

Business, Energy and Industrial Strategy and Work and Pensions Committees

Oral evidence: Carillion, HC 769

Tuesday 6 February 2017

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Members present: Rachel Reeves (Chair); Heidi Allen; Andrew Bowie; Frank Field; Ruth George; Stephen Kerr; Peter Kyle; Rachel Maclean; Antoinette Sandbach; Chris Stephens.

Questions 218 - 649

Witnesses

I: Zafar Khan, former Finance Director, Carillion; Keith Cochrane, Interim Chief Executive, Carillion; Emma Mercer, Finance Director, Carillion.

II: Richard Howson, former Chief Executive, Carillion, Philip Green CBE, Chairman, Carillion, Richard Adam, former Finance Director, Carillion, and Alison Horner, Chair of Remuneration Committee, Carillion

Examination of witnesses

Witnesses: Zafar Khan, Keith Cochrane and Emma Mercer.

Chair: Thank you very much for coming to give evidence to our Select Committees this morning about what happened to Carillion. We have a number of questions, and we have two evidence sessions this morning, from you and then from some of your colleagues, so we will get started straightaway. Antionette Sandbach will ask the first question.

Q218 **Antoinette Sandbach:** Carillion's 2016 annual report was published in March 2017, and it gave a very optimistic outlook. Just two months later, Carillion revealed that it was making an £845 million provision against contracts. Are you surprised, based on what you found when you assumed your roles on the board, or as the chief executive and the chief financial officer particularly?

Keith Cochrane: Perhaps I could start in answering that question. First of all, can I say how devastating the failure of Carillion has been for employees, for customers, for pensioners and for suppliers. I am truly sorry for the impact. It was the worst possible outcome. This was a business worth fighting for, and that is certainly what I sought to do during my time as chief executive.

To your question, you are correct: I was a non-executive director for two years prior to taking over as chief executive. As we look back at the 2016 annual accounts, there were a number of references to the opportunities that the business had and the very strong pipeline. At the same time, we did highlight some of the challenging markets, particularly internationally, which the business was looking at, and we did highlight very clearly a desire, which was driven by a number of board discussions, to bring down average net debt as a critical factor in the coming year, in 2017.

Q219 **Antoinette Sandbach:** You are claiming, as a whole, that the report filed in March 2017 flagged sufficient concerns. My question was around the £845 million provision thereafter. When had KPMG been asked to do the review of critical contracts?

Keith Cochrane: The critical contracts review was kicked off around the end of May, and was driven largely by a deterioration in cash flows on a number of major contracts, which occurred particularly as we went through Q2, in the second quarter of this year. As I said, we were aware of a number of challenging contracts. We were certainly not aware of the quantum that subsequently required to be provisioned against, but, if I may, it is also helpful to understand the context of that £845 million provision.

Q220 **Antoinette Sandbach:** What would you say to the suggestion that that review had actually begun earlier? We have had evidence that that had



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begun by around December 2016?

Keith Cochrane: I am not aware of that review. All contracts are looked at as part of the annual audit process. I was a non-executive at that time, so others may be able to give their own perspectives, but the board commissioned that review, essentially, at the end of May, recognising some of the concerns that the board had at that juncture over contract performance, over the direction of travel of the cash flow, and indeed around net debt.

Q221 **Antoinette Sandbach:** Mr Khan, what role did you have in the run-up to the preparation of the accounts, prior to taking up your role as CFO?

Zafar Khan: Prior to taking up the role of the CFO, I was the group financial controller, and in that role I would have supported the then group finance director in terms of the ongoing financial reporting within the group.

Q222 **Antoinette Sandbach:** Were you aware of the concerns flagged by the FRC in relation to the accounts in 2015, and the auditing of the accounts then?

Zafar Khan: Yes, I was, and we dealt with all of the points that the FRC had raised on the 2015 accounts, as part of our preparation, and they were substantively addressed in the 2016 annual report.

Q223 **Antoinette Sandbach:** Did any of the matters raised by the FRC raise questions with you that indicated that you might need to look a little deeper into some of the issues in the company?

Zafar Khan: No, there were not. The bulk of the points arising out of the FRC review essentially related to disclosure points within the 2015 financial statements, and there were some points around further disclosure in trends, judgments and estimates applied in arriving at revenue recognition, and also minor disclosure improvements elsewhere in the annual report. All of those, as I say, were fully addressed in the 2016 annual report.

Q224 **Antoinette Sandbach:** Did you have any disagreements with the auditors at all, in terms of the sign-off of the accounts that were lodged in March 2017?

Zafar Khan: No, we did not have any disagreements with the auditors. As always, the audit focused on key risks, estimates, and judgments applied, and, generally speaking, our policy always was to ensure that to the extent that there was disagreement, we addressed those disagreements prior to finalising the numbers.

Q225 **Antoinette Sandbach:** The report suggests that Carillion's order books were so complex that the Government had to use an outside organisation to consolidate and understand them. Was that your experience of Carillion's order books?



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Zafar Khan: No, that is not my experience. I did not think that the order book was particularly complex.

Q226 **Antoinette Sandbach:** What is your view of the evidence of the Insolvency Service, which told us of an incredibly poor standard of the company's own record-keeping?

Zafar Khan: I have been out of the company since September, and I am not aware.

Q227 **Antoinette Sandbach:** Mr Khan, you worked for the company for nine years, did you not?

Zafar Khan: It was actually six years, but in the time that I was with company, I had no issues around record-keeping within the business.

Q228 **Antoinette Sandbach:** So the records were in a good state, where you could instantly identify where the risks were to your cash flow, where the risks were on your debt rating, and where the risks were on your increasing debt in your pension fund.

Zafar Khan: That would be my view. If you look at the 2016 annual report, and if you look at the key risks identified within that, my view is that the setbacks and issues that we experienced in 2017 were largely related to the risks that we had set out in the 2016 annual report. What was not anticipated at the time was the number of risks that crystallised in the end, and also the quantum of the impact that we had to deal with. Some of that was around market conditions, and some of that was, again, deteriorating contract performance.

Q229 **Antoinette Sandbach:** Mr Cochrane, were you aware that a significant investor in Carillion had raised concerns with the Carillion chief executive and chairman in relation to weak cash generation due to working capital outflows, restructuring costs, pension contributions and capital expenditure needs as far back as 2014?

