



## Scottish Affairs Committee Business, Innovation and Skills Committee

Oral evidence: [Impact of the closure of City Link on employment](#), HC 928

Tuesday 10 February 2015

Ordered by the House of Commons to be published on 10 February 2015.

Witness:

- At 2.30pm
- David Smith, former Chief Executive, City Link

[Watch the meeting](#)

Members present: Members present: Mr Ian Davidson (Chair), Mr Adrian Bailey, Mr William Bain, Paul Blomfield, Katy Clark, Mike Crockart, Jim McGovern, Ann McKechin, Graeme Morrice, Pamela Nash, Mr Alan Reid

Questions 577-844

Witness: David Smith, former Chief Executive, City Link gave evidence.

**Q577 Chair:** We have been having a number of sessions looking at events surrounding the closure of City Link. I am grateful that you have been able to come along to see us today. Would you introduce yourself and tell us your previous position and your background for the record?

**David Smith:** Good afternoon, Chair, and members. My name is David Smith. I am the ex-chief executive of City Link Ltd, and obviously the subsidiary company, City Link (Properties) No. 1 Ltd.

**Q578 Chair:** I want to start off by asking you what, in your opinion, led to the collapse of City Link.

**David Smith:** City Link was a business that was put together back in 2007 by Rentokil buying two companies, essentially, City Link and Target. From that date onwards, the consolidation of the two businesses did not go well, and, in fact, the business never made a profit in its entire time from 2007. I joined the business at the end of 2011. In that December, my first month, it lost £7.5 million. In fact at that year end it lost £66 million or £67 million. It was always a business in distress. I was brought in to try to turn that around.

Essentially, we had three big problems. The first was that the IT of the business was two separate businesses put together and not properly invested in over a long period of time. The second was the operational processes of the business. Those processes had not kept pace with all the competitors in that time period. The third was the commercial contractual arrangements that the business had struck in the period between 2010 and 2011, fundamentally. We made great progress on all three of those, but ultimately we were not able to fix them all in time with the amount of cash that we had to turn the business around.

**Q579 Mr Bain:** We have been told that between November and December last year, City Link directors and Better Capital were looking at a range of options to try to secure the future of City Link. What options were you exploring?

**David Smith:** In fact, we started the review process on 9 October. That review process was to look at, as it turned out, a range of 10 options across that time period. In essence, we were looking at continuing with the existing business plan we had started that year with—a radical restructure of the business to focus more closely on the business-to-business market as opposed to the generality of the parcels market; an opportunity or set of opportunities to bolt on to the business, to bulk it up and make it larger so that it was able to compete more in the wider marketplace; and then potentially a trade sale as the alternative view to that. In fact, we looked at 17 different potential trading partners in that time period. We also then looked at the alternative of a structured close-down of the business and an unstructured close-down of the business in various different guises. That was done to give us the entire range of potential outcomes so that we could see what the best way forward for the business was.

**Q580 Mr Bain:** Broadly, it was about trying to get the business into a shape where it could perhaps be sold on as a going concern or, alternatively, looking at buying elements to make the business more profitable. There was perhaps another option which you were also considering, wasn't there, which was through the establishment of City Link B2b, a subsidiary company registered on 9 December? Can you explain what that move was designed to achieve?

**David Smith:** Yes, I can. As part of the option to slim down the organisation and focus on the business-to-business market, to make that work we were required to slim down the physical network of the organisation—in other words, the number of depots that we had. The City Link B2b limited company was set up specifically to enable us to move the property leases for the sites where we were going to stay into that new vehicle. No trading ever took place inside that company. In fact, at the moment we are in the process of striking it off.

**Q581 Chair:** Could we pause for a moment so that a member of staff can move the microphones slightly? We are not quite picking up the sound. It's not you; it's us.

**David Smith:** Is that better?

**Chair:** Yes, that does seem to be a bit better.

**Q582 Mr Bain:** There are different views on the establishment of that subsidiary company. The RMT have expressed quite strong concerns about why it was done. As you alluded to, you were looking at the reduction in depots, and presumably a reduction in staff thereby. The other aspect which Better Capital and others have raised is whether that

subsidiary company was going to be used in order to freeze City Link's debts and give it time to restructure. Can you address directly what the purpose of setting up that subsidiary was?

**David Smith:** I have given you exactly the reason why it was set up.

**Q583 Mr Bain:** Will you address each of the two points that I have just put?

**David Smith:** I do not know why the RMT believe anything different. They certainly were not a part of any of the conversations to set up the organisation. I cannot answer for them. In terms of a physical debt restructure of the organisation, the plan that we were pursuing as directors did not require us physically to restructure the debt structure of the business. It required Better Capital to continue to invest in the business. There was no restructuring vehicle required for that solution.

**Q584 Mr Bain:** Could you have explored debt restructuring in more depth as another mechanism to perhaps save the business?

**David Smith:** We did look at administrative restructuring. We looked at that as part of the 10, but it was not specific to the B2b vehicle that you asked me about.

**Q585 Mr Bain:** What Mr Jon Moulton told this Committee was that prior to City Link going into administration you had been looking at restructuring, as well as possible buyers. Is there more that could have been done, either by you or with the assistance of the administrators, to help with the restructuring?

**David Smith:** I would never say never. However, we went through an extensive process with external professional advisers, lawyers, specialists in turnaround, specialists in cash management and specialists in property. We took external advice on the mechanics that you would go through to do a restructuring of debt exercise, but we did not find an outcome that would work for us or for Better Capital, or for the landlords and other interested parties for that matter.

**Q586 Mr Bain:** At what date did you reach a final assessment that City Link could no longer continue as a going concern?

**David Smith:** That is very clear. That was 22 December at about 8.02 in the morning when Jon Moulton told us that Better Capital were no longer going to support the business.

**Q587 Mr Bain:** On 22 December you had no plans to trade until 26 December.

**David Smith:** On 22 December at 8.02 we then went into a conversation with our advisers and with Ernst & Young to decide what to do and what was the best way to put the business into administration. At the end of those conversations, with all of that input, we concluded that it was better for the body of creditors in the round to continue to trade through to Christmas eve, or Christmas day-Boxing day. It does not actually make any difference in the trading sense. To have not done that would have resulted in panic and severe difficulty for customers, suppliers and the general public in the movement of parcels. That was why we made that decision.

**Q588 Mr Bain:** When did you e-mail suppliers to say that City Link was aware of unfounded rumours that the business would cease trading on 24 December? You told the suppliers that those rumours were untrue. Can you confirm when that e-mail was sent?

**David Smith:** To be clear, I sent an e-mail to my senior management team on 21 November. I did not send anything directly to any suppliers. The purpose of the e-mail was to help my management team in conversations that they were having with suppliers, basically to give them the background to what was going on in the generality of the review process and to ask them to ask suppliers if necessary to talk directly to me or my finance director. A few suppliers did that; I can think of five or six that did that—talked to me directly. Generally they did not.

**Q589 Mr Bain:** Do you not think it was a worrying state of affairs that this e-mail found its way to suppliers, purportedly gave them some reassurance and then the company ends up going into administration less than a month later?

**David Smith:** If we look at the content of the e-mail on the 21st, basically the first thing it was saying was that we were content that we were trading and that we were going to continue to trade. At that point we certainly had that view. We had that view right through to 22 December. Secondly, it talked to the need for us to protect our name in the marketplace. In fact, subsequent to the 21st we took action with two parties around potential defamation of the company's name. Thirdly, it talked to the investments we had, and were continuing to make, in the business around handhelds as an example of the support that we were getting from Better Capital. We had made those investments, and those handhelds were in the business.

**Q590 Mr Bain:** The company went into administration on Christmas eve. The first redundancies were announced on Hogmanay, or new year's eve. Do you consider that that allowed enough time for potential buyers to put a bid together?

**David Smith:** We had been through a very extensive review of potential credible buyers in the weeks leading up to 22 December. We talked to 17 potential buyers. We found only one that had the interest but also the financial muscle to move to a credible diligence process. In fact, they fell away before the end of November as well. It is always possible that there may be somebody out there if you are prepared to wait long enough, but there is a balance between the time you want to wait to find that and the fact that the business is losing a significant sum of money every day you do that. The balance of the creditors' position also has to be factored into the judgment.

**Q591 Mr Bain:** That all comes from the Enterprise Act 2002. Did you seek any assistance or advice from BIS? I have experienced this as a constituency Member, and I am sure other colleagues have as well: where a company is in difficulty, there is assistance that BIS can provide. Did you liaise with Government Ministers at all to let them know that the business was potentially in difficulty, and whether any assistance could be provided by Government?

**David Smith:** No; the directors did not do that. That was in fact done by Better Capital in the pre-period, and it was done by Ernst & Young in the post-period.

**Q592 Mr Bain:** You are saying that Better Capital approached the Government.  
**David Smith:** Yes, and I did not know that myself until I saw the transcript of Jon's presentation here a few weeks back.

**Q593 Mr Bain:** That is very interesting. Are you aware of what particular types of support they sought from the Government, perhaps in terms of loans or help with restructuring? What advice and help were they seeking?

**David Smith:** I do not think they were. From the transcripts that I read, I believe that they were saying that potentially the business would be in difficulty and therefore they needed to start thinking about gearing up for jobseeker's support and things like that.

**Q594 Mr Bailey:** Let me go back to the issue around B2b. I am trying to understand the financial rationale for that particular decision. As I understand it, you basically set up a vehicle in which to cede the ownership of the leases of the depots that you did not want to use. Is that right?

**David Smith:** No, that we did want to use.

**Q595 Mr Bailey:** You did want to use them.

**David Smith:** Yes.

**Q596 Mr Bailey:** What was the purpose of that?

**David Smith:** We had taken external advice from property specialists. In the run-up to trying to find a solvent solution we were in negotiations with pretty much every one of the landlords, either to reset the lease time and the amount of money that we would pay for those leases or to look to terminate the leases early, essentially, for the ones that we did not want to be in. The advice that we had was that the negotiating position those advisers would be able to get would be improved if we could set up a separate vehicle to demonstrate that we were going to move from one world to another world. It was no more complex than that.

**Q597 Mr Bailey:** Basically, you did it to cut your costs.

**David Smith:** Yes. It was part of the turnaround process to cut the cost base of the business.

**Q598 Mr Bailey:** What were you doing with the depots you did not want to use?

**David Smith:** Those were in an extensive period of negotiation. I think there were 19 sets of negotiations going on. We had 17 potential agreements in place, none of which was executed in the end. Those agreements effectively terminated those sites, or would terminate those sites, during the early part of 2015 through to June time 2015, because we were moving into a different market and did not need as many sites.

**Q599 Mr Reid:** In his evidence, Jon Moulton told us that City Link lost £3 million in December 2014. I would have thought that the run-up to Christmas would be

the busiest time for a parcel business. Can you explain why there was such a big loss in the run-up to Christmas?

**David Smith:** Yes, I can. It was the busiest time in terms of volume, but the pricing positions that I had inherited in 2011 had a number of contracts that were set for a long period of time—two, three or four years. The largest of those contracts—I cannot tell you which company, because obviously that would be confidential—was very loss-making; in rough terms, for every parcel we were delivering we were losing about £1. If I tell you that that company was about 28% of all my volume for the month of December, you can start to appreciate the difficulties. In addition, we had more physical premises than we needed for the volume that we were carrying. We had a significant proportion of fixed costs that were not being covered by the volume that the business was carrying, hence the reason why we were looking at restructuring in the 2015 period.

**Q600 Mr Reid:** Those seem quite bad figures. What made you think that, despite all those bad figures, even up to 22 December, you could still make a go of City Link?

**David Smith:** Because a number of the elements of the plan were already well in train. For instance, we had served notice on that contract, and we were likely to come out in the early part of January 2015. We had made great progress on the physical restructuring of the sites. We had made great progress on the restructuring of the overhead base of the business, and we had built, although not completed the work, on the plans around the operation that would be needed for a smaller business. We had also put price increases into the marketplace in late December. We had served notice on our postal business, which was loss-making following the restructuring of Royal Mail; we could no longer make money in that part of the market. We had also made great strides in terms of the parcel broker part of the market, again to serve notice on loss-making accounts. We had a very clear line of sight and a robust plan that took us from December through to the end of May, and took us from losses to break even to profit.

