



Scottish Affairs Committee

Oral evidence: Sports Direct: employment practises and the sale of USC, HC 1111

Wednesday 25 March 2015

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Members present: Mr Ian Davidson (Chair); Jim McGovern; Iain McKenzie; Graeme Morrice; Pamela Nash; Simon Reeve.

Questions 393-513

Witnesses: **Philip Duffy**, Duff & Phelps, USC Administrator, gave evidence.

Q393 Chair: I welcome you to this meeting of the Scottish Affairs Committee. We have been looking at various matters relating to Sports Direct, particularly the pre-pack administration of the USC business. I apologise for the delay: the earlier session ran for quite a bit longer than expected. Will you please introduce yourself and say where you fit into the grand order of things and why you are here? We can then go into the specific questions.

Philip Duffy: My name is Philip Duffy. I am a managing director in the UK restructuring division of Duff & Phelps. I am joint administrator of USC. As a joint administrator, I am an officer of the court. We have a duty to creditors and a duty to report on the conduct of directors. I was appointed as administrator on the afternoon of 13 January.

Q394 Chair: Thank you. Unless I am mistaken, you were present throughout the previous session, weren't you?

Philip Duffy: Yes.

Q395 Chair: And you heard all that.

Philip Duffy: Yes.

Q396 Chair: When you reflect on the points that we raised, was there anywhere where you thought we had misunderstood or missed the point, particularly in relation to your own role, the timetable, what happened and so on?

Philip Duffy: The witness might have done, but not the Committee.

Q397 Chair: Right. I wanted to be clear, first, about how you thought we understood things. We have obviously read up on this and tried to be as clear as we could. In that context, will you clarify for us where you thought that the witness perhaps misunderstood the position?

Philip Duffy: First of all, we never dealt with the chief executive.

Q398 Chair: Right.

Philip Duffy: We dealt with someone who reported to the chief executive, although the chief executive did ultimately appoint us as the administrator, on behalf of the board of USC.

Q399 Chair: Can you clarify whether we were right in our assumption that the date of 14 November—

Philip Duffy: That was the first meeting. We were first contacted for a meeting on 11 November, and we had the meeting on the 14th.

Q400 Chair: Am I right in thinking that that was quite a significant move forward? It is not the sort of thing that just happens casually.

Philip Duffy: Well, we were meeting with Sports Direct as secured creditor on USC. We didn't get any information on USC, but they were looking at their options: as secured creditor in respect of USC, what could they do if USC had financial difficulties?

Q401 Chair: So am I right in thinking that, from 14 November, there was the option of closure and administration?

Philip Duffy: It wasn't that detailed. It was about what the options were. As a secured creditor you can issue a winding-up petition, you can appoint administrators, you can remove the board of the company, change management and so on. It was that sort of level of detail. There was no specific detail about what we would do if it was in administration.

Q402 Chair: I would be grateful if you could clarify whether we got this wrong: regarding the consultation with staff, we were making the assumption that so many different things

were in play that it would have been entirely reasonable for the company to have started to have discussions with its staff, saying, “Look, there are a whole number of options here that might happen. We are consulting with you about what you think.” Was that unreasonable?

Philip Duffy: Probably not at that time, no, because it was very much initial discussion. We were not advising the company on consultation issues or anything like that. We were just advising on potential restructuring situations.

Q403 Chair: When do you think it got to the stage where a pre-pack administration became a real possibility?

Philip Duffy: It was inevitable.

Q404 Chair: No, not necessarily inevitable, but a real and genuine possibility. Presumably, its being a possibility came before it became inevitable?

Philip Duffy: On 17 December, one of my fellow administrators, Robert Palmer of the Gallagher Partnership, had a conversation with Sports Direct, because Sports Direct had received—sorry, USC; when I say Sports Direct, it is the group we were dealing with—a statutory demand from one of the suppliers on 10 December, which was due to expire on 31 December. So on 17 December we were contacted with: “We have had a statutory demand. We are negotiating with the supplier, but where are you over the Christmas period in case we need to contact you?”

Q405 Chair: I would take the view that from that date at the very least there should have been some degree of consultation with staff. From that date, there was the very real possibility of closure. Is that correct?

Philip Duffy: It is certainly a grey area, and it gets greyer as the time goes on. If you receive a statutory demand, there are financial issues with the company, but in our experience of dealing with lots of companies over many years, lots of companies receive statutory demands and not all, if any, will consult employees, as they hope to resolve the situation. Sports Direct were telling us they wanted to resolve the situation with Diesel, the supplier at that time.