Keith Cochrane: No, I was not aware. Obviously, I joined the board in July 2015, but, as I said in a reply to an earlier question, the board was very focused on working capital management.

Q230 **Antoinette Sandbach:** When in 2015 did you join the board?

Keith Cochrane: July.

Q231 **Antoinette Sandbach:** There were meetings in September 2015 and December 2015 to discuss management and corporate government arrangements. Were you made aware by the CEO and the chairman of those meetings with then, at that time, one of the major investors in Carillion, holding a greater than 10% share?

Keith Cochrane: I cannot recall the specific details of those meetings. Having said that, the board was updated on investor meetings more generally, in terms of the general feedback coming out of meetings and concerns that were being expressed by shareholders.



Q232 **Antoinette Sandbach:** What were those concerns?

Keith Cochrane: Essentially, the concerns were around the net debt position. That was obviously a growing concern. There were concerns around the pension deficit and the treatment of the pension deficit.

Q233 **Antoinette Sandbach:** We are talking about 2015 here, are we?

Keith Cochrane: We are growing into 2016. From memory, these were lesser concerns in 2015, but certainly as we went through 2016, we recognised the importance of addressing these issues, and, very much as a board, tasked management with coming up with a plan as to how they would address these concerns. The appointment of a new finance director at the start of 2017 enabled us to look afresh at how we disclosed and how we articulated our position to our investors.

Q234 **Antoinette Sandbach:** Following on from the £845 million provision, did any major investors in Carillion argue that that disclosure should have been made earlier?

Keith Cochrane: I think I only met two or three investors post 10 July. There was obviously a lot of concern around the provision. There was a lot of desire to understand what had given rise to it, rightly. It had crystallised over a fairly short period of time. Of course, part of that provision—and this is a very important point to make—was an explicit recognition of the group seeking to exit from certain key markets, and, as it sought to exit from certain key markets and start to refocus itself on its core, that required us to take a different perspective on our ability to collect outstanding receivables in those markets.

Once one has gone public, in terms of saying you are going to exit a particular market, inevitably it becomes more challenging to collect cash in those markets from particular customers when they know your leverage is somewhat more limited. That accounted for just over £400 million of the £845 million provision, essentially linked to our businesses in Canada and the Middle East.

Q235 **Antoinette Sandbach:** Were there indications prior to July 2017—indeed, prior to May 2017—that you may have difficulty collecting cash?

Keith Cochrane: Collecting cash was a topic that came up at every board meeting. The board was aware of specific challenges around particular contract positions.

Q236 **Antoinette Sandbach:** At what point?

Keith Cochrane: It was ongoing. If one were to look at the board minutes, you would see that there was ongoing discussion about some of the nature of what I would describe as more of the qualitative challenges. The board also received a quarterly financial update on the position on each of those contracts.

Q237 **Antoinette Sandbach:** Going how far back?



Keith Cochrane: I can only go back as far as myself joining the board, but certainly every quarter. Of course, that was then validated at the full year and the half year through the work of our external auditors, and we also were fortunate to have Deloitte undertaking our internal audit function. They were out across the business, looking at individual contract positions as well.

Q238 **Antoinette Sandbach:** Do you think if there had been earlier engagement with investors, to recognise problems that were present at Carillion, we may not be in the position that we are in, sitting here today?

Keith Cochrane: I do not believe that that was a critical factor in the timeline of where we have got to today. As I said, the board did acknowledge the issues. It sought to address them. Indeed, we sought to move forward with a capital-finance-raising in June 2017 to resolve these issues, but ultimately were unsuccessful in being able to achieve that.

Q239 **Antoinette Sandbach:** What was your state of knowledge of the overrun, or the requirement to write down millions and millions of pounds, when you tried to issue that capital or go out to the market for that capital issue in June 2017?

Keith Cochrane: One of the reasons that the capital-raising did not go ahead was the advice from our brokers about the scale of the contract provision, the investor proposition that we would be able to articulate off the back of that and the nature of our share register.

Q240 **Antoinette Sandbach:** So you knew in June. When in June did you know the scale of your write-down?

Keith Cochrane: The first time I heard of the size of the number was at the end of June. The first time I saw the papers was the weekend before I was appointed. That was when I had the detail, because prior to that, it had been work in progress. Indeed, as the board minutes will show, I increased the provision through my own review that weekend, as I was appointed chief executive. I felt we needed to take further provisions, because if we were going to take a provision, it was all about materially de-risking the position.

Q241 **Antoinette Sandbach:** Can I ask about materially de-risking? I want to give a quote to you, and I would like to ask you to comment on it: "It was felt that management was not giving sufficient weight to the probability that trading may deteriorate further, or to the downside risk of this scenario, given the high level of debt. The board showed no inclination to drive the management change". This was from a major Carillion shareholder that substantially divested itself of Carillion shares during 2015-16. Do you recognise that comment, and do you accept it?

Keith Cochrane: No. From my perspective, I do not accept it, because the board was actively engaged both in testing and challenging management's assumptions.



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Q242 **Antoinette Sandbach:** That is clearly not right, is it, if you look at the subsequent write-down?

Keith Cochrane: With the benefit of hindsight, should the board have been asking further, more probing questions? Perhaps. From our perspective, against the backcloth of the management environment and the information that we received, and the testing and challenging of management, we believed that there was no basis at that time for not accepting the view that management put forward.

Q243 **Frank Field:** In your first weekend, you changed the advice and made the write-down bigger. To Antoinette's question, why was that grip not shown elsewhere in your leadership?

Keith Cochrane: From my perspective—and I can only speak from my own perspective here—I was a non-executive director, and the role of non-executive director is very different from the role of chief executive, as I am sure the Committee appreciate.

Q244 **Frank Field:** Your previous role was to challenge.

Keith Cochrane: It was to challenge, and indeed I sought to challenge in an appropriate manner against the backcloth of receiving perspectives from a number of different sources as to the control environment across the business, be that the external auditors, the internal auditors, or exposure to leadership across the business. Indeed, the two senior divisional MDs were attending every board meeting, so again they were giving us a direct perspective.

Q245 **Frank Field:** You failed, then, in your challenging role. How much did you get for your challenging role, please?

Keith Cochrane: £60,000 a year.