**Q601 Mr Reid:** You mentioned earlier that you had inherited two separate IT systems that were not up to the mark.

**David Smith:** Yes.

**Q602 Mr Reid:** Was any action being taken to get a proper and modern IT system in place?

**David Smith:** Yes. The business is fundamentally an IT business. You may think of the trucks and the vehicles, but to move any volume of parcels and know where they are, you need good IT behind it, because you need to be able to read the barcodes. When I joined the business it was not able to measure collections. It was not able to measure movement through the network. It was only able to measure the delivery. It was not able to measure individual parcels, only bundles of parcels together. It was not able to work out at all the profitability of each individual item as it moved through the network.

We had made great strides on all those elements. We also made great strides in terms of simplifying our customer care environment and our web front end, but we were still left with two operating systems from the legacy days of the two businesses coming together that needed to become one. From a customer point of view, if you wanted to take every one of our



products, you may have needed 18 different ways of connecting to us, which is clearly nonsense. There was still quite a lot to do, and the plan obviously contemplated completing that journey in 2015, and in fact 2016.

**Q603 Mr Reid:** When Mr Moulton was giving his evidence it was not very clear to me whether the decisions about which parts of the business to concentrate investment on were being taken by the Better Capital board or by the City Link board. Could you clarify that for us?

**David Smith:** They were very clearly taken by City Link. We had day-to-day responsibility for the direction of the business. We presented those plans to Better, of course—the large material investments that we made; an example being the sorting equipment that we put into Coventry in the summer last year. They would always get signed off by Better Capital, but they would be investment recommendations from the board at City Link.

**Q604 Mr Reid:** Clearly Better Capital put a lot of money in—£40 million—so presumably at the start of the process they believed, as well as the City Link board, that the business could be turned round. Why do you think that, despite the initial belief that that could happen, it was not able to turn round?

**David Smith:** Certainly we all believed it could be turned round. I think the board still believed it could be turned round on 22 December. What we believed though was that it would take longer than we originally thought, and certainly it would cost more money to do that. Like Better Capital, we put money into the investments at the start and obviously lost those as well. We were certainly involved.

In the end the business failed because, first, we did not get to grips quickly enough with the IT; secondly, the operational changes that we put in through the year in 2014 proved to be too difficult to do at the same time as we were changing the IT; thirdly, the commercial environment around us was changing rapidly and we were not able to exit quickly enough contracts that were loss-making; and, fourthly, fundamentally, we could not find an investment partner to complete the journey with us.

**Q605 Mr Reid:** What was changing about the world around you?

**David Smith:** If you go back to 2013 there was the Royal Mail privatisation, which had a profound impact on the overall market.

**Q606 Mr Reid:** In what way?

**David Smith:** For instance, we carried post as well as parcels, and following the privatisation we found it very difficult to be competitive in that part of the market. In terms of the HS2 decision to drive the new line right through the middle of Birmingham, unfortunately for the rest of us but fortunately for UK Mail, it enabled them to rehouse their hub and invest in a new set of hub facilities, which changes the market dynamic. More generally speaking, of course Amazon came into the marketplace as a carrier as well as a customer of the carriers. Those elements all shifted the price points of the market quite sharply.

**Q607 Mr Reid:** With the benefit of hindsight, which is obviously a wonderful thing, was there anything different you could have done, or was it all inevitable?

**David Smith:** I think I would have gone back to the sale and purchase time, in 2013, between Rentokil and Better Capital. With the benefit of hindsight, we should probably have had £60 million behind us and not £40 million. We probably should have been given a longer time to come off the IT estate that was fundamentally Rentokil's IT estate and to set up our own. With hindsight, you would say that we probably should have done those two things.

**Q608 Mr Reid:** Why did it take until 22 December to arrive at the decision that you had to go into administration? Why wasn't that 18 months earlier?

**David Smith:** Because until that point we had, first, a viable external buyer for the company. Secondly, we had a viable internal option that would demonstrably turn the business around by May the following year, provided that you had the backing to do it, and we were given support by Better to continue that process. If you had not had that, of course you could not have made that decision.

**Q609 Chair:** I want to pick up a couple of points on your comments. The first question relates to the major loss-making contract or contracts. Were they inherited from the Rentokil days, or were they signed up to by yourselves once you had taken it over?

**David Smith:** You have to remember that I covered both periods, including Rentokil, because I was in from the end of 2011. I had not joined the business when all those contracts were signed, but in Rentokil's time the strategy was more to fill the network than it was in Better's time when they were looking more at the cost. The contracts were predominantly signed in Rentokil's time before I joined, but one or two were after I joined.

**Q610 Chair:** Why were people signing up to contracts that were losing them money? Did they not know at the time that these were losing them money, or were they only losing them money because you had less volume, and they would have made you money had there been more volume, but then the nature of the business changed?

**David Smith:** In the early part of 2012, we did not have any customer profitability data at all. That came through my finance director coming in and bringing that into the business. The contracts were really being signed against whatever was the market rate. Once we had done the analysis and could understand what our real, true costs were, it was clear that they were loss-making. The second piece is that as volume declined, and our fixed costs therefore increased the overhead take that you would need out of each contract, a number of the contracts were loss-making at that point.

**Q611 Chair:** When Better Capital took over, or bought the company for £1, are you telling us that they did not know at that stage that lots of the big contracts they had were unprofitable?

**David Smith:** I believe they had an idea, because I think we presented it to them.



**Q612 Chair:** “Had an idea”—we’ve all got ideas. I wanted to be clear about whether or not they actually knew at the time what they were getting into, and that they were taking over contracts which were, at the time when they were buying, unprofitable?

**David Smith:** Yes; they would have known that.

**Q613 Chair:** I am just trying to clarify that. They knew what they were getting into at the time when they bought you.

**David Smith:** Yes.

**Q614 Chair:** I want to clarify a second point. You made a comment, if I caught you correctly, about putting money in. You had put money in. Did I pick that up correctly? You are one of the shareholders and you have lost money. I cannot remember having seen that anywhere else at all—maybe that’s just me, but the staff certainly have not drawn it to our attention.

**David Smith:** When City Link was purchased, the holding company that sat above it was called BCAP City Link (UK) Ltd. It was only set up to buy City Link and to invest in it. We are shareholders as directors; when the company was set up we became shareholders in that entity, but of course that entity will also go into administration down the line. That is why we will have lost money in the thing.

**Q615 Chair:** Presumably, you were quite substantial shareholders because Better Capital did not put in all that much equity. My understanding is that, of the £40 million they put in, about £39.999 million or so was in debt. Even if you put in, not quite tuppence but a relatively small amount, it would be quite a high proportion of the equity shares.

**David Smith:** Yes. I personally had a 5% share in the company.

**Q616 Chair:** What about the other directors? Was it about the same?

**David Smith:** I think between us it was about 17.5% or 18%—something like that.

**Q617 Mike Crockart:** Looking at the figures on the profit and loss for a second, in 2012 City Link made a loss of £27.5 million. In 2013, it made a loss of £14 million. That seems to look like a very high level of turnaround for the company. Was that your view?

**David Smith:** Yes. If you take it back a year earlier when we lost £68 million, it was £68 million in ’11, £27.5 million in ’12 and £14 million in ’13, so that was indeed the trajectory of the business over that time period. The budget for ’14 was to start to cross over that break-even line, and to start to make a return. Through the end of ’13, and in fact through the first quarter of ’14, we were on budget and on track.

**Q618 Mike Crockart:** In your opinion, what turned this around and prevented any further investment from being likely to come forward? You talked about various events that had happened—Royal Mail privatisation and HS2—and you said that shifted the price points in the market.

**David Smith:** To a degree, but to be clear they were not at the centre of what was happening at City Link. They were part of the wider market backdrop. The centre of what was happening at City Link was that the business was required, through the sale and purchase agreement with Rentokil, to come off the IT systems of Rentokil at the end of March 2014. To bring that to life and scale for you, there were something like 500,000 IT patches, 350 servers, a complete new data centre and a complete new set of customer service systems with complete migration of all of our interconnect networks from the old Rentokil world into a new BT world. In other words, it was a huge undertaking, and most companies would never undertake changing the whole IT world like that inside a year.

At the same time as we were doing that we were also being pushed, and were pushing ourselves quite hard, to complete the operational changes that we needed to make the business profitable. It was the combination of doing those two things at the same time that proved to be too difficult for the business through the spring and early summer of 2014. In the early summer of 2014, we essentially stopped the operational change programme and went back to fixing the IT, because we could not do it all on one day at the end of March.

**Q619 Mike Crockart:** During spring and summer of 2014 you knew that there were significant concerns and problems that you had to deal with.

**David Smith:** Indeed we did. In May, we identified to Better Capital that we were going to be significantly behind our budgets. In June, we wrote a paper to Better Capital outlining that we would be needing £20 million to £25 million-worth of additional funding. In August, I and Better Capital's operating partner went to the Guernsey fund directly to take them through that plan and to outline to them the need for £20 million to £25 million-worth of funding. They continued to be very supportive. They continued to understand the challenges that we'd had and what we were doing about them to fix them. Indeed, they invited us to continue to invest in things like the handhelds that arrived in November.

**Q620 Mike Crockart:** What made you feel able in October to go out to the trade press with a bravado performance saying that "City Link remains a business in turnaround, and our results for 2013 represent a great step forward on that journey...We are not there yet but the continued support of Better Capital—both in terms of investments made so far and in terms of future commitments—means that we will complete our turnaround story and that this business and our customers have a bright future to look forward to together"?

**David Smith:** Those were comments specifically about the 2013 results.

**Q621 Mike Crockart:** And projecting that forwards.

**David Smith:** Yes, but that was the timing. At that time, we knew that the results were okay at top level but that, inside those results, there were clearly concerns raised by the auditors. We wanted to calm the market down, and basically say, "Look, Better Capital is still supporting the business. It is not fixed yet but it is going to be fixed long term. Stick with us." Essentially, that is what we said.

**Q622 Mike Crockart:** This was designed to calm the marketplace.

**David Smith:** Yes.

**Q623 Mike Crockart:** At that point you were aware of the letter that Better Capital had written to City Link on 30 September. You have probably seen that we had a discussion with Jon Moulton about the meaning of the wording of the letter. The particular phrase is, “It is currently our firm intention to provide finance sufficient to enable the business to continue as a going concern for the next 12 months.” Jon Moulton’s view of that phrase, and certainly the auditor’s view of that phrase, is that it was pretty much worthless and they were very unlikely to get any further investment.

**David Smith:** I do not think you would get that from either of them. I did not see either of them saying that in the transcripts. What we did get—

**Q624 Mike Crockart:** They were pretty clear that there was coded wording in there. If you say it is currently your intention, in actual fact it is pretty much worthless.

**David Smith:** No. We did not see that as a board, I am afraid, and neither did the auditors, otherwise they could not have signed the accounts as a going concern.

**Q625 Chair:** Can I be clear? You did not see that as a board.

**David Smith:** No.

**Q626 Chair:** You did not perceive that. You actually saw the letter though.

**David Smith:** Of course. What I am trying to say is that we did not draw the conclusion that is being inferred here. Obviously we had the letter. The letter came from the top of Better Capital’s organisation, not from lower down in their organisation, which gave us—

**Q627 Mike Crockart:** Surely that gives it greater importance.

**David Smith:** It gave us a greater level of comfort. They do not normally give out letters at all, let alone from the top of the structure. We did not see the letter as an isolated piece of a jigsaw; we saw it as one element of a number of elements that enabled us as a board to—

**Q628 Mike Crockart:** You, as a board, took great comfort from that letter.

**David Smith:** We did take comfort, but we also understood that we had to go on a journey in October that would look at options.

**Q629 Mike Crockart:** Why do you think that the auditors took a very different view of that letter? In their audit opinion they say, “These conditions, along with other matters explained in Note 1 of the financial statement, indicate the existence of a material uncertainty which may cast significant doubt on the company’s ability to continue as a going concern.” They do not seem to have taken any comfort from that letter.

**David Smith:** They did take some comfort from it; otherwise they could not have signed the accounts.

**Q630 Mike Crockart:** I asked this question of the auditor. He seemed to think that because it said “material uncertainty” rather than “fundamental uncertainty”, that that

is perhaps the comfort they took, but “material uncertainty” sounds pretty worrying, does it not?