Q406 Chair: You heard how, basically, the fact that employees got 15 minutes’ notice of closure was all down to you.

Philip Duffy: Nobody had given them notice beforehand, so we had to do something.

Q407 Chair: Who should have given them some degree of either notice or consultation beforehand?

Philip Duffy: If I go from the timeline of our accelerated involvement, on 17 December it was, “We have received a notification, a statutory demand, from Diesel. We are negotiating with them. It runs out on 31 December.” After Christmas, on 6 January, we were advised that they were still negotiating with Diesel—they had had a seven-day informal stay on presenting the petition. Once the statutory demand expired, the supplier could issue a winding-up petition immediately. So the company was at threat of having a winding-up petition issued against it. It told us it had negotiated a seven-day informal stay with Diesel, and they were carrying out further negotiations with the Diesel supplier.

On 6 January they issued, because of the way the negotiations were going, what we call a notice of intention to appoint administrators. So the company is not in administration, but they are putting down a notice. The company, USC, issued a notice of intention to appoint administrators on the 6th to protect it, so that nobody could issue a winding-up petition at that stage. You are coming to the point now where they have issued a notice of intention to appoint. That is public evidence that they think the company is insolvent. You could argue that at that point consultation should have started. It is a public document, and it actually hit the press.

Q408 Chair: If it was a public document—

Philip Duffy: It is difficult to find, but it is a public document.

Q409 Chair: Yes, but if it is a public document by that date—in a sense, you are almost saying to me that there should have been consultation by then—surely, in the run-up to that being published, it was clearly under consideration that that would happen, and consultation should have started at that stage.

Philip Duffy: We were not dealing with the company at that stage. We went from 17 December to 6 January. That was the next time we had any dealings with the company.

Q410 Chair: Sorry, by the company, who do you mean?

Philip Duffy: USC, or the group. Over that Christmas period, we did not have any dealings with the company and the group.

Q411 Chair: I see. So if not you, should somebody?

Philip Duffy: It is a grey area. I am not a legal expert in employment law, but certainly the 6th is a line in the sand where insolvency was very likely, because you have issued a notice of intention to appoint.

Q412 Chair: Undoubtedly, unequivocally, it should have taken place from the 6th. What we are not clear about is going backwards.

Philip Duffy: Because we were not involved in any negotiations with Diesel or anything like that.

Q413 Chair: So that would not have been down to you?

Philip Duffy: No, we were only advising Sports Direct from the 14th, and then from the 6th onwards it was USC.

Q414 Chair: And therefore the suggestion that the 15 minutes' notice was your fault is not how you would see it.

Philip Duffy: We had to do it because they had received no notice—

Q415 Chair: Yes, you had to do it by that stage. What we are trying to identify is that somebody else should have given a greater degree of notice before you got to that stage.

Philip Duffy: From the 6th—we had a meeting on the 7th where we were advised that the company was removing stock from one warehouse to another warehouse because of issues over security, which we understand was the landlord issue, and that we should prepare for the administration of the business in detail.

That evening, it had hit the TVs and the press that the company was closing or removing stock from the warehouse—that Sports Direct was removing its stock from the warehouse. We arranged a meeting with the company on the morning of the 9th. That morning, we offered to give them draft letters of consultation, saying, “You should be giving these to your employees.” We said, “We can prepare draft letters.” We weren’t advising them. We said, “We think that you should do a consultation. Here are some standard letters that we would use in insolvency situations.” That was on Friday the 9th.

Q416 Simon Reeve: Who did you say that to?

Philip Duffy: That was to the senior management team we were dealing with.

Q417 Simon Reeve: Who?

Philip Duffy: It was Justin Barnes and Ben Gardener.

Q418 Chair: Who are senior management people in USC?

Philip Duffy: In Sports Direct group.

Q419 Simon Reeve: Where do they fit in? You heard the discussion about pyramids, parallel structures and different universes and so on.

Philip Duffy: I think that Justin Barnes is international brand manager so he looks after all the brands in the Sports Direct group.

Q420 Simon Reeve: You said that you began to deal with USC on 6 January so prior to that you dealt with Sports Direct International.

Philip Duffy: The things overlap.

Q421 Simon Reeve: What I am going to ask you is: were you dealing with the same people?

Philip Duffy: Yes. Sorry, there were maybe additional people like group financial controller and so on, and in-house legal counsel, inserting meetings earlier on.