Q246 **Chair:** Can I just follow up, Mr Cochrane, on a couple of your answers to Antoinette Sandbach's questions? In May 2017, KPMG were asked to look at your contracts, and that is when you say that you found that there were problems with your cash flows. Were there no problems with your cash flows before May 2017?

Keith Cochrane: There were growing problems with our cash flows through that period. There were two specific exercises undertaken. An internal reporting issue came to the board's attention.

Q247 **Chair:** When was that?

Keith Cochrane: The beginning of May 2017.

Q248 **Chair:** What was that problem that was brought to your attention?

Keith Cochrane: Essentially, what was flagged to us was that it looked as if there had been some netting-off between receivables and payables. Rather than the gross values being stated on our balance sheet, they had been reversed, so they would reduce the value of receivables and reduce



the value of payables. It was essentially a presentational issue. Once the board became aware of it, it commissioned an independent review. It invited KPMG to look at it, because our concern at that point was to ensure that our year-end financial statements remained appropriate, and that exercise took place over the course of May. The executive team will be able to give you more details around that.

Q249 **Chair:** Only two months previously, you had published your annual report, and two months later, you are saying that there were some ways in which it was presented that were not accurate or not the right way to do it.

Keith Cochrane: To be clear, the presentation was very much in the internal reporting. The reporting as stated in our annual reports was confirmed as being in compliance with accounting standards, but naturally, when one is made aware of an issue such as this, you want to follow through on it and investigate it. The end result was that it re-confirmed our year-end position, but on the back of that, together with the cash flow deteriorations that we saw, we believed it appropriate to essentially move from a look-back perspective to a look-forward perspective, and commission KPMG to do a more detailed review of the largest contracts across the business at that juncture.

Q250 **Chair:** Do you stand by the idea that the cash flows deteriorated between March and May, and that when you published your annual report in March 2017, at that point there were no deteriorations in the cash flow that you should have put in your annual report?

Keith Cochrane: Clearly, when one signs off an annual report, and indeed gives guidance to the market—and the guidance is both in terms of the profits that, as a business, you are going to expect to generate in 2017, and in terms of the direction of travel of net debt—the board receives an updated forecast from management. It tested and it challenged that forecast.

Q251 **Chair:** Before March 2017, there had been no deterioration in the cash flow. It all happened after March 2017. That is the question I am asking, Mr Cochrane.

Keith Cochrane: Let us be very clear: net debt at the end of 2016 was too high. The board tasked management with developing a plan to drive a reduction in net debt. Again, in the investor presentation, in the announcements that we put out at the beginning of March, management indicated at that juncture that we would be targeting a reduction in average net debt, albeit second-half-loaded. That was on the back of management presenting to the board a credible self-help plan.

Q252 **Chair:** I am sorry to keep asking the same question, but it is because I do not feel that I have had an answer to it. There is a difference between debt issues and liquidity issues, and I am asking about the cash flow, because that is what you said that you were worried about in May: there had been a deterioration in the cash flows. What I am asking is whether



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there had been any problems with cash flow before March 2017.

Keith Cochrane: I will need to think for a second. If I recall, trending was broadly in line with the budgeted position for the first couple of months of the year, but that is just a recollection. I would need to check the papers specifically, Chair, on that question.

Q253 **Chair:** Okay, if you could get back to me on that. Finally, in answer to Antionette Sandbach's questions, you said that you met with two or three investors after July 2017 to explain what was happening in the business, and how you were focusing on the core business, et cetera. What two or three investors did you speak to, and what did they do in terms of their shareholdings with Carillion in the months after those conversation?

Keith Cochrane: I spoke to Kiltearn, which was a major shareholder, and I spoke to a substantial shareholder, which I have forgotten the name of, based in Quebec, in Canada.

Q254 **Chair:** You spoke to Kiltearn after July 2017. What happened to their shareholdings with Carillion after your conversation?

Keith Cochrane: There was no change to their holding at that point.

Q255 **Chair:** What was the change in their holdings between July 2017 and the end of the year?

Keith Cochrane: If I recall, towards the end of the year, they started to sell down their position, but for the several months after the July warning, there was no change—from memory—to their shareholding. Again, I would just need to reconfirm that, but that is my recollection.

Q256 **Frank Field:** What did the company that you cannot remember the name of do?

Keith Cochrane: They did the same. They held on to their position.

Q257 **Frank Field:** You are presenting us with a picture, are you not, that somehow the public face you presented was pretty or hunky-dory, and then within a couple of months you began to drive the company into the ground? Is that the image you meant to put over to us?

Keith Cochrane: I am trying to present a balanced image as I saw it. I have also articulated, since I became chief executive, that the business faced a number of challenges. Let us be very clear: the business got itself into this position.

Q258 **Frank Field:** The business did not. It does not have an identity. The directors did.

Keith Cochrane: The company: the directors, the board, the management, the collective.

Q259 **Frank Field:** It is like these lads say: "I did not stab that person with a knife; it was the beer". You were in charge. You were taking money. The company had no personality on its own that could have done this.



Keith Cochrane: From my perspective as a non-executive director during this period of time, the role of the board was to challenge on the basis of information that was provided to it from management. That is what we sought to do. Clearly, with hindsight—and I recognise that a lot has happened—it is a question I ask myself. There was a lot of challenge that I believe I provided, but should I have challenged more? Again, back to the context, the environment and the backcloth of what I saw, what I heard and what was presented to me, we sought to challenge. Clearly, the business did have issues, undoubtedly. Do I wish we had done something about it sooner? Absolutely. I recognise that, again, with the benefit of hindsight, but I can assure you that, at the time, all of the decisions I took were very much seeking to do the best thing for the business at that juncture.

Q260 **Frank Field:** You had a challenge, and you were not up to it. Is that not right, really?

Keith Cochrane: I would not agree with that comment. I believe I challenged appropriately as a non-executive director on the basis of the information that was provided to me by management.

Frank Field: Then we have a crash, yes.

Q261 **Chair:** Mr Cochrane, you met with Kiltarn some time after you took over in July 2017. By the end of the year, their share in Carillion fell from more than 10% to less than 5%, and by the beginning of January, they had divested of Carillion stock completely. Is that correct?

Keith Cochrane: Yes, that is my broad recollection.