**David Smith:** It is not a clean set of accounts—of course it is not—but this is a company that had never traded profitably in their previous seven years. It had the support of its shareholder, and continued to have the support of its shareholder. It was being given encouragement to invest in October in handhelds, and it was given the opportunity to work on a future together. That was where we were.

**Q631 Mike Crockart:** But there seems to be a fundamental difference of opinion between what the City Link board took from what was going on and what everybody else seemed to. We have had evidence from Jon Moulton that the letter from Better Capital was quite clearly not meant to give comfort—that it was meant to raise significant concerns. The auditors understood that, and that is why they put in their audit opinion that there was a material uncertainty. Everybody seems to be agreeing that there were major problems, but you are in the press saying there is a bright future.

**David Smith:** There is a difference of emphasis only, I think. We all understood that the results of the business were not what we wanted them to be. We all understood that Better Capital and ourselves would need to go through a process of looking at options for the business going forward. In fact, we started that only on 9 October. We also understood that, in addition to the letter, Better had done a number of other things to give us comfort as a board; that we should be able to sign the accounts as a going concern, and that is what we did.

**Q632 Mike Crockart:** Signing it as a going concern is quite a low bar, is it not?

**David Smith:** Not if you are a director, it isn’t.

**Q633 Mike Crockart:** What changed between October, when you had a bright future, and December when you went into administration?

**David Smith:** What changed was that we had a shareholder that changed their view on supporting the business.

**Q634 Mike Crockart:** You are putting this at Better Capital’s door. In September, you were quite comfortable that they were going to invest the extra £25 million, but by December they had basically reneged on that.

**David Smith:** Yes.

**Mike Crockart:** I can’t wait to hear Jon Moulton’s view on what you have just said. He very much gave the opposite opinion.

**Q635 Chair:** You said that the quote in the interview was designed to calm the markets. Would I be accurate in saying that that was a euphemism for “designed to deceive the markets”?

**David Smith:** No.

**Q636 Chair:** Quite clearly you were in deep difficulties. You said in your very first answer to us that on 7 or 9 October you started a process of reviewing whether or not you could get somebody to take you over, or find another mechanism. That seems to me not to be a bright future. Can you clarify why it is that you seem to be saying two things at the one time?

**David Smith:** It was 9 October that started that process. In that process, we were content that we had a plan that would take us through to a solvent solution. We were content that we had the backing of Better Capital behind us to do that. We were also content that, if we chose a different route, we had options to sell the business, all of which were bright in terms of our judgment.

**Q637 Chair:** Had you said, “We think we can survive. We think we can get our way through this; we think that at the end of the day there is a survival plan that could work,” I could understand that. That would seem to me honest and straightforward. But to say it is bright seems to err on the side of optimism. What concerns me is not just that you were speaking to the trade press, which I suspect very few of our constituents will read, but you were also in a sense sending a message out to your employees and suppliers of contracts, vehicles and the like. You were saying to them, at the same time as you were exploring ways of allowing the business to survive, that the future was bright. It just seems to me that had the staff and your contractors known at the time the situation you were genuinely in, and that you were looking for alternatives, they would have taken some very different solutions. Does that not seem fair to you?

**David Smith:** I am not sure what solutions they would have taken. We were sitting there with—

**Q638 Chair:** They might very well have said, “Zoom, I’m away.”

**David Smith:** But we were sitting there with an investor saying, “Continue to invest and continue to push forward with your plans. Get ready for peak; get ready for 2015.” That was the backdrop.

**Q639 Chair:** I understand that. You were in a position where you were taking comfort from the fact that with Better Capital you virtually had a blank cheque, and you thought at that stage that they were going to provide for you, even though everything else was in difficulties, things were not going as well as you expected and you were having to look at plans; but because you had, as it were, the equivalent of a sugar daddy the future was bright, as long as the sugar daddy remained there. That is not quite how you put it though, is it?

**David Smith:** Don’t forget that we had also presented those plans to them in June and again in August with a clear view that said we needed £20 million to £25 million of further investment.

**Q640 Chair:** But you knew that really, didn’t you?

**David Smith:** We did know, and they knew that. We presented it to them.

**Q641 Chair:** You thought they were still going to provide the money.

**David Smith:** Yes.

**Q642 Chair:** I want to come back again to the question of the letter, what the terms of the letter mean to normal people and what the terms of the letter seem to have meant to the person who wrote it. I got the very clear impression, having listened to Mr Moulton, that he was telling us that basically this letter was worthless five minutes after he wrote it. It was true at the time it was written, but its value did not last for any length of time at all; yet you seem to be absolutely clear that this was a strong and binding commitment from which auditors should take great comfort. They knew that the business was in difficulties but because the sugar daddy, as it were, was still standing behind you, you were going to be okay. Do you understand why we have a difficulty in working out how these two things can both be compatible simultaneously?

**David Smith:** Yes, I do. I think that we took comfort, not great comfort, from the letter. We took comfort from the fact that we had presented to them in August and asked for a further £25 million, and they had asked us to continue to progress that plan. We took comfort from the 9 October meetings, as they came along. Later in the piece, Better Capital continued to write of their continued support as late as 3 December, when we received a similar comfort letter from them, having presented to them on 28 November. We continued to believe that Better were going to support us, not just on 30 September as a snapshot date, not just on 9 October and not even just on 3 December when we got the last of the letters from Better to tell us that they were continuing to support the business.

**Q643 Chair:** To be fair, I do not think we have heard before that there was another letter of comfort on 3 December. Heads are shaking. Could you arrange for us to get a copy of that?

**David Smith:** Of course I can. I can give you a headline of it now, if that would help.

**Q644 Chair:** Yes, that would be helpful.

**David Smith:** It is of course couched in the same language as previous letters. The letter says, "This letter is one of current intention." It was written to us after we had presented the update of the plan that we were pursuing, which was on 28 November. The directors asked for feedback on that plan and what we needed to do next in order to secure funding. That letter acknowledged that we were asking for funding, quantified an amount of money, and laid out to us that there were a number of moving parts still to be concluded in the overall plan before they could get to their own opinion. They requested a detailed operating plan, which we indeed built for them.

They requested that we find third party asset-based lending, which we did. They outlined the need for Rentokil and its role as a secured creditor to give us some leeway in terms of their position. They asked that we pursue the landlords, as I have told you we were doing, and they identified that there should be no significant worsening in trading and the trading conditions of the business, which there were not. We had all those elements and were working on the basis that, if that was what was required to get the funding, we were clearly in a position where we could demonstrate that we were doing all those things. They finished the letter by saying, "We are impressed with the progress made to date and will continue to work with management in seeking to deliver a solvent outcome." That is 3 December.



**Q645 Chair:** Clarify for me where the commitment is in that.

**David Smith:** The commitment is in the second paragraph. They are talking about the acknowledgement that we are asking for funds to be invested in the turnaround plan. They are saying, “Yes, you should pursue that plan.” It is the same greyness, if you like, as previous letters, but it is a continuation of that story.

**Chair:** I have just been given a note saying that a vote is imminent. We will continue until the vote comes, and then we will have to break.

**Q646 Mr Bailey:** What would have been required to keep City Link going as a viable concern?

**David Smith:** In its whole shape as it was at 24 December?

**Mr Bailey:** Yes.

**David Smith:** An investment of probably £25 million to complete the investments in IT and structuring changes that were necessary, as well as a further investment of £20 million plus to buy out Better Capital’s interest in the business: £40 million to £50 million-worth of investment and then for those turnaround elements actually to be delivered; IT changes, landlord agreements and so on.

**Q647 Mr Bailey:** Better Capital obviously decided that whilst it had hitherto been prepared to provide the £25 million, subject to all your plans demonstrating that they were actually being achieved, it balked at the extra needed to keep it viable in the long term. Would that be a fair summary?

**David Smith:** Yes. The request to Better was for about £20 million, and we were looking to asset-based loan providers to provide the balance.

*Sitting suspended for a Division in the House.*

*On resuming—*

**Q648 Mr Bailey:** On 22 December, Better Capital provided a further £2 million of funding. When Jon Moulton was questioned about that, he acknowledged that they had provided it but he was not clear how it was used. He seemed to think that you were the person who disbursed it. Could you tell me what it was for and where it went?

**David Smith:** I am glad to have the opportunity because I would have raised this, had you not. Better Capital did not actually put any further funds into the business in that time period. The mechanism for us was that they put in the facility in April 2013 when they bought the business, and then we drew down from that facility centrally into the trading company as required. The last physical drawdown was in fact in September, not in December at all, as Jon suggested to you.

I think what Jon was trying to convey, however, is that from the 22nd to the 24th the business and the directors were very minded that if we continued to trade in that time period

we needed to be satisfied that we were not making the creditors' position worse. We did a set of calculations which, at the time, calculated out at about £2.5 million to be paid to those creditors who were trading with us through that period. Of course, in making that payment, we inevitably, in the end, would make the position worse for Better Capital as a secured creditor, because we were paying unsecured creditors. I think that might have been lost in translation, but we certainly did not receive an injection of cash specifically from Better Capital at any time in December.

**Q649 Mr Bailey:** That is interesting, because certainly the impression that I think was conveyed to this Committee, and was certainly perceived by the Committee, is that an extra £2 million had actually been provided.

**David Smith:** No.

**Q650 Mr Bailey:** Obviously you are not answerable for Jon Moulton's responses—

**David Smith:** Indeed not.

**Mr Bailey:** But there appears to be a very contradictory interpretation about this particular payment. I need to get it clear in my own mind. That money was not extra money; it was just payments to contractors that would have made the position of Better Capital worse in the event of a winding-up and dispersion of assets afterwards. Is that correct?

**David Smith:** Yes, that is correct.

**Mr Bailey:** That is a reasonable interpretation of what you are saying. It certainly seems to contradict what we heard previously. Obviously it begs questions which we may want to ask Mr Moulton in the light of the evidence that we have heard today.

**Q651 Mr Reid:** In Mr Moulton's oral evidence he said, in reply to Question 339 from the Chair, "That was why I mentioned earlier that we had put in £2 million between the 22nd and Christmas eve." Are you saying that that is not correct?

**David Smith:** Yes. I saw that quote as well and checked with the accountants, having seen that quote. No physical funds were put into the business from Better Capital in that time period at all. But, as I said, as we were making payments out to unsecured creditors in that time period, you might infer from Jon's position that in fact we were making his position in the event of an administration worse by that amount of money, which would have been about £2 million.

**Q652 Mr Reid:** Was it a case of Mr Moulton giving you permission to spend that money?

**David Smith:** In that time period we sat down with the administrators in waiting, Ernst & Young, and with Better Capital. We laid down what we were proposing to do around payments. They were comfortable that that was what we were going to do; yes.

**Q653 Mr Reid:** Mr Moulton was comfortable.

**David Smith:** Mr Moulton was not specifically on the call, but Better Capital as the shareholder was on the call.

**Q654 Mr Bailey:** In the light of what Mr Moulton said at this Committee a couple of weeks ago—you obviously heard it—did you have any conversations with him about it?

**David Smith:** No. My conversations were only with the accountants and the finance director, my own team, to check what actually happened.

**Q655 Chair:** I am confused. You were stressing there that there was no physical additional money—£2.5 million. I am not quite sure whether or not that means this is some sort of metaphysical money, because we got the very clear impression that something was transferred, that there was additional money. The impression I quite clearly had was that Mr Moulton wanted to avoid suppliers—we will come to the detail of this later on—who were providing services between the 22nd and later on being out of pocket, and therefore this money was supplied. I genuinely do not quite grasp this concept of how it was simply drawn down in some way as distinct from supplied, if there was not a concrete decision, which was passed on to you, that, yes, this could be done for that purpose. You have read the evidence and you will be in no doubt about the impression that was created in our minds. I simply cannot square what you are telling us now with what we were told before. I am seeking a little more illumination.