Q422 Simon Reeve: But the people on 9 January to whom you offered the draft letters were the same people you had been dealing with, albeit with Sports Direct hats on, prior to that.

Philip Duffy: Yes.

Q423 Simon Reeve: So when you say that you dealt with USC for the first time on 6 January, you did in name, but in terms of personality, it was a continuous—

Philip Duffy: Yes.

Q424 Chair: Can I just go back to some more basic things about the question of pre-pack administration? What is the advantage of doing a pre-pack as distinct from a normal administration?

Philip Duffy: It normally results in higher realisations of the assets and more jobs saved. The stats show that. You get a better return to creditors and better safeguarding of jobs.

Q425 Chair: Could you maybe clarify for me, because we also had discussions as a Committee about Citylink—when they were trying to sell off Citylink to somebody else. Presumably, selling off this business would have been the best. Rather than having it completely collapse, selling it off in a pre-pack is better than letting it collapse because selling it off in a pre-pack is almost selling all the assets shorn of the debts.

Philip Duffy: In the insolvency situation, whether it is a pre-pack or not, that is exactly the same situation. If you sell it in a pre-pack or you sell it after trading it, you do not sell the liabilities.

Q426 Chair: Yes, so the only difference between a pre-pack and a sale, as it were, is that you shed the debts.

Philip Duffy: Sorry, what do you mean by sale?

Q427 Chair: We dealt with Citylink. Efforts were made to sell it as a going concern.

Philip Duffy: Before it went into administration.

Chair: That's right.

Philip Duffy: That's correct.

Q428 Chair: So here, presumably there would have been an option to try to sell USC as a going business but if it had done that, it would have taken the debts with it.

Philip Duffy: That's correct, yes—a going concern. On Wednesday 7th, because it hit the press, we received a notice from Atradius, which is a trade credit insurer, that the company and/or the proposed administrators were unable to sell any stock from the stores.

Chair: I see.

Philip Duffy: Normally, in retail administrations, you would trade the business for two, three or four weeks to try to find a buyer on the open market while negotiating with suppliers. We had no alternative. We could not trade the business. I would have been liable for conversion at that point; that is a personal liability against me, my house, wife and kids. We would have been liable for that cost and I did not want to take that risk.

Q429 Chair: I understand. Can I just be clear on something? I do not understand some of the terms, and I don't think my colleagues would, either. If you had stock and were able to sell it on, presumably that would bring money into the business, which would help pay the amount owed to those people who had debts with the company.

Philip Duffy: That's correct, but I was on notice from Atradius, the trade credit insurer of the suppliers, that the product that their clients supply, which was subject to their licence agreements, could not be sold.

Q430 Chair: I see. Sorry, yes.

Philip Duffy: Therefore, if I had sold it in stores I would have been personally liable for conversion, which is a personal liability.

Q431 Chair: Right. I don't quite understand the term conversion.

Philip Duffy: That is converting somebody's product into something else, which they do not want to happen. So, you are selling something that you should not sell. It is illegal to do that.

Q432 Simon Reeve: Let us assume that you have a shop with stock in it. What you are saying is that you as administrator did not own that stock in the sense that you were able to sell it. Somebody else said, "If you sell it you are turning what we own into money and you are then responsible for that."

Philip Duffy: The whole proceeds of that.

Q433 Simon Reeve: What perhaps the Committee finds difficult to understand is why that stock was not theirs to sell.

Philip Duffy: It was under licence, so the licence holder had the ability to tell the company whether it could sell that stock. It was also subject to intention of title. The company had yet to pay for a good deal of stock.

Q434 Simon Reeve: So if I go to the wholesaler and pay £50 for £50-worth of stock, in cash, and open up my stall on the market, I can then sell it.

Philip Duffy: Subject to any licence agreement.

Q435 Simon Reeve: But the way this was working, they didn't actually "own", in the sense that we would understand, the stock that they were selling.

Philip Duffy: That is normal in most retail businesses.

Q436 Simon Reeve: So there was a permission needed to sell what was in their shops, and that was withdrawn. If you sell it anyway, they might come after you for the value of the stock.

Philip Duffy: Yes, the gross value as well, not just the net cost. You buy a pair of socks for £1 and sell for £3 and they would claim the £3 off me not the £1.

Q437 Chair: Can you then clarify for me how it was possible for the shell to be sold on as part of a pre-pack? Did that contain stock with it?

Philip Duffy: The shell?

Q438 Chair: Whatever was left of USC. Presumably it was the assets with the debts being dumped. Did that include the stock when it was then sold on to Sports Direct?