Chair: It would be good to know—and perhaps you could give us this in writing—which other investors you spoke to and what impact your reassurances had on them.

Q262 **Rachel Maclean:** Emma Mercer, you were the CFO for the four months prior to the collapse. Is that correct?

Emma Mercer: Yes.

Q263 **Rachel Maclean:** When you came into the company, did you think that Carillion was pursuing an aggressive accounting approach to recognising revenue?

Emma Mercer: I have worked for Carillion for some time, but I spent four years leading to March 2017 in the Canadian business, returning to the UK in April 2017.

Q264 **Rachel Maclean:** How long were you in the Canadian business?

Emma Mercer: For just over three years.¹ I returned to the UK in the construction division, and spent a very short time in there before taking

¹ Ms Mercer subsequently clarified for the Committees that she worked in the Canadian business for three and a half years but was outside of the UK for four years factoring in



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up the CFO role. When I returned back to the UK in April 2017, what I saw at that point was a slightly more aggressive trading of the contracts than I had previously experienced in the UK before I left.

Q265 **Rachel Maclean:** In another company?

Emma Mercer: No, in Carillion before I left the UK. I would not say that I necessarily disagreed with many of the individual contract positions, because all sorts of judgments have to be made, but the overall tone had become a little bit more aggressive than when I left the UK previously.

Q266 **Rachel Maclean:** You were the CFO. Was that down to your judgment?

Emma Mercer: No. This is when I returned to the UK in April 2017. I was part of the construction division during that time.

Q267 **Rachel Maclean:** Somebody else had been adopting this slightly more aggressive tone.

Emma Mercer: Yes.

Q268 **Rachel Maclean:** Who was that?

Emma Mercer: From a divisional perspective, my predecessor in the construction business, and then as a management team, the management team before that, so Zafar Khan as CFO, and Richard before that. During that time, we looked at a lot of contracts, and I would not disagree with the position that we traded the financial statements of 2016, but they had become more aggressive than in previous years.

During 2017, in the construction business itself, I contributed to supporting the contracts review that we did during that time. By the time that I took up the post in September, the clear focus of that was that we had done the contracts review across the construction business. As part of Keith's strategic review, we had changed the way that we were looking at some of the services contracts, and that resulted in an increased position at the end of September, in terms of an additional £200 million of provision. Our key focus, as we went through September right up until the last part of the business, was driving to get a successful restructure for this business.

Q269 **Rachel Maclean:** You are saying that you inherited this practice of aggressive accounting from your predecessor Zafar Khan and other predecessors, and you came in and started to look at that with a fresh approach. Is that what you are saying?

Emma Mercer: I am not saying that I disagree necessarily with the positions that they took. What I am saying is that they were more aggressive in tone than what I had seen in the UK previously.

Q270 **Rachel Maclean:** Can you explain how?



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Emma Mercer: Then, during my tenure in the construction division, from April through to when I took up the post of CFO, we did see some really significant deteriorations across some significant contracts in that business, some of which have been cited publicly. We had some significant operational difficulties on those contracts, and as part of that, we had to generate the provisions that we did during July, and then more latterly increased those in September.

Q271 **Rachel Maclean:** I understand that, but obviously accounting does require professional judgment and the use of assumptions.

Emma Mercer: It does, yes.

Q272 **Rachel Maclean:** That ultimately does come down to subjectivity to some degree, and that is led by the person ultimately responsible for that, because they can say that they did not agree with that assumption or not. Can you explain to the people who are not accountants, in your view, what exactly the difference was between the aggressive tone that you saw and what you saw before?

Emma Mercer: Having a number of construction projects means that you have to exercise judgment over all sorts of things: when the contract is going to get finished; how much we are going to receive; if we are claiming against anybody; what entitlement we may have. What I saw when I returned to the UK is that both the number of contracts we were taking judgment on and the size of those judgments had increased. What that meant is that when we saw the deterioration in the first part of 2017 and into the second—when we saw those huge deteriorations on those contracts—because we were already at a more aggressive position, it was very difficult to withstand those deteriorations on those projects.

Q273 **Rachel Maclean:** Zafar Khan, do you agree that this was the start of a slippery slope under your tenure, where legitimate earnings management could have descended into earnings manipulation?

Zafar Khan: I do not believe that there were any instances of earnings manipulation. I signed off the 2016 annual report. The numbers within that were audited by KPMG, and in terms of how we have managed the business, we have a whole range of contracts. You have contracts in Canada; you have contracts in the Middle East; you have contracts in the UK. You have finance directors, managing directors and commercial directors in each of those businesses, who take into account all of the available information at that point in time, and come to a judgment.

As a central management team, you would not necessarily be looking to second-guess a lot of the judgments that are taken on contracts. I do not agree that there was a concerted effort to adopt aggressive accounting as such. To my mind, the numbers that were reported in March 2016 were appropriate, based on the information that was available at that point in time.

Q274 **Rachel Maclean:** Your judgment is different from your colleague Emma



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Mercer.

Zafar Khan: Emma has a long history with the group. I had not spent time in the UK construction division previously and then spent more time in it to make a comment on whether it was better or worse than before. I did not have that sort of perspective, but, to my mind, the group had appropriate structures, processes, and policies in place to make sure. If you look at the business as a whole, it does depend on every single contract, on judgments and estimates. Whether it is a services contract or a construction contract, you are dependent on the team on that contract to come to a view on what the position is at a particular point in time.

Q275 **Rachel Maclean:** Mr Khan, if you had come to a different view—shall we call it a more conservative view?—maybe something more like Emma Mercer, what would have been the impact on the investors, in terms of the earnings that you could show?

Zafar Khan: I am not sure what different view you would have taken in March 2016 if you had had somebody else in that position. We are second-guessing what an alternative approach might have been.

Q276 **Rachel Maclean:** Are you saying that it would not have been possible to take a more prudent or conservative view at that time? It is judgment.

Zafar Khan: It is judgment. At the end of the day, it is judgment, and you are dependent on the professionals and experts and people running those business units to come to a conclusion on those. There was no effort in the time that I was in the business, in any part of it, to push people to come up with a more aggressive position.

Q277 **Rachel Maclean:** Did you inform the Government of the company's weaknesses at this point? At what point did you inform the Government of the company's weaknesses?

Zafar Khan: Which weaknesses?