**David Smith:** No new physical cash was put into the business. Absolute fact. None whatsoever. I have checked that with my finance director and accountants. In terms of the money that was in the business, had we closed on the 22nd, you will have heard from the administrators how that potentially would get divvied up. By paying down unsecured creditors, or people who were helping us trade through to the 24th, to the tune of £2.5 million we were, in effect, taking that money away from Better Capital, because we were going to give it to them. If you looked at it through that lens, you could see from Jon's perspective why he would say that I specifically wanted that £2.5 million to be spent. That would be my interpretation of what he said.

**Q656 Pamela Nash:** I was just looking at the evidence that Alan referred to. Mr Moulton said that he would send us further detail of that payment. I have just clarified with the Clerk that that information has not yet arrived. Are you aware of any possibility that that money could have gone straight to the administrator rather than through City Link?

**David Smith:** No.

**Q657 Pamela Nash:** You are not aware of any possibility.

**David Smith:** No.

**Q658 Pamela Nash:** Our understanding is that a good reason to put that money in was to avoid the accusation of trading whilst insolvent for those couple of days. As far as you are aware, that money could not have gone straight to the administrator.

**David Smith:** No, it did not.

**Q659 Chair:** There is one aspect of this that still puzzles me. It has been suggested that this £2 million or £2.5 million—I cannot remember the exact figure—was used to reimburse the creditors who were running up bills by buzzing about in their vans and so on. By the 22nd, surely the administrator was in charge of that. On what basis did he allow these payments to be made to people who were unsecured creditors when, as I understand it, the legal position would be that any money there was designed for secured creditors?

**David Smith:** The technical piece is that the administrators were not actually appointed until 7 o'clock on Christmas eve. From the 22nd to the 24th, the directors had responsibility to continue to trade the business or to stop trading immediately on the 22nd.

**Q660 Chair:** Even though it was decided to put the business into administration—  
**David Smith:** Yes, because the process took from the 22nd to the 24th to go through. Of course we did not make any decisions in isolation. All those conversations on the 22nd, 23rd and 24th were tripartite between the administrators, the directors and Better Capital—for that matter we had our own advisers as well—to make sure that in trading through those days we were not wrongfully trading and we were not making the creditors' position in the round worse. Because Better inevitably was being made worse by what we were doing, we had Better's permission to make their position worse. That is why I think Jon is saying to you that he saw the £2.5 million that he injected as his. He did not physically do that, but the practical reality of it is that he was worse off by £2.5 million or thereabouts because we traded through those two days.

**Q661 Chair:** I understand that. Effectively, the unsecured creditors were better off and the secured creditors were worse off as a result of the transactions that were taking place. The wording of this is a bit like that letter, which turns out not to have meant what a normal understanding of reading the English would be. A normal understanding of reading the words that Mr Moulton gave us would lead us to a completely different conclusion from the one that you have now explained. Do you accept that? Unfortunately, *Hansard* does not record the nodding of heads, so it would be helpful if you could confirm that.

**David Smith:** I am now the third one out of three who has nodded instead of saying yes. I understand your point and I concur with it, yes.

**Q662 Katy Clark:** I draw attention to my entry in the Register of Members' Interests, which I have referred to before. There are reports that when Better Capital bought City Link your salary was increased from £368,000 a year to £646,000 a year. Is that true?

**David Smith:** No, it is not true. What actually happened was that my basic salary did not change at all. My contract of employment did not change at all, nor did I receive any increases at all across the time period before or after, from the first day I joined the business. In that specific year, however, I earned an annual bonus, paid under Rentokil's watch, and that is the difference between the salaries in the different years.

**Q663 Katy Clark:** What about your pension? Were there any changes to your pension?

**David Smith:** Like everybody else in the organisation, we moved from the Rentokil pension to the people's pension. The company contribution declined post Rentokil from before Rentokil.

**Q664 Katy Clark:** When were the contractual arrangements that led to your bonus entered into?

**David Smith:** All of my contracts were based on the contract that I signed around June 2011. I obviously could not join the business straight away because I had previously been at Royal Mail, which was a competitor, so I spent six months doing not much. That contract was consistent throughout the time period, and did not change.

**Q665 Chair:** Can you see how it looks externally? Here is a business that is in great difficulty and the money that you get goes up shortly before the business goes down.

**David Smith:** It was a year and a half before, and they were the contractual terms under which I was employed. I can understand that people might not see that that was value for money in their eyes.

**Q666 Pamela Nash:** I want to explore those contractual arrangements a little bit further. This additional money was earned in the form of a bonus.

**David Smith:** Yes.

**Q667 Pamela Nash:** What was that bonus given for?

**David Smith:** It was a bonus given for the successful sale of the business from Rentokil to Better Capital.

**Q668 Pamela Nash:** It was specifically around that sale, I take it, and not on the performance of City Link.

**David Smith:** Correct. In fact, most of that money was then invested in shares in City Link.

**Q669 Pamela Nash:** I want to move on to what for me is the main issue raised by my constituents who have lost their jobs and livelihoods through City Link—the situation around self-employment, or bogus self-employment, at City Link depots. During the time that you were chief executive, how many City Link employees were made redundant and subsequently re-employed, or given work, as a self-employed contractor?

**David Smith:** Unfortunately I do not have those figures in detail to hand. I can tell you that in the last year—because we reviewed this in the board in September, looking at the 12 months previously—approximately 550 employees left the front line of the business. About 150 of those were made redundant, to give you a scale, and only 27 of those then went from being redundant to becoming self-employed SD partners.

**Q670 Pamela Nash:** Could you repeat the time period?

**David Smith:** This is the 12 months up to September 2014, which was the last time we looked at it as a board.

**Q671 Pamela Nash:** To be fair, this issue is over a longer period of time leading up to the end of City Link. Is there information held by you or City Link as a whole that would show that pattern?

**David Smith:** The company records would probably have that detail; I do not. What I would say is that over the three years the business increased the number of self-employed subcontract partners and service delivery partners, which were the two variations of the contract. When I joined it was probably about—

**Q672 Pamela Nash:** Could you explain the difference between the two?

**David Smith:** When I first joined in '11 there was a contract in place that the self-employed drivers were working under. We relaunched that in '12, I think, and called it subcontract partners. Then we revisited it again in '13 to make sure we were staying in line with employment and tax legislation, and changed it to service delivery partners. It was essentially the same type of job but with a different contract each year. This is from memory now so it may not be 100% accurate; we went from approximately 55% self-employed when I joined, to about 78% at the time of the last set of records we've got—November last year.

**Q673 Pamela Nash:** Why was that the case? Was it a conscious policy decision to move towards that?

**David Smith:** Yes, it was.

**Q674 Pamela Nash:** Who made that decision?

**David Smith:** The board made the decision. Let me explain why. If you look at the industry—this is pretty much across every one of the carriers—the volumes that we carry across the year are not steady. They go up and down for days, weeks and months. The difference between the low point of the year in August and the high point of the year is probably 100%. You cannot carry a fixed-cost permanent employee base that covers all those eventualities. The model that was developed way back in the early 2000s—when I was in Parcelforce in 2003 we had this in place—was to have self-employed drivers paid by delivery item, by delivery route or by delivery day. There are variations around that. They pick up the difference between your low point, essentially, and the rest of your volatility. They are paid differently. They are specifically at arm's length from the business from a tax and employment position, but in return for that they are likely to earn higher rewards for the volatility, and the fact that they are taking on additional risks around ownership of uniforms, vans and all those things.

**Q675 Pamela Nash:** I understand that obviously there is volatility in the level of business a parcel firm would have, and I can see that being filled by agency work or a method of self-employment, but my understanding is that these employees, mostly men, who were employed there were required to wear City Link uniforms. They had to have



their self-funded transport in City Link colours. I am led to believe that that cost the individual around £3,000 to do. They were not allowed to work for other rival firms during that period. That would prevent them from doing a level of work at other times of the year. Why was that the case?

**David Smith:** It was not the case. The contract was very specifically set up to enable them to work for other people. They could not carry other people's goods at the same time as carrying our goods; that was true. We had Queen's Counsel advice to make sure that we were clear in terms of enabling them to work for other people. We did insist that they were uniformed, and that they used our handheld devices because we needed the data; and we wanted uniforms because we wanted our customers to know and trust that it was us who were doing the deliveries.

**Q676 Pamela Nash:** Did you provide the uniforms or did they have to pay for them themselves?

**David Smith:** They had to pay for the uniforms as part of the contract. We went through various iterations on the van. At certain times we asked them to run with a van that was liveried and in our colours. Later we said they could use a white van and what we called livery lite; there were a number of variations around that over the three-year period. Fundamentally, we recognised that there were different types of individual: the person who wanted to be an employee, who wanted the benefits of employment rights around holiday, pension, sickness and those things, and a self-employed person who was an individual entrepreneur running their own business, and prepared to work in a different way to earn more reward but with more risk.

**Q677 Pamela Nash:** I have to say, Mr Smith, that, whilst this may be anecdotal, that is not the impression I have had from any of the staff I have met who worked at my plant and who worked at the plant in Glasgow. All of them told us that they felt forced into a self-employed situation. They did not do it for the rewards. Indeed, they did not get financial rewards. They were put at great personal financial risk to take on this work, and ultimately paid the price that we saw over Christmas.

**David Smith:** I can tell you that in the year to the end of September only 27 people went from being employed to being subcontract partners across the whole country. We were not in the position where we were asking people to do this. We were really struggling with agency drivers—very short-term man and van—where quality and cost was poor. We were trying to recruit both permanent employees and subcontract partners right throughout 2014.

**Q678 Pamela Nash:** Could I ask you to provide the information you referred to earlier about how many people were made redundant and then employed again, but over a longer period of time, perhaps from the merger, and not just the year before? Certainly in relation to the men we met it had not happened in the last year.

**David Smith:** I will ask the administrator to pull that data together for you. I do not personally have access to those records, but I will ask for that.

**Q679 Pamela Nash:** We have heard from you and from Mr Moulton about the benefits of the high rewards to people who had become self-employed. Was there any movement within City Link of people asking to move from being a full-time employee to being self-employed?

**David Smith:** Not hugely. As I say, only 27 people across the year who were made redundant moved across. Not many others beyond that wanted to make that move. We only had about 400 employed drivers in November last year, and about 1,300 or so subcontract partners. That gives you the scale, but we did not have a lot of movement in either direction, because they are fundamentally different types of people who want to work in different ways. I reiterate again that it is a very common thing in the industry. This is not City Link specific. The contracts that we had are very similar to the contracts that you would find in Parcelforce, DPD, Yodel, UK Mail and the whole sector.

**Q680 Chair:** I want to come back to some of these points. Why did you move from so many full-time employed staff more to the core and periphery? I understand the point about fluctuations, but would I also be correct in assuming that it was much cheaper for you to do it that way? Even if people were doing exactly the same things, it was cheaper to have them off the books as bogus self-employed, or self-employed, rather than directly employed.

**David Smith:** It is not a black and white answer. What we did—most of our competitors would do this—was to look at it route by route. When you are looking at a route you are looking at how many drops it is possible to do in a day and what the rate of pay is in that part of the marketplace. You are then comparing the cost of an owner/driver, with his van and all of those costs, with the employee model. Given our type of traffic profile, which was bigger, heavier and larger than a postal van because that was the type of business we were carrying, we got to a certain mix position of 75% or thereabouts that should be self-employed in that space. That was the optimum financial answer, but it also worked well from a quality perspective. Generally speaking, we saw higher levels of completion of delivery from the subcontract partners than we did from the employed people. Essentially, they are only paid if they complete the delivery. There was a cost and quality element to it.

**Q681 Chair:** What does a higher level of completion mean? Does that mean that directly employed drivers don't deliver things? What do they do? Throw them away? Do they sell them? Do they come back to do them the next day? I do not quite understand this concept.

**David Smith:** Essentially, what happens is that the employed driver in our world would have completed about 70 deliveries a day and might have done another 10 collections a day on top of that. A self-employed driver would probably be doing 85 or 90 deliveries a day. Why? Two reasons. One is that the route enables them to drive less distance between each place they are going to.

**Q682 Chair:** The route makes the difference, not their employment status.

**David Smith:** Partially. Correct.

**Q683 Chair:** If we leave that aside, the question of the route does not make a difference between having somebody directly employed or self-employed—the variation. Explain to me the other factor that makes the difference.