Philip Duffy: As administrators, we sell only whatever has right, title and interest. I was passing on that risk of conversion over to the purchaser.

Q439 Simon Reeve: But if Sports Direct buy USC stock, they buy it pretty confident that they are going to be able to sell it in the way they were, as USC.

Philip Duffy: Because they have relationships with suppliers.

Q440 Simon Reeve: Because they have relationships with suppliers. If I have a roomful of stuff that I want to sell, but there is debt attached to it, by doing what they did, later on I will be able to sell that roomful of stuff but I won't have the debt any more.

Philip Duffy: Any retailer has relationships with suppliers. As administrators, we don't tend to have relationships with suppliers.

Q441 Chair: I think we are in danger of losing the will to live. Some of this is quite complex and, while it is fascinating, I am not sure we need to know it.

Philip Duffy: It was the reason for the pre-pack. Normally, we would trade retail businesses but I could not do that in this scenario.

Q442 Chair: I understand that. Can I clarify this point? Apart then from the closure of the USC warehouse in Dundonald and the shedding of the debt, what has the impact been of selling the remainder of USC to Republic?

Philip Duffy: We've realised assets for cash—money—which will be distributed to creditors. Preferential creditors will get the first, so the employees' arrears of wages will come first. Then it will be the secured creditor, with a 20% deduction for unsecured creditors. There is a fund or prescribed part. Preferential, secured and unsecured creditors all benefit from the sale.

Q443 Chair: I see. Can I clarify this? When I raised this with our previous guest, I was under the impression that the unsecured creditors were getting nothing at all.

Philip Duffy: No, there is going to be a distribution to unsecured creditors.

Q444 Chair: Right. Well, he didn't correct me on that, so I presumed that he wasn't aware of it.

Philip Duffy: I don't think he knew.

Q445 Chair: Okay. I think we would have expected that he would have known. Do I take it, then, that Sports Direct, as the secured creditor, has got all its money?

Philip Duffy: No.

Q446 Chair: Can you clarify, then, what happened to its secured debt, which I think was—

Philip Duffy: It was £7.9 million.

Q447 Chair: We have got the figure of £7.367 million, but let's not quibble over the odd £600,000.

Philip Duffy: We have had nothing at this stage, where we have taken on the funds. We have got work to do in terms of the exact level of the debt, but we estimate at the moment that we will get about £750,000 back.

Q448 Chair: I am slightly surprised. I was under the impression, from the discussions that we had in relation to CityLink, that a secured creditor would get their money ahead of all the unsecured creditors.

Philip Duffy: No; the Insolvency Act has a prescribed part, so 20% of whatever you realise is put into a fund for the unsecured creditors and they get money at the same time as secured creditors, under a floating charge, get money.

Q449 Chair: How much in the pound are the unsecured creditors likely to get?

Philip Duffy: There is a fund at the moment of about £200,000, we estimate.

Q450 Chair: They will get £200,000 out of what—£15 million of debt?

Philip Duffy: The level of claims may not be £15 million, because as we have sold the business and assets of USC to Republic, they have taken over the liability for

retention of title. We estimate that there were significant levels of retention of title. This is where a supplier will supply stock and not get paid, so it is still theirs until they get paid. We estimate that the level of claims will come down significantly, because Sports Direct group or Republic will have to settle the valid claims with suppliers.

Q451 Chair: Coming back to the question, how much in the pound will those who are not covered by that get?

Philip Duffy: We don't know at this stage, but it will be in the low single pence, I imagine. That is my best estimate at this stage.

Q452 Chair: Coming back to the point that we also made about HMRC, they are liable to get only several pence in the pound on the £500,000 or so in debt to them?

Philip Duffy: They went *pari passu* with suppliers, yes.

Q453 Chair: Can I clarify the question of salaries, wages, redundancy payments and so on? Are these being met in full, and if so, by whom?

Philip Duffy: I have detail of the actual figures, if you want. The redundancy payments service has paid out £70,000 in preferential claims and £127,000 in unsecured claims, which is in lieu of notice in redundancy. We estimate that the total amount of preferential claims will be about £90,000, because some claims will not yet be finalised, and the total amount of unsecured claims will be £190,000. The preferential claims will get paid in full, so the money we are holding will go back to the Government—the Government will receive back £90,000 of what they paid out—but the £190,000 will be an unsecured dividend, so it will be pence in the pound on that.