Q278 **Rachel Maclean:** The weaknesses that we have seen: the profit warnings and the write-downs.

Zafar Khan: Of course, we had regular dialogue with the Cabinet Office through our crown rep, essentially, and as part of that, we would cover a whole range of issues. The last session I was sat in covered governance, audit arrangements, cash flow performance and the pension deficit; it was a very broad agenda in terms of the topics that were of interest to our crown rep.

Again, I think we were always open in terms of where the business was, where it was headed, and anything of interest to the Government. Clearly, the Government were a key customer for the business, and we were keen to make sure that we had an open and honest approach, and that the Government understood what our key issues and concerns were.



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Just going back, in terms of Keith's comments on the cash flow deterioration, as we sit here, it does look odd that things can deteriorate so dramatically over a short period of time. We need to bear in mind that, by and large, Carillion had some quite large contracts that we were working with, and cash flows on those can change over a short period of time. I picked up the role of the finance director, effective 1 January 2017. We had a budget, and the process that we adopted to arrive at that budget was no different to the one we had adopted in the past. It was no more challenging than we had come to expect.

Q279 Frank Field: Did you not think that you should have protections in place so that we did not have this terrible collapse? You are telling us this as though it came down Mount Sinai: "It hit us all and we are absolutely surprised. We walked away from the wreckage". It is your job, surely, to have in place procedures that prevent this outcome.

Zafar Khan: In terms of the controls, processes and risk management disciplines, the business has operated with everything you would expect to see within it, essentially. With the cash flow issues that we experienced in 2017, there were a number of factors. We were forecasting some reasonably material receipts from the Middle East that continued to be promised on a monthly basis but never arrived.

Another factor that I do not think has been given enough attention is that, going into 2017, we had a number of large-ish contracts in our UK construction business that were coming towards completion. For a contractor, it is very important in terms of cash flow that you replace the volumes that are coming off. If you see a contraction in volumes, that is bad news for cash flow. In the UK business, we had a number of contracts that were essentially coming towards completion, and our working assumption was that we would replace those volumes. We had a good pipeline of opportunities to do that, with contracts where we had signed up as preferred bidders.

Q280 Heidi Allen: Could I just interject on that? You need volume if your margins are so tight that you are not going to earn money. If you have reasonable margins and have costed them properly, then you do not need to be so desperate and hungry for new business. That is what I would suggest. Did you look at the margins of these companies?

Zafar Khan: We did, absolutely. I do not think we are talking about volumes for the sake of volumes.

Q281 Heidi Allen: But it was volumes, though, was it not? It seems to me, at least, that Carillion was taking on excessive numbers of contracts purely as a means to keep the cash flow going. These were not profitable pieces of business; they were just there to milk a cash cow.

Zafar Khan: I cannot comment.

Heidi Allen: You were the financial controller.



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Zafar Khan: I am not aware of any contracts having been taken on purely for the volume historically. That is the position.

Q282 **Frank Field:** But you were aware, were you not, that this was a house of cards that could fall down at any moment? That is really Heidi's point. There was no real fall-back position. If you just failed somehow to get these contracts, the whole thing came down.

Zafar Khan: We had challenges in 2017 with the number of things coming together at the same time, and not replacing those volumes. Coming into the year, as I say, we had some contracts that we were preferred bidders for, but they continued to drift out to the right because of the Brexit-related uncertainty. That was amplified by the general election announcement, and that had an impact on our ability to replace the contracts that were coming off.

Q283 **Chair:** Zafar Khan, Emma Mercer said that whilst she was in Canada, accountancy practices became more aggressive. Carillion declared revenue and profit based on forecasts—based, perhaps, on optimistic forecasts. Whilst Emma Mercer was in Canada, who made those changes to the accountancy practices, to make them more aggressive?

Zafar Khan: As I said, I do not believe that there were any changes made to adopt a different stance to those forecasts.

Q284 **Chair:** So Emma Mercer is wrong to say that it became more aggressive in her absence, is she, Zafar Khan?

Zafar Khan: As I said, Emma was commenting on her experience of the UK construction business prior to her going to Canada, versus coming back and going into that business. I am not aware of any change in policy.

Q285 **Frank Field:** You said to Rachel that it was not excessively aggressive, so you accept that your accountancy procedure was aggressive. They were your words. They are on the record: "I refute that we were excessively aggressive", in a reply to Rachel. It was just aggressive.

Zafar Khan: I do not believe that we were aggressive. With the way the numbers are put together in our business, in terms of coming up with the forecast, you are essentially dependent on the professionals and experts making judgments on those contracts.

Q286 **Antoinette Sandbach:** Mr Khan, can I ask how you balanced your duties under Section 172 of the Companies Act, which requires the board to take decisions in the long term, to take into account the interest of the company's employees, the need to foster the company's business relations with suppliers, customers and others, and the need to act fairly—in other words, to act in the interests of shareholders and creditors of the company, which included the pension fund? Can you explain how, if this was not aggressive accounting, the board balanced those obligations?



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Zafar Khan: In my time on the board, I believe that the board was mindful of taking into account the interests of all stakeholders, in terms of the way that the business was run.

Q287 **Antoinette Sandbach:** Demonstrate that. Where do we see that?

Zafar Khan: The way you run the business is to make sure that you understand the key risks around the business, and you are putting in place plans to address those. As Mr Cochrane said earlier, coming into 2017, the key issue that we were looking to address was the net debt position. The net debt, when I came into the role, was thought to be at a level that was undesirably high. We made a public commitment to look at reducing our net debt. Getting net debt down is clearly good news for the pension fund, because it means that it has a better covenant.

Frank Field: Only if it works.

Zafar Khan: These were public commitments that were set out in our 2016 annual report, and I talked about these at length in the investor presentation back in March.

Q288 **Chair:** Mr Cochrane, in an answer to an earlier question, said that he wished that he taken action sooner, and that mistakes had been made. Zafar Khan, do you wish you had taken different decisions, or taken them sooner, and if so, what?

Zafar Khan: As I say, I picked up the Finance Director's role at the beginning of 2017.

Q289 **Chair:** Yes, but you have worked for the company for six years, Mr Khan. You were there in a crucial position at a crucial time for the business. Just answer the question, Mr Khan. Do you wish you had done things sooner, and do you wish you had done things differently? If yes, what?