**David Smith:** The other factor is the way they are paid. Effectively, the employed driver is paid for a day; if he does one delivery or 100 deliveries, he is paid for the day. If you are a self-employed person, you are paid by delivery. If you do one delivery, you are only paid for one delivery. If you do 100 deliveries, you are paid for 100. If you do 110, you are paid for 110. The incentivisation model to enable them to earn more money essentially means that that is what they do.

**Q684 Chair:** If I have a route and there are three parcels, I cannot deliver 100 even if I am really desperate to work all day. I've only got three parcels because you've only given me three parcels, so I do not quite understand this point about incentivisation.

**David Smith:** On those particular routes, which are typically rural routes, they would more or less all be employed drivers for that very reason.

**Q685 Chair:** In urban areas, is there a big pile of parcels and I would drive in and decide how many to do? If I was employed, I would work from x hour to y hour but if I was self-employed I would just work on, to get more money, for as long as it took.

**David Smith:** No. The routes are set up with a broad productivity view of what is sensible to do in a day. Obviously we are not going to ask people to work beyond a normal working time and we are not going to ask them to do unhealthy things in terms of carrying heavy or too many parcels and that type of stuff. Each route was structured and contracted as a route. The route is typically 80 to 100 deliveries in a day. That is what they did.

**Q686 Chair:** If people were doing 80 to 100 deliveries in a day, what difference does it make between being employed and self-employed? Do the self-employed drive faster? I do not quite understand this concept of the difference that it makes.

**David Smith:** The differences are that the employment model adds costs to the business that we do not incur.

**Q687 Chair:** If all other things are equal, employing somebody costs more.

**David Smith:** It would do. If their productivity was the same and everything else was the same, we would probably have higher costs from an employee than we would from a self-employed person.

**Q688 Chair:** It has taken us really quite a long time to get where I think we were always going to get to. I have some other questions, but it would help if you had told us the accurate answer at the beginning rather than forcing me to go through this long rigmarole. We have got to the position now where you are telling us that, all other things being equal, it is cheaper to employ somebody on a self-employed basis than on an employed basis. Can you clarify why that is?

**David Smith:** Fundamentally, the productivity levels are generally greater from those people.

**Q689 Chair:** But I thought we had said that all other things were equal. Does the self-employed driver drive faster?

**David Smith:** No. He probably stays out an extra half hour or goes out half an hour earlier in the morning. It is that kind of thing.

**Q690 Chair:** That is not productivity then. I would take productivity to be a question of work done divided by time. What you are saying is that they work longer. You can surely get people who are directly employed and tell them, “Here are your set hours, but if there are additional parcels we will ask you to stay on another half hour.”

**David Smith:** Yes, but you would pay overtime for that.

**Q691 Chair:** So it is an overtime avoidance mechanism.

**David Smith:** It is overtime, the national insurance structure, a whole set of elements.

**Q692 Chair:** The national insurance structure presumably does not flow from productivity, does it? It is a question of the status of their employment. We are getting closer to the reality now. What issues would drive you towards having people on self-employment rather than direct employment, other than national insurance?

**David Smith:** There is a set. It is whether you can actually get anybody to do the job. We had vacancies for PAYE drivers for the entire period of last year and could not fill the roles. In other words, there was a shortage of people who wanted to come to work for us.

**Q693 Chair:** How much an hour were you paying?

**David Smith:** I cannot tell you off the top of my head.

**Q694 Chair:** Give me an approximation.

**David Smith:** We were about 90 pence to £1 above the minimum wage per hour—that sort of level.

**Q695 Chair:** Have you ever considered getting more drivers by raising the wage? That is normally how capitalism works.

**David Smith:** Yes, but there is a market price that the market will bear in terms of the charge-out that you can apply for the parcels on the other side. We were already loss-making, so increasing the wages was not going to help.

**Q696 Chair:** Absolutely. Presumably you effectively had self-employed people who were working for below that 90 pence above the minimum wage. Having people on a self-employed status was a way of driving down the effective wage rate. Is that a fair assessment?

**David Smith:** It did improve our cost base, yes.

**Q697 Chair:** I think, “Yes, it did improve our cost base,” is a better way of putting it, isn’t it? We have got to the position where we are clear that the reason why you had people on this self-employment was in order to drive down costs. I want to clarify a couple of points that you responded to Pamela on. You mentioned, I think, that 500 left, 150 got redundancy and 27 then went on to be self-employed. That does not tie in with my assessment across the whole business. Presumably that is over a relatively short time window, is it?

**David Smith:** It is over the 12 months until that September.

**Q698 Chair:** My impression was that over the longer period the numbers were much more substantial, in particular for people who left the business but then felt obliged, as they told us, to move into self-employment. In terms of people who left the business to become self-employed, were they made redundant as such? How were they terminated? The point we were seeking to clarify was whether or not, if somebody had been retained in employment and then at the end when the business went down they were still in employment, they would have got redundancy payments; whereas, if they had been employed by the business, left, become self-employed and the business went down, they would not actually get anything. I want to clarify this transition between employed and self-employed.

**David Smith:** If we look at people who were made redundant, left the business and then became self-employed, they would have been made redundant and would have received their full redundancy entitlement, whatever that was for them individually. Then separately, as a completely separate transaction, they would have come back to the business and taken on a contract. In other words, they got paid their full redundancy.

**Q699 Chair:** Fine. That clarifies that. Are there any people who would not be in that position, however, who would have been removed from the business and then come back as self-employed who would not have had the redundancy payment?

**David Smith:** I do not know of any who would be in that position.

**Q700 Chair:** I understand that with a business like this, which is not paying much above the minimum wage, you are going to get a degree of churn all the time.

**David Smith:** That is why I said that of the 500 that left in that period last year most of them just left.

**Q701 Chair:** I understand that, but you can understand the point that we want to clarify as well.

**David Smith:** Yes, I do.

**Q702 Chair:** One of the issues that has been raised with us, and about which we might want to make a recommendation, is whether, if somebody is forced to change their status and the business then goes down, they end up losing out. They clearly do not if they were made formally redundant and they got their redundancy payment, but if anything else happened they end up worse off.

**David Smith:** I would also strongly refute that they were forced to become self-employed with us.

**Chair:** Oh.

**David Smith:** I would. It was two separate things. One is that you are made redundant. Secondly, there are vacancies for the self-employed. “Do you want to work with us or do you want to work self-employed with somebody else?” The whole industry is short of individuals in this sector.

**Q703 Chair:** Do you want to work self-employed with us or do you want to be long-term unemployed? In many of the areas that we represent there are not a host of other jobs to go into. People were effectively told, “We are making you redundant, or we’re sacking you or terminating your employment”—however you want to phrase it—“as an employed person. However, here is a vacancy.” That was the nature of the transaction. The people that we spoke to felt bludgeoned into accepting what was on offer as an alternative to being unemployed.

**David Smith:** I do not have that evidence from my team.

**Q704 Chair:** You don’t, but we do. I want to clarify the question that Pamela raised about people who were asked to buy the uniform, provide their own transport and have the transport painted in your livery by a contractor that you specified, at a cost which was much more than they could have got it done for in the free market. They were not allowed to work for anybody else with that van. To all intents and purposes, they are direct employees, are they not?

**David Smith:** No, because that is not the case. The contract very clearly enabled them to work for other people.

**Q705 Chair:** But not with your van.

**David Smith:** They could work for other people.

**Q706 Chair:** But not with your van.

**David Smith:** They could work for other people.

**Q707 Chair:** Could they work for other people with your van?

**David Smith:** I do not know in the individual circumstances you are talking about. I would have to go and check.

**Q708 Chair:** If somebody gets a white van and they get it painted in your livery at your instructions, do you think it is reasonable to anticipate that they are likely to use that van to work for a competitor? If you were hiring somebody as a contractor, would you like them to come up with a TNT-painted van and say, “I’m your man from TNT but I’m actually working with City Link today”? Of course you would not. The stipulation to these



people was quite explicit. They could not use City livery vans to work for anybody else. It just makes sense.

**David Smith:** No, I do not think that is what the contract says.

**Q709 Chair:** You don't think so.

**David Smith:** No.

**Q710 Chair:** Fine; we will go back and check that. We would have expected you to know. If you are saying that, as far as you are aware, that did not specify the case, somebody is misleading us.

**David Smith:** It is certainly very clear in the contract that they could work for other people and that they could use the vans in other forms of work. It was also clear, by the way, that we had a number of people working for us who had other people's liveried vans, because there is a shortage of subcontractors in the market.

**Q711 Chair:** I have to say that what you are telling us is a bit like a question of "He said, she said." What you are telling us does not gel with what we have been told by some of the staff, or former staff, that we met. We will obviously have to go back and clarify this, and if necessary we will have you and them back to see us on oath.

**David Smith:** Would it be helpful for us to provide you with a copy of the contract? Have you got a copy of the contract?

**Chair:** We went on the words that staff were telling us about what they had been instructed to do by their managers, and the conditions under which they were employed. We did not think we needed to go to that length, but clearly we do now.

**Q712 Pamela Nash:** Mr Smith, it would be helpful to have a copy of the contract, but do you accept that even if that wording is in the contract—I take you at your word that it is—despite that, you still created a situation at City Link that made it impossible for those self-employed people to work for another company, for the reasons that the Chair laid out? If their van has City Link colours, they are not going to get work at another company.

**David Smith:** I think it would be difficult, yes. I also think that we went out of our way to ensure that when we set the contracts up they were economically sensible, and that they could earn a liveable wage to use the van and pay for it and all of the things that you are concerned about. We checked and monitored that on a number of occasions to make sure that it was what was happening. Where that was not the case, we were in fact going through a process of recommissioning and recalculating those rates to renegotiate again with the drivers, which we did on a regular basis. It was certainly not our intention to have a whole host of drivers who were disenfranchised from the business, who did not want to perform and did not want to provide the service to customers. That would be completely counterproductive.

**Pamela Nash:** And it proved that it was.

**Q713 Ann McKechin:** I want to come back to the memo that you sent on 21 November, which Mr Bain referred to earlier in the evidence this afternoon. You will be aware, Mr Smith, that at the time, with the difficulties the company was experiencing, such a statement would have to be very carefully drafted so that you did not provide any misleading information to your suppliers. Why is it the case, as you have explained this afternoon, that, instead of you taking direct control and sending the message yourself directly to the suppliers, you disseminated it first of all to your managers and, in the words of Mr Kelly, the lead administrator, when we took evidence from him last week, it was “for dissemination to suppliers or other employees within their team as they thought reasonable and right”? How did you maintain consistency and the ability that you were not providing any inaccurate information?

**David Smith:** The information was, as I said before, sent to my first line reports—my directors, if you like. The information that they were given was, in our judgment, clearly correct: we were trading and had a reasonable prospect of a solvent solution. We were taking legal action against those outside the business that were seeking to defame the company, and we were making investments in handhelds, and so on. In terms of the facts that were in the letter, we were comfortable. The e-mail that accompanied the suggested form from me to the directors was very clearly saying, “If you need to use this, then this is the guidance to use.” Also, within that letter, it suggested that any supplier that was concerned should contact me directly. My contact details were on that letter, and so were my finance director’s. To the extent that we had any supplier interaction, we talked to those suppliers.

In terms of employees, we had a set of mechanisms, which we used consistently in the entire time that I was in the business, to talk to employees. I had a blog that I used regularly. We had a City Link newspaper for all staff, in which I had a column every month. My senior management team met me every couple of weeks, during which we discussed the position of the business. The front-line managers had a monthly teleconference with me around the performance of the business. In terms of understanding where the business was and what position it was in, this is not an isolated piece of paper; it is part of a much wider communication structure.

**Q714 Ann McKechin:** Mr Kelly agreed that statements made in this memo were relatively categoric, and that is part of his current investigation. In the first line you state that you are aware of “unfounded rumours” and then in the second sentence you state, “These rumours are untrue.” But clearly on 21 November you were having discussions about a range of options. One of those options was administration of the company.

**David Smith:** The unfounded rumours we were talking about were specifically that the business was going to go into administration at the start of December or during December.

**Q715 Ann McKechin:** I think you said on 24 December. That turned out to be uncannily accurate.

**David Smith:** Indeed.

**Q716 Ann McKechin:** That is a wonderful coincidence. How do you think they managed to get that date? Did they just pluck it out of thin air, Mr Smith?