Q454 Chair: Goodness me. So when I was suggesting to Dr Hellawell that in fact the state would end up picking up the redundancy payments and the wages, that was not correct?

Philip Duffy: The redundancy payments, yes, and they will get a dividend back, but it will only be pence in the pound. The preferential element will be paid out of the funds we are holding.

Q455 Chair: So all the wages will be paid out from the company, from the money, and the state will not have to pick up that cost?

Philip Duffy: There is a limit per person on preferential—

Q456 Chair: It's £464, isn't it?

Philip Duffy: No, that is the amount the Government pay. The preferential limit is £800. It has been £800 since 1986; it has never increased for some reason.

Q457 Chair: Again, just to be clear, the employees will get their wages paid, without the state having to contribute, up to £800?

Philip Duffy: Yes.

Q458 Chair: Is it £800 per week?

Philip Duffy: No, in total.

Q459 Chair: Right. Then the payment in lieu of notice will be made by the state?

Philip Duffy: Yes. And redundancy.

Q460 Chair: Okay. So some of that will undoubtedly be paid by the state, on top of the money that we already identified as being lost through HMRC.

Philip Duffy: Yes.

Q461 Chair: Okay. That is much clearer. Can I just come back to this question then of pre-pack administration and the use that employers could make of it to avoid the legislative obligations to consult? Here, we have clearly had a firm that by one route or another has managed to avoid its legislative responsibility to consult. That is correct, is it not?

Philip Duffy: I do not know. I am not an employment lawyer. I have told you my thought process on the timing. Prior to the 6th, it is a grey area. After the 6th it is a less grey area. On the 9th, we offered draft letters to go in consultation.

Q462 Chair: And did they take that offer up?

Philip Duffy: We e-mailed it to them, yes.

Q463 Chair: You e-mailed them to the company. Did they then use them?

Philip Duffy: No, I do not think so.

Q464 Chair: No, I presume not.

Philip Duffy: Because we were the ones who had to give the employees notice.

Q465 Chair: And you gave the 15 minutes' notice on the basis that there was nothing else you could do in those circumstances.

Philip Duffy: That is correct. The warehouse had been emptied. From an administrator's point of view, it was a financial burden. Administrators have to mitigate claims against the company and losses.

Q466 Chair: And from your point of view, it was an entirely sensible decision to give people 15 minutes' notice on the basis that the redundancy payments and the payments in lieu of notice were going to be picked up by the Government.

Philip Duffy: The law states that you have to consult, no matter how long that consultation is. The fact that we gave 15 minutes' notice was on advice from our lawyers. In my mind, it is complying with the law, but not really with the spirit of how the law was created, but we have to do that to mitigate claims against the company.

Chair: Okay, I understand that. Jim, do you want to come in?

Q467 Jim McGovern: Thanks for coming along today. Just on the point that you were covering there, a lack of consultation would presumably allow former employees to go to an employment tribunal and claim some sort of compensation for that lack of consultation.

Philip Duffy: I presume so, yes. It has happened in past administrations and insolvencies; employees have gone to tribunal and won cases.

Q468 Jim McGovern: It is obviously devastating to get 15 minutes' notice and you are out of a job, but compensation for that would be available in the legal process.

Philip Duffy: That is true.

Q469 Jim McGovern: I think maybe the Chair has covered most of the points, and I am possibly reiterating something he has already said, but why were the work force not informed until 6 January?

Philip Duffy: It was the 14th.

Q470 Jim McGovern: Well, what I have here is that they were told about a possible administration on 6 January, but they were told that they were losing their jobs some days later.

Philip Duffy: I do not know anything about 6 January. We were appointed on 13 January.

Q471 Simon Reeve: I think there was a conversation between you and USC first about the possibility of administration, but the work force were not told on that day.

Philip Duffy: I do not know whether they were or not. I am presuming not, but the notice of intention to appoint administrators was filed at court on 6 January, and we were appointed on 13 January.

Q472 Jim McGovern: Were the work force informed at that stage?

Philip Duffy: I do not presume so, but we were not involved in the detail of that. That was still in the company's hands. The company's directors are still in control of the company prior to the date of administration, which was 13 January.

Q473 Jim McGovern: You have already said that you heard the evidence from the previous witness. In my understanding, he was saying quite clearly that USC was not going into administration; it was still trying to save the company.

Philip Duffy: On the 6th, it issued a notice of intention to appoint administrators. Occasionally that can be used as a protective method while resolving a financial issue, but once that notice has been issued, 95 times out of 100, it will end in administration or some form of insolvency process.