Zafar Khan: To my mind, one of the issues that contributed to where we ended up was the fact that our debt had grown over the past few years, essentially. That, combined with the number of challenges that we faced in terms of four large contracts underperforming significantly, in terms of the market generally for support services having become very difficult, and the construction market in the UK being difficult, meant—

Q290 **Frank Field:** As you have not answered Rachel's question, can I just ask one? Were you surprised, therefore, that the whole thing crashed? Rachel says, "Would you have done something different?" You cannot answer that question. Were you surprised?

Zafar Khan: Yes, I was surprised. I was surprised at the outcome that eventually came to pass.

Q291 **Chair:** Do you feel perhaps, Mr Khan, that you were asleep at the wheel? You were surprised; you would not have done anything different.



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Zafar Khan: No, I do not believe I was asleep at the wheel. As soon as I came into the role, we were looking to tackle the issues, and the key focus of my time in the role was to bring net debt down.

Q292 **Chair:** You feel, then, in the nine months that you were in the business, that you did the right things at the right time.

Zafar Khan: I believe I did everything that I could have done, essentially. Debt was high; we said at the outset that we would look to reduce that. In the context of that, there was a lengthy debate around the dividend in January and February, before that was passed.

Chair: We will come on to that shortly. Four months after you left, the company went into liquidation, with just £29 million left, leaving thousands of people potentially without jobs and thousands of people saving for their pensions without the pensions that they had expected, but you did everything right at the right time. Well done, Mr Khan.

Q293 **Stephen Kerr:** Mr Khan, just remind us: what was your role before you became CFO?

Zafar Khan: I was the financial controller.

Q294 **Stephen Kerr:** You were the financial controller for the entire business?

Zafar Khan: Yes, for around three years.

Q295 **Stephen Kerr:** So what you discovered when you became CFO could not have come as a surprise to you. It was not like you turned the page and discovered something that you did not already know.

Zafar Khan: No. We spelled out the issues that I felt needed to be addressed.

Q296 **Stephen Kerr:** But you knew of those issues long before you became CFO.

Zafar Khan: The net debt position had built up over a period of time. The markets we were operating in were difficult, and were gradually getting more difficult.

Q297 **Stephen Kerr:** Soon after you joined the board, there was a full review of contracts. Was that instigated by you?

Zafar Khan: With support from the board, yes.

Q298 **Stephen Kerr:** Why did you choose to do that?

Zafar Khan: Why did we choose to do that? Coming into the role, we felt that the key issues were that some of our overseas markets had gradually got difficult, such as the construction market in Canada, and in the Middle East. We were looking to review how much longer we wanted to continue to play in those markets. As we went through the year, we saw deterioration in cash flows on a number of significant contracts in the



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UK. Putting those together, it made sense to have a broader look at the contract positions across the group.

Q299 **Stephen Kerr:** The three specific UK deals that got into difficulty were the Royal Liverpool University Hospital, Midland Metropolitan Hospital, and the Aberdeen bypass, correct?

Zafar Khan: Yes.

Q300 **Stephen Kerr:** Should this review of contracts not have happened much earlier, and been thorough, to the point that this did not just sideswipe you? It is coming across as this suddenly arose as an issue, but these projects had been going on for some time.

Zafar Khan: The projects had been going on for some time. Part of the problem with construction contracts is that you do not always have complete visibility or certainty in terms of where things may land.

Q301 **Stephen Kerr:** What does that tell you, and us, about controls within the organisation, in terms of managing these very expensive contracts?

Zafar Khan: Again, the view is that the business had the right structures and processes in place.

Q302 **Stephen Kerr:** It had the right structures and processes, but could not foresee that these longer-term contracts were suddenly going to effectively capsize the business.

Zafar Khan: We did not.

Q303 **Stephen Kerr:** Does that not reflect something on the controls within the business?

Zafar Khan: Again, we had controls, good processes and structures in terms of people on projects, in terms of those fitting into the divisions and in terms of regular review of those. You do get contracts going on, and it is not always possible to predict everything at a particular point in time.

Q304 **Stephen Kerr:** You have this book of contracts with wafer-thin margins and not a lot of room for error. Notoriously, in construction, things take longer and cost more. Everybody who has ever done anything in their own home knows that. You are working on wafer-thin margins. Tell me what happens after July 2017, then, because you gather in some more contracts—not enough, according to what you said earlier. Is there something different about the way you assess the viability of the contracts after July 2017?

Zafar Khan: We had addressed the lessons learned from the contracts review, and, on the back of that, the conclusions were that we exited the construction markets overseas, and we were exiting the PPP market.

Q305 **Stephen Kerr:** Were there any lessons in relation to the control of the projects?



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Zafar Khan: There was increased selectivity, not bidding for certain types of contracts. Part of the problem with construction in the business model that we were operating within construction was that you were often left as the last man standing, essentially.

Q306 **Stephen Kerr:** Why, because there was so little margin?

Zafar Khan: Not necessarily because of the margin, but if your supply chain does not perform, and you are signed up to deliver your contract at a particular point in time, you have to supplement that and fund the costs until you can get some sort of recovery of them. That recovery, again, is subject to lengthy debate, discussion and negotiation with the supply chain. If your customer makes changes as you go through the contract, again, you are obliged to act on those changes, because if you do not you are going to be late delivering the contract, but again, the compensation for that takes time. You have all of these dynamics. You are boxed in, where you have to deliver but in terms of your ability to make a sensible return or keeping hold of the cash, you are dependent on people doing the right thing.

Q307 **Stephen Kerr:** I understand that, but you have been described as the person calling the shots. Do you recognise that as a description of your role on the board—that you were calling the shots?

Zafar Khan: I do not know where that description comes from. When I came into the role, I sought to address the issues that I saw within the business.

Q308 **Stephen Kerr:** As a very key person—someone who has been described as the person calling the shots—did you change anything about the way you bid for these contracts?

Zafar Khan: Yes, we did.

Q309 **Stephen Kerr:** What did you change?

Zafar Khan: As part of the lessons learned, we exited the PFI market, which to my mind was probably the riskiest form of contract, and had been responsible for some of the damage that we suffered during 2017. Also, we were looking to limit our exposure to fixed-price, lump-sum contracts going forward.