**David Smith:** No. If you look from the outside, you would know that our industry's peak trading time is up until Christmas.

**Q717 Ann McKechin:** If you are a company in difficulty, the most likely date would literally be the day just before Christmas day. Was that a reasonable assumption to make?

**Chair:** Unfortunately, *Hansard* does not record the waving of the thumbs and the grimace. It would be helpful if you just said something.

**David Smith:** I think the 24th is an intelligent guess as to a date when a company like ours might go into administration.

**Q718 Ann McKechin:** Would it be fair to say that people were making some intelligent guesses about what could happen to your company?

**David Smith:** What was happening in the marketplace, I believe, was that the accounts that had gone out had caused a degree of noise. We discussed that earlier. There were the conversations that we had had with 17 potential trading partners. Some of those potential trading partners had been fairly disingenuous in terms of putting noise into the market, two of whom we took action against, and the administrators are aware of the individual companies. Through the early part of December we were also having conversations with 50-odd landlords. Again, those landlords were not necessarily as quiet, given the NDAs they had signed, as we hoped they would be. Inevitably, there was some noise in the marketplace.

**Q719 Ann McKechin:** But it certainly was not untrue on 21 November that you were actively considering that one of the options you might have to follow would be liquidation.

**David Smith:** No. We had a set of options that we calculated, and we believed—

**Q720 Ann McKechin:** And one of those would be administration.

**David Smith:** Yes. We believed that a solvent solution was still reasonable.

**Q721 Ann McKechin:** That is all I need to know. One of the options was administration, and that is correct. Would you confirm that that is correct for the record?

**David Smith:** Yes, it was correct.

**Q722 Ann McKechin:** Thank you very much. Do you think it is right that your employees and your subcontractors were encouraged to take on more work, and in the case of the subcontractors more staff and vehicles, when there was such a serious risk to the company and when, given their unsecured creditor rate, the personal impact on them would be very high indeed? Did you take that into account at all when you were considering your options at that time?

**David Smith:** We had a number of conversations with Better Capital about the trading cycle, and also with our advisers. We were very clear that in going into the peak period all

our customers and all our suppliers would increase their volumes. We did a number of calculations to demonstrate that in fact, and Better were very clearly aware of that. We asked for and got some comfort that they would continue to support us. On that basis, we continued to trade as normal.

**Q723 Ann McKechin:** The livelihoods of the small contractors were not your top priority at that time.

**David Smith:** Our top priority at that time was finding a solvent solution to continue to trade the business in the long term.

**Q724 Mr Reid:** At any point in this process did you take a decision to stop paying contractors for work that they had already done?

**David Smith:** No, we did not. The subcontractor payment model is typically, but not entirely, two weeks. We paid that right through. There was some confusion in one of the earlier sessions about the last payments. The last payments were signed off on the 17th for payment on the 19th as normal. Once it became clear to us on the 22nd that we were going into an administration process, we again did a calculation for those days from the 22nd to the 24th, but at no point were we sitting there saying, “We should not be paying subcontractors.”

**Q725 Mr Reid:** When the Committee met contractors in Glasgow, one of the contractors said that he was due to be paid on the 19th and had not been paid. Could you perhaps speculate why he may have thought that?

**David Smith:** I cannot speak to an individual case like that.

**Q726 Pamela Nash:** Just to be clear, it was more than one.

**David Smith:** I know that we made the payments that we were due to make. They were signed off on the 17th and paid on the 19th. I know that we then made a subsequent payment between the 22nd and the 24th to the subcontractors. Individual contractors at any point in time would send invoices to us. They may have missed the timing of a normal invoice run. There may have been a dispute between the manager and the staff as to what had actually been delivered. We may have misprocessed it. There is a whole host of reasons why it may have happened.

**Q727 Mr Reid:** Can you clarify what misprocessed means?

**David Smith:** What that means is that we did not pick it up and put it through our ledgers in time.

**Q728 Mr Reid:** Can you explain how the system works and how you pay your contractors?

**David Smith:** Broadly speaking, the contractor will carry out a week’s work. They would get that signed off by the local manager. They would then send in an invoice to the accounts payable function, who would put it on to the system for payment. The manager’s

approval would come through separately from that. When the two match together, the accounts payable team would then release that into the payment cycle. That payment would then get paid two weeks later.

**Q729 Mr Reid:** How long a gap is there between the contractor doing the work and actually getting paid?

**David Smith:** Two weeks or two and a half weeks, something of that order.

**Q730 Mr Reid:** Does that mean that the contractors will not be paid for all work that was done in the two weeks running up to 22 December?

**David Smith:** Broadly speaking, I think they would go into the unsecured creditors' pot.

**Q731 Mr Reid:** But they won't get paid.

**David Smith:** I do not know whether they will get paid. The administrator has yet to calculate fully what that will be. I do not think they will get all of their money back for those two weeks.

**Q732 Mr Reid:** I would not have thought they would get any of their money back.

**David Smith:** I do not know.

**Q733 Mr Reid:** Any contractor that did any work after approximately 8 December will become an unsecured creditor. Is that correct?

**David Smith:** Yes.

**Q734 Mr Reid:** But you are also confirming that unless an error was made they would have been paid for all work done before 8 December.

**David Smith:** To the best of my knowledge, yes.

**Q735 Mr Reid:** If an error was made and a contractor was not paid, what is their situation? Do they become a priority creditor or are they an unsecured creditor?

**David Smith:** I don't believe their position changes. I think they would still be an unsecured creditor.

**Q736 Mr Reid:** Even if it was your mistake.

**David Smith:** I think so.

**Q737 Pamela Nash:** I want to follow up Mr Reid's questions. I am happy to be corrected, but my recollection from the contractors who were affected by this is that they received notification in writing that their payment was deferred. It was not an error or a

query over their payment. They had very clear notification on the 19th that the payment was deferred. Can you give any reason why that might have been?

**David Smith:** No, I cannot. My intelligence from the accounting team is that they made the correct payments on the 19th.

**Q738 Chair:** I want to clarify a couple of points. You mentioned that a couple of the people or organisations with whom you had been negotiating were disingenuous. What is that a euphemism for?

**David Smith:** What we are trying to say is that there were a number of individuals talking to our customers and suppliers, saying specifically that the business was going to go into administration.

**Q739 Chair:** That is not disingenuous. That is either accurate or inaccurate. We prefer not to have euphemisms; we are simple folk and we just want to get it straight. These were people with whom you had been in negotiations, allegedly under confidentiality. They broke that confidentiality; they went out and tried to drop you in it, or undermine your financial position, by letting people know that you were in difficulties. That is bad behaviour and you were badly treated. I understand that, but I just want to be clear that that was the position.

**David Smith:** Yes.

**Q740 Chair:** Let me come back to the first line of your letter: “City Link is aware of unfounded rumours.” It is the question of “unfounded”. These rumours were not unfounded at all, because presumably the people spreading them had a solid basis on which to base the things that they were saying. Therefore, far from being “unfounded rumours”, they were absolutely spot-on. Is that not correct?

**David Smith:** No, it was not correct at the time.

**Q741 Chair:** Okay. Why was it unfounded? The eventual solution that they arrived at, which was ceasing to trade on 24 December, was one of the options being discussed. It was not inevitable; I understand and accept that, but it was clearly one of the options being considered. Therefore it was entirely founded, if that is the opposite of unfounded, that it was a possibility that you would close on 24 December.

**David Smith:** The directors’ position was, and remained throughout that period, that we believed there was a solvent solution for the business. We believed that we could trade through and would have a viable plan for 2015, or that we would have a trade sale.

**Q742 Chair:** I understand that.

**David Smith:** Therefore, that was the basis of our opinion.

**Chair:** I understand that as well.

**David Smith:** If that was the basis of our opinion, anything other than that is unfounded.



**Q743 Chair:** I understand all these options, but it was not an unfounded rumour to say that one of the options under consideration was closure on 24 December. Therefore to say “unfounded rumour” is simply untrue. Had you given a more balanced submission to your suppliers or senior staff and said, “Look, a number of things are being considered. However, our view is such-and-such,” that would have been more truthful. I can understand why it might have undermined your position in the marketplace, but that is not really what we are discussing at the moment. The fact is that your statement was not only misleading but presumably was designed to be misleading.

**David Smith:** No, it was not designed to be anything of the sort. It was designed to give the view from the board on where we thought the business was, and that is what it did.

**Q744 Katy Clark:** We have obviously heard a lot about these unfounded rumours. At what stage were staff actually made aware that their jobs were at risk?

**David Smith:** Formally, I gave them an e-mail on 26 December. Obviously they saw TV and the press on the 25th.

**Q745 Katy Clark:** Do you think it was appropriate that they found out that they were likely to be made redundant on the television on Christmas day?

**David Smith:** No, of course not, and that was not the plan.

**Q746 Katy Clark:** What was the plan?

**David Smith:** To be clear, the business did not have a plan to make any announcements about administration. Our plans were—

**Q747 Katy Clark:** At some point you must have had a plan.

**David Smith:** Yes; bear with me. Our plan was the solvent solution plan, and our intention in the early part of January was to start a consultation process, and to carry that through the spring and early summer. In terms of—

**Q748 Katy Clark:** What was the consultation process? Was it for redundancy?

**David Smith:** For the turnaround plan. In terms of the communication process to staff, on the 22nd, once it had become clear that we were not supported by Better—

**Q749 Katy Clark:** You are saying that on 22 December you began to have a plan.

**David Smith:** Yes. We started to have conversations with the administrator and with Better, and as a group of directors, on what we should do. We concluded that we should say nothing to the staff between the 22nd and the 24th, nor to suppliers or customers, because in the round the best answer for the body of creditors was for us to trade until Christmas eve and not to engender panic in the marketplace.

**Q750 Katy Clark:** What would have happened—

**David Smith:** From a communication point of view, the administrators, who were then going to be responsible for that communication, started to build a plan and we input into that plan. I personally input into that plan.

**Q751 Katy Clark:** When did that plan start to be created? From the 22nd?

**David Smith:** On the 22nd and 23rd. My understanding of that plan was that Hunter's intention and desire was to communicate on the 26th, as the best day, not the 25th or the 24th, and that as part of that plan, formally it was better for me to send a letter or e-mail to staff to say that this was what had happened rather than for him to do it.

**Q752 Katy Clark:** What would have been in the letter on the 26th?

**David Smith:** It was a very matter of fact statement. "Unfortunately we have had to go into administration. The administrators are Hunter Kelly and his team. This is what will happen next." It was really just laying out the process that was signed off by E&Y with me before it got sent. That was as much of a communication plan as there was.

**Q753 Katy Clark:** Between the 22nd and the 26th, your plan was that the staff and the contractors would not be aware there was a problem.

**David Smith:** Essentially, because we did not want to cause panic in the market for the parcels that were being delivered.

**Q754 Katy Clark:** We have heard repeatedly that the lead-up to Christmas is perhaps your busiest time of the year. Were individuals working very long hours during those last few days?

**David Smith:** Yes, they were, but their position as preferred creditors would be protected, and we did pay out. You have heard from Hunter as well that that would get paid out over time.

**Q755 Katy Clark:** Are we talking about the employees or the contractors?

**David Smith:** That was the employees.

**Q756 Katy Clark:** You are saying that the employees are preferred creditors. Did you take that into account in your thinking from 23 December, in terms of your communication plan?

**David Smith:** No.

**Q757 Katy Clark:** In relation to contractors, could you confirm that they are not preferred creditors?

**David Smith:** They are not, but we set aside the payments, as we discussed earlier.

**Q758 Katy Clark:** We have been through that in some detail, and we have also heard a great deal of evidence in relation to contractors and whether they are or are not

going to get paid. Let us just focus on those last few days from 22 December onwards. You have outlined in great detail why you think the contractor relationship is a good one and why you think it means that people will work longer hours. Is it fair to say that a lot of people who were on a self-contracted basis would have been working very long hours during that period?

**David Smith:** Yes. The whole business would have been working incredibly hard during that period; of course, it would.

**Q759 Katy Clark:** Therefore, disproportionately that group will lose out as a result of working very long hours over those last few days.

