.
- 6.15 Provide clearer and more consistent reporting to highlight critical supplier financial health and emerging supply chain risks and issues.

### **Value for money mitigations**

- 6.16 Using new systems (SAP Ariba and PowerBi) to leverage TfL's commercial data. TfL has a significant addressable annual spend of circa £4bn and the improved availability of this information will assist P&C teams when forming sourcing strategies and preparing for commercial negotiations.
- 6.17 P&C colleagues are working with asset managers to reduce our reliance upon OEM suppliers to drive towards the sourcing of generic components with unrestricted IPR. Where it is feasible, P&C will support the identification and prioritization of opportunities to reverse engineer and identify alternative equipment suppliers/manufacturers to reduce our reliance on OEMs, improving competition. TfL are also working towards sourcing generic components to standardize our specifications in accordance with industry and international standards, supported by market engagement.



- 6.18 Deliver procurement and contract savings: One of P&C's strategic goals is to enable significant procurement and contract savings, with £113m achieved in Financial Year 2022/23 (compared to the original target of £85m). Further savings will be delivered in 2023/24 made up of budgeted savings, revenue generation and cost avoidance.
- 6.19 Coordinated approach to the management of financial failure of critical suppliers by enhanced third party data monitoring, and expedited communication to relevant P&C and operational teams. Contingency plans for the key suppliers are being reviewed and further developed where necessary.
- 6.20 Improved efficiency of governance procedures to reduce time to source lower value (under £125,000) goods and services while providing greater transparency to sourcing decisions via improved documentation of quotations and benefits, increasing commercial vigilance of lower value spend items and helping to prevent fraud.
- 6.21 The engineering team are refreshing their approach to product approval catalogues/lists which will provide up-to-date solutions/standards for our goods and supplies, leading to greater opportunity for competition taking advantage of supply chain innovation.

## **7 Strategic Improvement Workstream Actions**

- 7.1 The development of the 14-point improvement plan has led to new activities which will further support the mitigation of risk across ER05 and the P&C function. These include:
- (a) the P&C Central Enabling Team (CET) has been combined to consolidate and strengthen CET support across P&C. This will create synergies, better matrix working, consistent strategic objectives and bring an end-to-end approach to the identification, monitoring and management of risk and supplier intelligence;
  - (b) production of a P&C Supplier Risk, Intelligence & Relationship Management Strategy; this will include working together to review the pipeline to identify common issues facing the P&C function. Focussing on the most directly controllable risks will give the best improvements to our risk exposure. This will improve our ability to manage both risk and supplier intelligence, and will enable delivery of a process to ensure risks and issues are appropriately captured across P&C;
  - (c) improvement of our tool for monitoring supplier financial health by enhancing our current methodology including the monitoring of several data points to assess the financial health of a supplier and the consequent risk to TfL. The methodology will be expanded to achieve a more accurate measure of a supplier's risk to TfL;

- (d) quarterly risk forums will be held to support senior leadership and provide visibility and focus on ER05 risks ensuring that risks are being managed, mitigated and reduced; and
- (e) a Supplier Relationship Management programme is being implemented by the Capability and Supplier Management team in P&C to develop strong supplier relationships with TfL's key suppliers focusing on collaboration, risk identification and mitigation, cost reduction and strategic value enhancement across core contracts.

**List of appendices to this report:**

Appendix 1: P&C 14-point improvement plan and workstreams

Appendix 2: Proposed P&C scorecard for 2023/24

A paper containing exempt supplementary information is included on Part 2 of the agenda.

**List of Background Papers:**

None

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## Appendix 1 – Procurement & Commercial 14 improvement workstreams

TfL Plan	#	P&C Improvement Workstream	Enabling Principles
Safety & Security	1	Prevent Error & Fraud	<ul style="list-style-type: none"> <li>✓ <b>Self-delivery</b> by us as a leadership community with support from colleagues across P&amp;C</li> <li>✓ <b>Engagement and inclusivity</b> for P&amp;C colleagues and customers</li> <li>✓ <b>Diversity &amp; Inclusion</b> to underpin everything we do</li> <li>✓ <b>Coordination and collaboration</b> across workstreams</li> <li>✓ Understanding relevant <b>common cross-cutting themes and interdependencies</b></li> <li>✓ Identification and delivery of <b>financial and non-financial benefit</b> contributions by P&amp;C</li> <li>✓ Supportive <b>leadership, oversight</b> and clear <b>governance</b></li> </ul>
	2	Improve Compliance	
Colleague	3	Increase our Capability & Performance	
	4	Improve our Inclusivity & EDI	
	5	Improving Colleague Engagement	
	6	Simplify our Governance Templates	
	7	Change Lessons Learned	
Customer	8	P&C as a Trusted Business Partner	
	9	Further Embed Source-to-Contract	
	10	Manage our Critical & Strategic Suppliers	
	11	Deliver the Capital Improvement Plan	
Green	12	Deliver Responsible Procurement	
Finance	13	Deliver Procurement Savings	
	14	Keep to Our Budget	



## Appendix 2 – Procurement & Commercial 2023/24 Scorecard

### P&C FY23/24 scorecard

Roadmap	Measure	Target	Floor target
 <b>Safety and Security</b>	Over threshold single source rate	1.2%	1.5%
	CAM compliance rate	80%	75%
	Deliver key milestones in P&C Continuous Improvement Workstreams: - Prevent Error & Fraud, Embed Source to Contract, Improving Our Inclusivity & EDI, Deliver the Capital Improvement Plan and Managing our Critical & Strategic Suppliers	To be set individually	To be set individually
	Complete Audit Actions on Time	100%	N/A
 <b>Colleague</b>	Total engagement	57%	56%
	Temporary staff (NPLs and consultants) as % of FTE	18%	20%
	Attendance	96%	95%
 <b>Customer</b>	Internal customer survey	TBC	TBC
	On time project delivery	90%	80%
 <b>Green inc. Responsible Procurement</b>	% of spend with SMEs	12.0%	11.0%
	% staff completing Carbon literacy training	70% of permanent staff	60% of permanent staff
 <b>Finance</b>	Cash releasing benefits	£45m	£24.4m
	- of which recurring	TBC	TBC
	Profitable revenue generation benefits	TBC	TBC
	Cost avoidance benefits	£71m	£60.6m
	Net Opex spend vs budget (P&C team cost)	At or below budget	N/A