Q310 **Frank Field:** Your answer to Stephen was that everybody let you down, you could not rely on suppliers, it was all moving around, and so on. It was nothing to do with you; it was all these other terrible people you had to rely on to deliver your contracts. They all let you down.

Zafar Khan: No, I was describing the structure of the construction contract. You are left holding the baby a lot of the time, and that contributes to these issues.

Q311 **Frank Field:** That is why you need good margins, is it not?

Zafar Khan: Yes.



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Q312 **Stephen Kerr:** And good control systems. Why were you sacked in September 2017, after fewer than nine months in your job?

Zafar Khan: Post the 10 July trading update, we had committed to a range of initiatives to improve the position of the business. Key within those was the continued focus on improving the cash flow, and also delivering the revised forecast. As we went through July and August, trading conditions did not improve much, and things continued to be difficult for us.

Q313 **Stephen Kerr:** Was that going to be changed by sacking the CFO?

Zafar Khan: That was a decision by the board. Again, it was not really for me to debate. I provided the board with a further update in September. Not long after that, I was asked to step down from the board.

Q314 **Stephen Kerr:** Their consideration was that your performance had been below the standard that they expected, I presume. Is that what you were told?

Zafar Khan: I had a very short conversation with Mr Cochrane, and in the conversation I was told that the update I had provided to the board had spooked the board, and certain lenders were unhappy.

Stephen Kerr: The messenger got the bullet.

Chair: Maybe Keith Cochrane would like to answer that question.

Keith Cochrane: Just coming back on that last point, part of the reason for appointing Emma and replacing Zafar was recognising where we are in terms of the degree of financial restructuring that the business required to undertake. As part of a series of broader management changes that I announced at the same time, I appointed a chief transformation officer, essentially to drive the restructuring programme. Lee Watson was seconded in from Ernst & Young.

I also wanted someone in the CFO role, given that that was going to be very focused on the external-facing work, dealing with all of the financial stakeholders—and he had experience in that area—and we needed someone to focus very much on the business units. Clearly, you have heard earlier about the challenges in UK construction, so Emma, I felt, was best placed, given her knowledge of the UK construction business, to take on the role and to drive that cash generation.

May I, Chair, just come back to one of the earlier comments that Mr Khan made, and the challenge of Mr Field in terms of what else went wrong in terms of cash generation? Post 10 July, coming in as the interim chief executive, I have made a number of comments in my investor presentations, but at its heart, part of the challenge around the cash generation was that this was a business that sought to do the right thing for the customer. Indeed, in terms of the customer feedback that I received throughout my six months of tenure, there was a huge



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recognition of the support, engagement, and capability of Carillion employees right around the world. That should be acknowledged, but what that meant was that we incurred the cost upfront, and then sought to recover it later.

Q315 Chair: But in your accountancy, you did not do that, Mr Cochrane. In your accounting practices, you were already banking revenues and profits. You are right in reality: that is what you did. You incurred a cost and hoped to recover the revenues later, but in your accountancy, that is not what you did, and that is part of the reason why you are in the difficulties that you are in, Mr Cochrane. Is that not right?

Keith Cochrane: With respect, Chair, that is not quite right. Clearly, we incurred the cost, and we recognised the receivable associated with it. We did recognise the receivable, although not always 100% of the receivable, recognising that there will always be a debate around these things. From a cash point of view, this gets back to the point that if you look at the bulk of the provision that we recognised, it was non-cash. The reality is that the cash had been spent already, and it was all around how quickly we could collect the cash.

With some of it, sure, the business made mistakes. The business did not do things as efficiently as they had assumed in the bid, but if you take the Qatar job that has been reported in the press in recent weeks, this is a job that had doubled in size. It had 2,500 design variations to it, and essentially we were not paid for 18 months prior to the business failing. Should we have done something differently about that? I think that is a fair question to ask.

Q316 Chair: That is not just a fair question, Mr Cochrane. If you were not paid for 18 months, that is even worse payment than you offered to your small businesses, your subcontractors, and that was pretty poor: 120 or 126 days. You had not been paid for 18 months. Why did you carry on doing the work? Should you not have put an impairment in? Should you not have accounted for this much? It is not a question of, "Perhaps we should have done". You should have done, Mr Cochrane, should you not?

Keith Cochrane: Again, in terms of the specifics, one of the roles of the previous chief executive was to have direct engagement with a number of key customers. I do recall a board meeting in April 2017 in Manchester when Richard Howson came back and said, "They have agreed that they are going to pay all their bills". There was this expectation of getting paid. Having said that, six weeks later the world had changed, for a variety of reasons, and it was not paid.

Q317 Chair: But it is not just six weeks, Mr Cochrane. It was 18 months. Surely at some point earlier, an impairment should have been put in, or a warning should have been put out there for those revenues that had already been banked and had already been put on your balance sheet. Should that adjustment not have been made sooner?

Keith Cochrane: Again, it is a judgment call.



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Q318 **Chair:** Did you make the right one, Mr Cochrane? Did Richard Howson make the right one?

Keith Cochrane: All I can say is that I looked at that contract and, certainly over my tenure as chief executive, I sought to achieve a settlement as well. We had the ups and downs of those negotiations, ultimately failing, but the reality was that there was a substantial change in scope in that contract, so undoubtedly there were sums due to Carillion.

Q319 **Frank Field:** We are not disputing that. Contracts change. Rachel's question is about the money. You can change the contract 1,000 times, but they were not paying you the money, and you still went on. There does not really seem to be an answer to that. Can I just ask how much Mr Khan got as a pay-off after his stewardship, please?

Keith Cochrane: Mr Khan received his contractual entitlement: essentially 12 months' salary. That was paid, as it was for all senior executives, on a monthly basis, and that was a very conscious decision by the board.

Q320 **Frank Field:** What does 12 monthly payments equate to, please?

Keith Cochrane: From memory, I think his salary was £425,000.

Frank Field: You sacked him, and then paid him £425,000. Thank you.

Q321 **Ruth George:** Mr Khan, was the writing not on the wall from the 2016 accounts? 84% of your balance sheet was made up of goodwill. There was only £300 million-odd of actual assets within the company, whereas your debts were around £600 million net. Would that not say to you, as someone coming into the role of chief finance officer, that this company is in serious trouble?

Zafar Khan: We acknowledged that the net debt in the business was on the high side, at an undesirable level.