**David Smith:** I am sorry, I missed the first part of the question.

**Q760 Katy Clark:** Is it fair to say that the contractor group, who are not going to be treated with any kind of preferential status, are disproportionately going to lose out heavily as a result of taking on large amounts of work over those last few days?

**David Smith:** No. We did a calculation looking at the work levels that they had done in the previous two weeks.

**Q761 Katy Clark:** When did you do this calculation?

**David Smith:** On the 22nd. On the 22nd, in order to understand what we needed to pay to the subcontractor community that you are talking about, we looked at what levels of work they had done in the previous two weeks, which was the same in the last week. It does not go up particularly in the last week.

**Q762 Katy Clark:** It is from your historic knowledge.

**David Smith:** We used the previous two weeks' estimates as the basis to say that they would work the same again in the last three days, those three days being a smaller proportion of the week than they would have done in the other weeks. We then did a calculation from that.

**Q763 Katy Clark:** But we have already heard that that money is not ring-fenced in any way for contractors.

**David Smith:** No, but it was physically paid out in the period between the 22nd and the 24th. It was paid out.

**Q764 Katy Clark:** But will those individuals who worked on the 22nd, 23rd and 24th actually get the money?

**David Smith:** They had the money in their bank account before the 24th, or by the 24th. We paid it out.

**Q765 Katy Clark:** That is not the evidence we have heard, as I understand it.

**David Smith:** We paid out £2.4 million in those three days of that week.

**Q766 Katy Clark:** You are saying that people in that position were paid up until 24 December on a notional basis.

**David Smith:** For those three days.

**Q767 Chair:** This is one of the things about which there is doubt. We will have to go back and check this. Jon Moulton's evidence and the evidence of the administrators was that there are effectively three periods in all of this. There is the period which is paid for by the payment that went out on the 17th/19th, when everybody should have got their money and, if they did not because of your delay or mix-up, they might have lost that.

**David Smith:** Yes.

**Q768 Chair:** But everybody should have got that. That is not the evidence we have had so far, but leaving that aside—

**David Smith:** I would agree with that. I think that is right.

**Q769 Chair:** Leaving that aside, there is a middle period where people will lose, particularly the contractors, but the employees will be considered as preferred creditors and they will get up to a maximum of £464 a week, which in some circumstances might not be the amount that they were due. That is that level. Then there is the third period, which is the 22nd to the 24th. You are saying to us that these people were paid; the contractors were paid. Some of the evidence we have is that, no, they were not. We will have to follow some of this up and try to identify the reality. Is that your understanding of the three periods?

**David Smith:** That is right. To be clear, we paid £1,848,000 on the Monday, £936,000 on the Tuesday and £631,000 on the Wednesday. I have a complete list of who was paid.

**Q770 Chair:** Because you normally had a system of paying two weeks in arrears, people must have thought it a bit odd that they were getting paid on a daily basis. Were they actually getting paid on that day?

**David Smith:** No, we paid different amounts to different people through the three days. You did not get paid three days, each day individually.

**Q771 Mr Reid:** You have partially asked my question, Chair. I want to clarify this. In answer to an earlier question from me, Mr Smith, you said that it normally took about two weeks after the work was done for the contractor to be paid, but in this case you paid the contractors straight away.

**David Smith:** Yes.

**Q772 Mr Reid:** Was that on the basis of their historical work?

**David Smith:** Yes. The reason for the payment was that we knew that beyond the 22nd, when we had an opinion as directors that we might have to go into administration, on the 22nd, 23rd and 24th, to continue to trade, we had to make sure that those creditors' positions were not worsened. The only reasonable way of working out what to pay in that

time period was to look at what they had done in the previous two weeks as an approximation. We also talked at the time about setting up a trust as an alternative way of creating money to be paid to them for those three days, but, in reality, we did not have sufficient time to think about the mechanisms of the trust, the trustees, the structure, the amount of money and all the things you would have to think about. Having taken lots of advice, and in full knowledge of the administrators in waiting, this was considered the best way to do what we could for those three days.

**Q773 Mr Reid:** Did the administrator advise you that that was what you should be doing?

**David Smith:** The administrator was comfortable with the process we were following, but obviously they cannot give us guidance, as they are going to be reviewing our performance afterwards.

**Q774 Mr Reid:** Am I right in saying that you made an estimate of the work that would be done by each contractor, so some contractors could be fortunate and get paid more than the work they actually carried out over those three days, but even those fortunate contractors could lose out because they were not getting paid for the previous fortnight?

**David Smith:** Yes, it is possible, but we had no other way of doing the calculation.

**Q775 Mr Reid:** And other contractors, as well as not getting paid anything for the previous fortnight, might also be unfortunate and get paid even less than the work they did over those three days.

**David Smith:** Unfortunately, that is true.

**Q776 Katy Clark:** Christmas is a very expensive time for everybody. How do you think staff were affected by the redundancies?

**David Smith:** In the same way as everybody was affected by them. It is the deepest regret and sorrow we have that we could not save the business and that the timing was what it was.

**Q777 Katy Clark:** But it is a time when individuals rack up a lot of personal expense, whether you are a contractor or on a more conventional contract of employment. You would be spending a lot of money, which you might not spend if you thought you were just about to lose your job.

**David Smith:** Yes, I understand that.

**Q778 Katy Clark:** Was that taken into account in any way in your plan or your thinking?

**David Smith:** No, because our plan—

**Q779 Katy Clark:** Your plan was to wait until after Christmas—until the 26th.

**David Smith:** No, because our plan until the 22nd was that we believed that we had a solvent solution for the future of the business. That was what the directors—

**Q780 Katy Clark:** I thought your plan on the 22nd was to send a letter on the 26th.

**David Smith:** Up until the 22nd, that was what the directors had in mind, and that is what they were doing. On the 22nd, our calculation was that for the creditors as a body the best answer—a better answer than to tell them on the 22nd, “You’re out of a job and you’re leaving today”—was to trade through until close on the 24th. The reason for that was, first, we had paid them that money; and, secondly, we also brought in income of about £3.4 million in the same time period. We would not have done either of those two things, so in the round those creditors would have actually been in a worse position than they were afterwards.

**Q781 Katy Clark:** You are saying that the staff—the people on direct contracts—and also the contractors would have been in a worse position if they had found out on 22 or 23 December rather than 26 December.

**David Smith:** They would not have received the £2.4 million that we paid out. That is certainly true.

**Q782 Chair:** But they would not have worked all those hours either.

**David Smith:** But they would not have got paid for them either. They are getting overtime for that work.

**Q783 Chair:** Let me get this clear. You paid out £2.4 million or so during that period. Is that roughly it?

**David Smith:** Yes. The total payment was £3.4 million, but some of that was for professional advisers and things that we had to have through the period.

**Q784 Chair:** The professional advisers during the period are not the people actually doing the work.

**David Smith:** No; I am trying to give you the total picture. The actual payments in that week were £3.4 million. The professional charges were £463,000.

**Q785 Katy Clark:** Was that to the administrators? Who was that to?

**David Smith:** That was to our advisers.

**Q786 Katy Clark:** Who are they? Lawyers?

**David Smith:** Lawyers and accountants, essentially.

**Q787 Katy Clark:** Lawyers and accountants. How much money?

**David Smith:** In that time period, about £400,000.



**Q788 Mr Reid:** That is a lot of money.

**David Smith:** Yes, but we could not act as directors without advice; £2.9 million was paid out to the staff in total.

**Q789 Katy Clark:** Was the work done during those few days for that £400,000 of legal advice?

**David Smith:** The vast majority of it, yes.

**Q790 Katy Clark:** You have already mentioned that you had a QC's advice.

**David Smith:** Not on this specific piece. The QC's advice was in relation—

**Q791 Katy Clark:** Was that on top of the £400,000?

**David Smith:** No. The QC's advice was in relation to the subcontractor contracts in 2013. It was nothing to do with this.

**Q792 Chair:** There is £400,000 for lawyers and accountants.

**David Smith:** Yes, and £500,000-odd was for fuel to run the vans. The rest went to the subcontractors and hauliers to trade through those few days.

**Q793 Chair:** You got in, I think you said, £3.4 million.

**David Smith:** Thereabouts, yes.

**Q794 Chair:** Presumably you broke even over that period.

**David Smith:** Over those three days.

**Q795 Chair:** Indeed. Had you shut the business down earlier, you would still have had to pay the lawyers and accountants, wouldn't you?

**David Smith:** Yes.

**Q796 Chair:** Let us be clear then. We take that out, since that was an inevitable cost. Over this period, you incurred costs of £2.9 million and you brought in £3.4 million.

**David Smith:** We invoiced £3.4 million. It is still to be collected.

**Q797 Chair:** Let us assume that you get money in from the invoices and pay out the money you were due. Over that period you actually made £500,000 surplus which would otherwise not have been made. You would accept that it is unfair to offset the lawyers' and accountants' costs against that since they would have been incurred anyway. Running the business in those last few days made you half a million pounds.

**David Smith:** It made a contribution to the creditors' pot in the round, assuming that all the debt could be collected, of that sort of money, yes.

**Q798 Chair:** That is a yes, isn't it? Assuming that you pay out all the money you are paying out, which is another possibly debatable question, and you get in all the money that you are owed, which is debatable, you will have made half a million pounds out of running in those last couple of days.

**David Smith:** A half million pound contribution to the rest of the creditors that we did not pay.

**Q799 Chair:** That is right, but you've half a million pounds. Let me be clear about this. The secured creditor above all is Better Capital, so Better Capital are essentially half a million pounds better off by you running it for those last couple of days, as distinct from not running it for the last couple of days.

**David Smith:** If all of the income can be collected, potentially yes.

**Q800 Chair:** And if all the expenditure that is incurred is paid, which is another caveat, Better Capital as a result of running for those last couple of days are half a million pounds better off than might otherwise have been the case.

**David Smith:** Yes, and at the time when we did the calculations we believed it would be break even. In fact, volumes were slightly higher through the last few days so we got slightly more income. That was essentially what was being calculated at the time.

**Q801 Chair:** There was one point I wanted to ask about. Jon Moulton said to us, "There were very extensive plans carefully laid out. All the contingencies were covered. They did not survive contact with Christmas day." That suggests to me that these cunning plans were all drawn up before Christmas day, and presumably Christmas eve, yet you seem to have been suggesting that there was a more ad hoc arrangement and you were working it up as you went along. It was not entirely clear at an earlier stage what you were going to be doing, but the plan was to send out e-mails and letters for that period. Can you see that there seems to be a contradiction there?

**David Smith:** Yes, I can. E&Y were doing some work for Better Capital in the previous weeks, I think. We were not party to very much of that, so there may have been more that they and Better shared between themselves; I do not know. Certainly in terms of a communication plan, there was not a detailed communication plan presented to me before the 22nd, and even on the 22nd we worked on it together through that day and the next day.

**Q802 Chair:** Was there an extensive communications plan in place by the 24th?

**David Smith:** There was a plan to communicate with all staff between the 26th and 27th, I think.

**Q803 Chair:** Sorry, that is not what I am asking you. What I am asking you is whether or not there were very extensive plans carefully laid out and in place by Christmas day?

**David Smith:** I do not know. I did not see them. That was Hunter's responsibility.

**Q804 Chair:** That is strange, because Jon Moulton told us that. You were the managing director. You would have expected to know about something like that, would you not?

**David Smith:** My responsibility for running the business ended on Christmas eve at 7 o'clock. I did work with Hunter from the 22nd to the 24th on the communication plan that was due to be presented to staff from the 26th onwards.

**Q805 Chair:** So there was a plan ready by the 24th for use on the 26th and 27th.

**David Smith:** Yes, and I have said that.

**Q806 Chair:** I was not entirely clear about that.

**David Smith:** But there was not an extensive plan before the 22nd, that I had seen.

**Chair:** No, I understand that.

**Q807 Pamela Nash:** I apologise for going over the material, but I want to be clear in my mind. For exactly what period of time in December are subcontractors not being paid? What dates?

**David Smith:** I do not know the exact date, but it will be approximately two weeks from the 8th to the 22nd, something of that order.