Q474 Simon Reeve: If the chairman of the company's evidence was right, he must have been unaware of the fact of that notice.

Philip Duffy: I presume so, yes. It was a document signed by the chief executive of the group, who was the director of the company, USC.

Q475 Jim McGovern: So when the chairman of the company is saying that he was absolutely unaware of this and that the ultimate aim was still to keep the company afloat, do you agree or disagree with that?

Philip Duffy: That is a question for Sports Direct, but the facts are that a notice of intention to appoint was issued on 6 January.

Q476 Jim McGovern: At what point did you know which members of USC staff would be redeployed elsewhere and how many would be made redundant?

Philip Duffy: We had a detailed meeting with USC on 9 January because of the Atradius notice. My judgment call was that the only way of saving the rest of the business was to do a pre-pack sale. If we were appointed administrators without a sale of the business, we would have had to shut it on day one and make wholesale redundancies because we couldn't trade. That detailed process started on 9 January.

We worked all over the weekend—Saturday, Sunday and Monday—and agreed a sale of the business on the Tuesday. It is normal to market a business by going out to market, advertising the business for sale and trying to get as many interested parties as possible. My judgment call was that we didn't have time to do that because it would have taken two or three weeks to get the market going, and I considered that the only potential purchaser would have been a Sports Direct group member because USC owned only the stock in stores, subject to retention of title. It didn't have any warehouse stock, so we couldn't replenish anything in stores. It didn't own the brand USC, which was owned by a brand company within Sports Direct. On the conversion issue—everyday trade—the company was liable for its own conversion, too, because it received notice from Atradius not to sell any stock.

Q477 Jim McGovern: I entirely understand what you said earlier about “conversion.” I am not quite familiar with that term, but I know what you said about you, your wife and your family possibly ending out on the street. I can sympathise with that, and I understand why you would want to avoid it, but do you have a view as to whether this could have been handled better?

Philip Duffy: I personally do not like it when there isn't a good lead time to plan an administration because people can have a hold over you—ransom creditors can have hold over you. Unless you know the exact situation, it leads to a reduction in the realisation of assets. A shorter time frame is always more difficult. We would prefer a longer time frame to deal with an administration so that we can plan properly.

Q478 Simon Reeve: Did Sports Direct in any way benefit from the decisions that had to be made as a result of the time scale?

Philip Duffy: I don't believe so.

Q479 Simon Reeve: They had a subsidiary that effectively wrote off a large amount of debt in USC, didn't they? So that was one benefit.

Philip Duffy: If we had planned it, we could have negotiated with suppliers.

Simon Reeve: I am not criticising you.

Philip Duffy: I'm just trying to get to the point. If we'd had time to plan, we could have negotiated with suppliers, traded the business for two or three weeks and realised much more by selling goods at retail value, rather than discounted value. Unfortunately, the British public like a retail business in administration. As soon as it is announced in the press that a retail business has gone into administration, people flock to the stores and buy. They can't help themselves. Sports Direct would have recovered more money if we had traded the business because we would have generated sales at stores. They would have benefited from an immediate return on their secured debt.

Q480 Simon Reevell: But that's in the short term. In the longer term, there is a company that is still trading, as I understand it.

Philip Duffy: Yes.

Q481 Simon Reevell: If you go back to 1 November 2014, Sports Direct had a company that was losing money. It now has the same company, but the debt liability that had been incurred has gone. It is trading in a way that presumably no longer incurs debt liability. That is why Sports Direct wanted to buy it as part of the pre-pack, perhaps because they thought that, if it got rid of its debt, it would be profitable in the medium and long term.

Philip Duffy: Getting rid of debt does not make a company profitable.

Q482 Simon Reevell: It depends on whether it has got to fund the debt, doesn't it?

Philip Duffy: But that is not profit. Profitability is about selling stock at stores.

Q483 Simon Reevell: Well, its net profit is its profit after it has covered its costs.

Philip Duffy: Yes, but it's not cash.

Q484 Simon Reevell: No, it's not cash; cash is a different thing. At one level, to use a technical phrase, this all looks well dodgy. It looks as if a group of executives kept the remainder of the board in the dark to make arrangements to put a company into administration, and they sprung it on the board at the last minute so that the board had to agree. The process went through and the only people who could buy it were a company run by the same people who had known all along that administration was a possibility. And, at the end of it, all that seems to have changed is that they are no longer responsible for quite a large amount of debt. I am just wondering if that is what you think happened.

Philip Duffy: It was my judgment call.

Q485 Simon Reevell: It had to be, didn't it?

Philip Duffy: Because of the financial situation, yes.

Q486 Simon Reevell: Because of the way it was dropped on you, that had to be your call.

Philip Duffy: Yes.

Q487 Simon Reevell: Right. So if I want to engineer the sort of situation that I have just described, I can be pretty confident that you will make the call that you did, because I own

the branding rights, I am the only person in town who is likely to buy the thing and, if you do not make a quick decision, you will have nothing to sell. So there is a pretty good chance that I will be able to buy it off you, because that is the only sensible decision that you can make. Do you think that is what went on here?

Philip Duffy: I do not know whether there has been any engineering of that situation.

Q488 Simon Reeve: You do lots of these things, so how dodgy does this one look?

Philip Duffy: Atradius were not associated. If I had not had Atradius issuing that notice, I would not have sold it as a pre-pack; I would have traded the business.

Q489 Simon Reeve: But because of the way the business was run, that notice was bound to come.

Philip Duffy: That was the first time I had ever seen a notice from Atradius like that.

Q490 Simon Reeve: But a company like that, which is effectively warehousing to sell stock that it doesn't actually own, is bound to be affected by that sort of notice if it is going into administration. The only alternative is that the owner of the stock says, "We'll just ride it out and see what happens."

Philip Duffy: I certainly see how it can be perceived, but I have got no evidence for that. We are carrying out investigations into company directors and we have already had meetings with the Insolvency Service.

Q491 Simon Reeve: Is there anything about it that makes my concern unreasonable? Am I missing something that means that I must be barking up the wrong tree, or is it a case that there is not any evidence, so we don't know?

Philip Duffy: To start off, I have not finished my investigations. I see how it can be perceived that way, but I have not got any evidence that it was engineered that way.

Simon Reeve: I understand that point. Thank you.

Q492 Chair: Following the point of how it was handled, had the USC section of Sports Direct not been a separate company, you would not have had an administration and all the losses would have had to have been borne against the Sports Direct balance sheet. If they then wanted to shut down the warehouse and make people redundant, they would have had to have done that as a normal restructuring of part of the business. But by having that structure there, they were able to pull the plug on the whole of USC and do a pre-pack and so on, so they have ended up shedding a large number of financial responsibilities that otherwise they would have been stuck with.

Philip Duffy: Because it was a separate company.

Chair: Yes.

Philip Duffy: And that is quite common in most large retail businesses: separate brands are in separate companies.

Q493 Chair: Yes, but has it never occurred to you that the points that I have made might well be part of the reason for that? You set them up as separate companies in order that if one part of the empire goes down, it just goes down. Somebody else loses out, but that does not go as a charge against the main company.

Philip Duffy: It is to protect the rest of the business. Yes, I understand that. I thought that they bought this company into the group.

Chair: Yes.

Philip Duffy: So they did not set it up that way; they bought it in.

Q494 Chair: That is right. They bought it into the group, but they had the choice of either keeping it as a separate structure or absorbing it into the mainstream. The fact that they bought it in thinking that they could make a go of it and did not manage it is regrettable, but people make wrong business decisions all the time. It is a question of whether they have been unreasonably protected against the consequences of their error by the structure they chose and the fact that they were able to dump many expenses such as tax on to the taxpayer.

Philip Duffy: In my mind, every company in the country would do it that way. If they are going to buy a company, they would not just buy the business and assets and put it into their own company. They would buy the company separately as a subsidiary, and every financial adviser would advise them to do the same.

Q495 Chair: Absolutely. Financial advisers would advise them to do the same, on the basis that they can limit the loss if it goes down, because they can dump the debt and dump the costs on the taxpayer, and therefore it is a perfectly rational decision for them to make.

Philip Duffy: It is certainly less risky.

Chair: Yes. That doesn't mean to say it's right, but it is a rational decision for them to make within the framework.

Q496 Pamela Nash: We heard earlier that the majority of staff were transferred under TUPE to Republic. That wasn't the case for those staff who were working in the warehouse.

Philip Duffy: That's right.

Q497 Pamela Nash: Can I ask why? Was it considered that they could be transferred to other parts of the business?

Philip Duffy: There was no business at the warehouse. The warehouse had been emptied, so as an administrator, I had nowhere to transfer it to. I had to make them redundant because there was no full ongoing trading to make wages payments.

Q498 Pamela Nash: Is it legally possible that they could have been transferred and offered work elsewhere in Sports Direct?