**Q808 Pamela Nash:** The payment before that was the payment that—

**David Smith:** That was paid on the 19th.

**Q809 Pamela Nash:** And they were paid for the last three days separately?

**David Smith:** Yes.

**Q810 Pamela Nash:** In addition to what Katy outlined about personal expenditure at Christmas, these subcontractors were taking on additional staff, and the risk of that, at the request of City Link. I am sure that went across the Christmas period, through October, November and December, but it was more so in those couple of weeks than at any other time. If you have information to the contrary please let me know, but that is the evidence we have taken. They were renting additional vehicles in order to meet that Christmas rush, yet they have not been paid for that. What is your response and your message to those people who were pressured into taking on that additional risk by City Link employers?

**David Smith:** My message is the same as it is to staff and to customers. It is with the deepest sorrow and regret that we were unable to turn around City Link, despite the efforts that we all put into that. As directors, we believed that we were going to get support from Better right up until 22 December. Once it was clear that we were not going to get that, we took the appropriate steps to put the business into administration in an orderly fashion. Had we known or had we believed that Better were not going to support the business at any time before that, we would have done the same things as we did on the 22nd. It is deeply, deeply regrettable that those people have ended up in that position. They have lost

a significant amount of money. I have personally had many sets of correspondence with them, so I understand and sympathise with what you are hearing as well. I, like the rest of the directors, will continue to do everything we can to support the administrators to get as much cash back as possible, but I think the truth is that they will see a very limited return on what is still outstanding.

**Q811 Pamela Nash:** Just to be clear, you would refute any claims that requests to these people to take on that additional expense and work were ever at any point done with the knowledge that the business was going to go under and that there was a significant risk that they were not going to be paid.

**David Smith:** No. We understand, and they understood, that the business had a cycle. It was significantly higher in peak than at any other time. That is why it is called peak. We understood and they understood that they would take on additional resource in that time period. We supported them in doing that because we believed that we were being supported by our shareholder at Better Capital. Had we not been in that position, of course we would not have taken any other decision but to put the business into administration.

**Q812 Pamela Nash:** Do you think that City Link could have been saved had Better Capital given the support that you expected?

**David Smith:** My belief is that, yes, it could, but my belief is also that the return on investment that Better would look for as a private equity house would have been lower than they would have normally anticipated, so I can understand why they made the decision they made.

**Q813 Pamela Nash:** But they could have made a return; it could have been brought back to profit.

**David Smith:** Probably over a two or three-year period they would have made a reasonable return, yes. That was what our plans were showing.

**Q814 Chair:** The way that this works is that they have cut their losses, but a substantial amount of the losses incurred have been effectively passed on to the taxpayer, because the taxpayer, through the Insolvency Service, is going to have to meet redundancy costs and a whole number of these expenses. Is that correct?

**David Smith:** I am not an expert in insolvency practice but I understand and believe that that is correct, yes.

**Q815 Pamela Nash:** Part of the evidence that we have received is that not only were the subcontractors encouraged to take on that additional risk in staff and vans—I appreciate the fact that you were hoping to save the business at that point—but it was put to them that work might not be put their way in January, should the company continue, if they did not take on this risk. They were bullied into taking on extra staff and vans. Are you aware of this happening, first of all in Scotland, where we took evidence, and was this policy in place across the country?

**David Smith:** No, of course it was not. The business would not entertain that as a company policy. I was not aware of that as a way of behaving in any of the management team. I think it is very clear—

**Q816 Pamela Nash:** Has it been raised with you before today?

**David Smith:** No, it has not. I have not heard it before today. I think it is very clear that the business in December is running at 200% of what it is running at in the second week of January. There clearly is a step down in activity. It is also normal to look at the people who have supported you at peak and look after them when the periods are lower, as a natural thing to do, but nothing more than that.

**Q817 Mr Reid:** Before 22 December, did you think that the business could be saved?

**David Smith:** Yes.

**Q818 Mr Reid:** Was that because of promises that were made to you by Better Capital?

**David Smith:** No; it was because we had a solvent plan. We had a set of steps on the journey of that plan that were being delivered and were tangibly in place. It was because I and many other members of the team had turned around businesses in this position before, and it was because Better Capital was supportive and prepared to put in the cash. It was the set of those elements, not just Better Capital.

**Q819 Mr Reid:** Up until the 21st, Better Capital were telling you that they were supporting the business.

**David Smith:** Yes.

**Q820 Mr Reid:** And on the 22nd, Better Capital told you that they were no longer supporting the business.

**David Smith:** Yes. We had a meeting on 19 December with Better Capital in London to present the turnaround plan in its detail, and all the elements that they were requesting of us from the letter of 3 December. We presented that and it was a clear, coherent and robust plan.

**Q821 Mr Reid:** Do you also think that even on the 22nd, Better Capital could still have saved the business and made a return on the capital, but they did not consider the return on the capital to be good enough for them? Is that a fair statement?

**David Smith:** I would not want to put words into their mouth as to why they made their decision.

**Q822 Mr Reid:** But you said in an earlier answer—

**David Smith:** That would be my judgment, but I don't know that it is theirs.

**Q823 Mr Reid:** That is your judgment.  
**David Smith:** Yes.

**Q824 Mr Reid:** I think you can understand why we are all very suspicious about this. The organisation that gains from keeping the business going through December and putting it into administration on the 24th was Better Capital, and Better Capital, according to your evidence, were telling you right up until the 21st that they were supporting you. Then suddenly at the optimum time for them, but the worst time for all the contractors, they suddenly decide that they are no longer supporting you. Can you understand why we are all a bit suspicious about Better Capital's intentions?

**David Smith:** I can understand that.

**Q825 Chair:** I want to ask a couple of other points. Do you know how many former directors of City Link are also directors of other Better Capital entities?

**David Smith:** I do not know, but I cannot think of any that are currently in the Better Capital world, other than Tom Wright, who is still a director at City Link. Then there are the founding partners, Jon Moulton, Mark Aldridge and Nick Sanders. I think Rob Asplin might at one time have been a director of City Link as well. I think there are five people.

**Q826 Chair:** There are five people who were directors of City Link who were also directors of Better Capital.

**David Smith:** Of other parts of Better Capital.

**Q827 Chair:** Have you had any discussions with Better Capital about being involved as a director in any of the other arms of the empire, or are you involved?

**David Smith:** No, I was not. The only involvement I had with Better Capital at all was in City Link.

**Q828 Chair:** Jon Moulton mentioned to us that he thought he would give the directors of City Link a mark out of 10. You saw that presumably. He seemed to give you seven or eight out of 10.

**David Smith:** Yes, that is probably as close as I will get to a reference from Jon.

**Q829 Chair:** Do you think that was a fair assessment?

**David Smith:** I think the business and the directors tried incredibly hard to turn around a business that was losing £65 million a year when we started. They made strong progress over the three years, but ultimately failed and could not turn it around. I do not know what the score would be, but I don't think it is a zero, which some people suggested would be the case.

**Q830 Chair:** Just to draw things together, we came into this as the Scottish Affairs Committee because of the concern of staff and so on. I know that BIS will want to



pick up on some other aspects of it. Am I right in thinking that you understand and believe that all staff should end up getting paid everything they are owed, by somebody, up to the limit of £464 a week, which I understand to be the upper limit on payments like redundancy and so on? Is that your understanding of the position?

**David Smith:** Not quite.

**Q831 Chair:** Clarify it for us.

**David Smith:** I think they will get paid as you have outlined, but people who had contracts of employment with redundancy terms, like myself for instance, will not get that money back.

**Q832 Chair:** That is the £464 figure. There is an upper cash limit. It is only those on a higher salary who will not get the higher level. Everybody should get paid everything for the period below that. Is that your understanding?

**David Smith:** My understanding from the inputs I have had, and from advice I have been given, is that as preferred creditors, yes, that is the case. They will get their basic pay as was required—with overtime in other words—and they will get holiday pay and redundancy.

**Q833 Chair:** Much of that might certainly end up coming from the state in the short term, depending on their status as preferred creditors. The other issue I wanted you to clarify is the question of overtime. You mentioned that they would get their basic salary and overtime, but it would depend upon how many hours of overtime they did, wouldn't it, whether or not it took them above the £464 level?

**David Smith:** If they go over the threshold, yes, it would.

**Q834 Chair:** Some of the hourly paid workers who were working almost all the hours that God sent in the last period might end up losing out, but not all that much, depending on how much they did above £464.

**David Smith:** I think that is correct; yes.

**Q835 Chair:** Okay, thanks. As I indicated to you earlier, at the end we always ask people whether or not there are any answers they have prepared to questions that we have not asked. Are there any points that you feel we should have raised with you that we have not, or any final points that you want to leave us with that we have not adequately covered?

**David Smith:** The only area that I would leave you with, which is an area of difficulty for a director, not just me but going forward, is that there is a clear challenge for us as directors when you get to the position of potential insolvency and consultation with staff. We did not spend too much time talking about it today. In the period post-22 December our responsibilities as directors switched quite markedly towards the body of creditors in the round, rather than in normal times when our normal duty would be consultation with the staff.

In our particular case, given the outlook of the business, it was better for us not to start the consultation process, because we would have ended up in a position where we would have triggered potential panic in the customer base. I think something for the Committee to look at and consider is the interplay between normal consultation and how that changes when you go into an insolvency or administration world. As a director, it is very clear that the two are pulling you in different directions, potentially.

**Q836 Chair:** When you said better for us, it is a bit like the Lone Ranger and Tonto. It depends who the “us” was.

**David Smith:** I was talking about the body of creditors in the round, of which obviously the employees are a subset, but they are a subset and not the core body of the thought process.

**Q837 Chair:** Had you been closing the business down in March or August, presumably the same sorts of pressures would not have applied, because you would not have the substantial build-up of business from which, as we have heard already, you made a half million pound surplus that might otherwise not have been made, followed by a trough after new year. You could have had a longer, more drawn-out and more consultative arrangement. Is that fair?

**David Smith:** No. The legal structure of the business was the same for the entire time that it was owned by Better Capital. At any point, we would have ended up with the losses, and Better Capital being the secured creditor getting whatever was left. The quantum of the amount that was left outstanding for everybody else would have been smaller than they would have been paid, but they still would not have got the money.

The second point is that the reason we ended up where we did, and did not go into a 45-day consultation period, is that the losses in the business were significant, regardless of which month of the year you were in. I suspect, if you were to ask the administrators why they did not take a 45-day process on either, it is because the losses were far greater than the amount you would end up paying back to a preferred creditor in a case for not following through on the consultation process. Regardless of what time you would have been in, I do not think any of us would have gone to a 45-day consultation period.

**Q838 Chair:** Because that would have cost you more.

**David Smith:** Because it would have ended up costing the body of creditors more money than just effectively taking a case for not following due process.

**Q839 Chair:** And you knew as a safeguard that the Government was there to pick up any costs of redundancies.

**David Smith:** The redundancy service pays that and then claims back the preferred creditor element.

**Q840 Chair:** If there is enough money.

**David Smith:** If there is enough money; but there is enough money for the preferred creditor in this situation.

**Q841 Chair:** Presumably the difference would have been that, had it been 22 June when the decision was taken, you probably would have shut it right away rather than struggling on to 24 June.

**David Smith:** Possibly.

**Q842 Chair:** Because you had half a million pounds to make during that period. You used the term “customers”, but presumably you could have switched off the clients, in the sense that those who were buying your service—those who would have been inconvenienced—would have been the ultimate recipients of the parcels. Jon Moulton suggested that the staff would possibly steal them if you did not continue the business in secret.

**David Smith:** The primary problem is always shutting at a hard-edged point. It is very difficult to know where the parcels are going to be. The only day of the year when you know where all the parcels are, and they are under lock and key, is Christmas eve through to Boxing day morning. At any other point, regardless of what point in the year it is, you still have parcels in the system and you are not entirely sure where they are, who has got them or why they have got them.

**Q843 Chair:** If you are running a business like this, the best time to close it down is on Christmas eve because then people cannot steal the parcels.

**David Smith:** From that perspective, yes.

**Q844 Chair:** What other perspective is there? You just indicated that there is pretty much no other perspective that counts in these matters.

**David Smith:** If you wanted to take the view that you did not care that things would get stolen, and you were prepared to take that risk, you could choose a different date.

**Chair:** Thank you for clarifying that. If there are no other questions, I thank you very much for coming along. Your answers have been very helpful in terms of assisting us in drawing up our report.