Philip Duffy: You would have to ask Sports Direct that. I don't know.

Q499 Pamela Nash: Is there any legal barrier to that?

Philip Duffy: I don't believe so, no. I am not an employment law expert, but I don't believe so.

Q500 Pamela Nash: I appreciate that, but that option wasn't given to you as an administrator.

Philip Duffy: Nobody made an offer to me for the warehouse.

Q501 Pamela Nash: No, not that. In terms of staff, could they have been offered alternative work—not even warehouse work? Was there any discussion with you and the company?

Philip Duffy: No.

Q502 Pamela Nash: So the only option that was given to you was to make them redundant.

Philip Duffy: That's correct, yes. There was no trade going on in the shell of USC, so I had no money to pay wages.

Q503 Chair: I understand that, but Sports Direct didn't come along to you and say, "Look, we are transferring this warehouse function to somewhere else. There'll be some jobs created there and we can take some of these people. They may not want to transfer to Nottingham or Mansfield, or they might not want to transfer to stores elsewhere in Scotland," but you were never given that as a possibility.

Philip Duffy: That's correct.

Q504 Mr McKenzie: I have two questions on creditors, beginning with the non-preferential unsecured creditors. How much can they expect to get back?

Philip Duffy: It's early to say. We estimate that about £200,000 will be distributed among unsecured creditors. Our first estimate of unsecured creditors is £15 million,

but that will reduce, because a lot of those creditors are suppliers and they will have retention of title claims, and Republic, the subsidiary of Sports Direct that has bought the business and assets, will have to settle those retention of title claims.

Q505 Mr McKenzie: How many of those creditors are there, and can you name them at all?

Philip Duffy: The suppliers?

Mr McKenzie: Yes.

Philip Duffy: I think there are about 11 million, but I have a list of creditors here, which is in public—it is in the report, which is a public document.

The largest suppliers are suppliers of product—*[Interruption.]*

Mr McKenzie: I think we may have them.

Philip Duffy: It's in the report. You have that already.

Q506 Mr McKenzie: On average, they will receive what?

Philip Duffy: It is too early to say. The total claim is about £15 million, but that will reduce because Republic will have to settle retention of title claims. So Republic will have to pay for stock that is in the stores that we only sold the right to title and interest—we did not sell the stock subject to retention of title. They will settle with the supplier of that stock. So £15 million might well come down to £7.5 million.

Q507 Chair: Which is coming back to the point—am I correct?—that you mentioned earlier on about single pennies in the pound.

Philip Duffy: Yes. So it is still 3p or 4p in the pound.

Q508 Chair: I think that covers everything. Now, perhaps more than with the previous witness, because we had so long with him, are there any answers you had prepared to questions that we have not asked? Are there any things you think we should be pursuing with you that would be helpful for us to know and that we haven't touched on?

Philip Duffy: Just to clarify a point made in the previous session about the supply of goods—there was some confusion over the supply of goods into USC and Sports Direct. USC used to buy goods from branded suppliers, so they would incur the liability, but they would then sell it to Sports Direct. Sports Direct would hold it across the group, and they may put those goods in various other businesses. When stock came back from the warehouse into stores, Sports Direct would then sell stock back to USC. There was confusion earlier over the—

Q509 Simon Reeve: So people who did not want to sell to Sports Direct but who would sell to USC—the stock actually went to Sports Direct anyway, but might come back to USC.

Philip Duffy: Yes, and where Sports Direct used it, I don't know.

Q510 Simon Reeve: So the question of who was withholding money—

Philip Duffy: It was still USC.

Q511 Simon Reeve: It was USC, but in conjunction with Sports Direct because that was the conduit.

Philip Duffy: It was the funder.

Q512 Chair: Can I clarify whether there is a potential issue of transfer pricing here—that USC could quite easily be bankrupted by the prices at which Sports Direct charged them for the goods as they went back and forward?

Philip Duffy: I don't believe so because I think they were transferred in and out at the same price.

Chair: Fine. That is very helpful.

Philip Duffy: I've not seen any evidence of that, so I think it was—that was the case.

Q513 Chair: You can understand why we ask. We have heard so many interesting things today that almost anything is possible. Are there any final points that you want to raise with us?

Philip Duffy: No.

Chair: Thank you very much for coming along. This has been very helpful, and we found the papers that you gave us very helpful as well. I apologise again for the delay in calling you in. I hope that has not been too inconvenient for you. Thank you very much.