Q322 **Ruth George:** More than the assets.

Zafar Khan: That is not particularly unusual.

Q323 **Ruth George:** You do not think that 84% of the balance sheet as goodwill is unusual.

Zafar Khan: The background to goodwill is that that balance had arisen over a number of years, essentially on the back of acquisitions.

Q324 **Ruth George:** This was the most shorted stock on the stock exchange. How much is goodwill worth in that sort of situation?

Zafar Khan: The way that goodwill is dealt with in financial statements is pretty well-prescribed in the accounting standards.

Q325 **Ruth George:** Your annual report says that your auditors raised queries about that, and that the company decided to override them.



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Zafar Khan: I do not believe that that is the case.

Ruth George: That is what the 2016 annual report says regarding the valuation of goodwill and amortisation.

Zafar Khan: I am not aware of any disagreements with the auditors in terms of the carrying value of the goodwill. Goodwill is one of those things where the carrying value has to be assessed by reference to future cash flow forecasts, and in the process we adopted in arriving at the valuation, we followed what the accounting standards ask you to follow in determining that value.

Q326 **Ruth George:** That was queried. With the accounts based on that, and the worsening cash flow situation, you signed off a dividend that was higher than the previous year. Was that a responsible thing to do, do you feel?

Zafar Khan: The decision around the dividend is a board decision, at the end of the day, and I felt that we had debated that at length, both at the January board and at the February board, as well as with our external advisers. From my point of view, it would have been helpful, given that we were committed to debt reduction, to not pay the final dividend, but at the same time, we had a budget that showed that in 2017, we could service the dividend, we could put more money into the pension scheme, and achieve a small reduction in the average net debt. Those were two relevant reference points. We had a long-established policy of paying dividends in line with earnings growth. Our earnings had gone up by 1% in the prior year, and the final dividend was only increased by 0.8%.

Q327 **Ruth George:** "Only", but only based on that valuation of goodwill. You paid the dividend on 9 June, you issued a profit warning on 10 July, and then you gained some contracts on 17 July, just after that. Does that not seem as though it was manipulation of when that profit warning came in? You have been saying that there were concerns raised over the contracts in 2016. That work was being done much earlier in the year. Was that not rather late in the day to be issuing a profit warning, and did you not have a responsibility, to the company's employees and the Government's contracts that were being made on the back of it, to issue that profit warning much sooner?

Zafar Khan: To my mind, there was not any manipulation of timelines, or sequencing having been done to achieve certain timelines. The contracts review was launched as soon as we were aware of the merits of the contracts review. That was launched around the end of May or early June, essentially.

Q328 **Ruth George:** Emma was saying that she was working on it in March, when she came back from Canada.

Zafar Khan: Emma had come back from Canada into the UK construction business, and started her review of the UK construction business, essentially. The group-wide contracts review was initiated around the



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end of May, and continued through the month of June. The results of that, again, were finalised around the weekend of 8 and 9 July.

Q329 Ruth George: The profit warning came in; the shares dropped 75% in value. Mr Cochrane, when you came in, was it not obvious from the balance sheet from 2016, from that shared valuation drop, that the company was basically insolvent in July?

Keith Cochrane: No, it was not obvious, because the cash flow forecasts at that juncture and our ability to comply with covenants on 10 July suggested that this was a problem linked to specific contracts. It required us to look afresh at the business and its focus, the shape of the business, its overhead structure and the like, but there certainly was not a thought in my mind when I took on the role on 10 July that ultimately, we were going to end up in insolvency. There was, at its heart, a very good business here. Yes, things had gone badly awry in a number of contracts, but that did not take away from the fact that there were a number of very good businesses within Carillion, as well.

Q330 Heidi Allen: I am interested in the mechanics of the organisation culturally, and how it felt about debt and borrowing. I am conscious that you were all relative latecomers to your senior roles. Perhaps just very briefly, what were your thoughts on how the company dealt with debt and borrowing?

Keith Cochrane: Perhaps I could start. Clearly, when I took on the role as chief executive, my focus was very much all about cash generation. As part of that, I brought in EY.

Heidi Allen: I am talking about debt, how the company felt about debt, and whether it was comfortable with debt and borrowing.

Keith Cochrane: From my perspective—from a board seat as a non-executive director for the prior two years—the board had recognised that the net debt position had got to a point where we needed to do something proactively about it.

Q331 Heidi Allen: It was £242 million in December 2009, and it was £1 billion by January 2018, so it had now got to a position where you needed to do something about it.

Keith Cochrane: Clearly, a lot happened between July and January, in terms of sequence of events. I am very happy to take you through some of those events that drove what happened in the last few months, but if you look at it in the context of the year-end 2016 position, as we have said earlier, the debt was too high. The board had challenged management, and indeed management had come forward with what we believed at that time to be a credible self-help plan. The board then sought to do a fund-raising, to substantially reduce net debt, which would have been launched in early July. Because of, as I said earlier, the scale of the contracts provisions and because of that that meant for the investor proposition—



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Q332 **Heidi Allen:** Do you genuinely believe that the debt could have been dealt with, that it was just about contracts and a few things going wrong, and that it was not a systematic issue with the organisation?

Keith Cochrane: If I can then add a bit of hindsight as chief executive, as I came into the business, there was a lot of focus on reported debt across the business. Was there the same focus on collecting cash, day in, day out, with the relentless attention that we applied post 10 July? Did that appear to be the case before 10 July? No.

Q333 **Heidi Allen:** What did you do about it when you came in?

Keith Cochrane: When I came in, as I say, we appointed EY. We initiated weekly cash flow forecasts. We revamped the cash flow forecasting process to ensure that it was robust.

Q334 **Heidi Allen:** Did you think about pushing for more equity?

Keith Cochrane: We did. That is something that we contemplated. Indeed, it was something that we seriously contemplated.

Q335 **Heidi Allen:** But you did not do it.

Keith Cochrane: We did not do it, for a number of reasons. One was that at the end of September, which would have been the natural point to do so, when we announced our half-year results and the results of our strategic review, the market capitalisation of the group was such that raising equity in itself would not have fixed the problem.

Q336 **Heidi Allen:** You were still strong enough to do it then, but you chose to—

Keith Cochrane: No, the advice from our brokers was that it would not be possible to get a successful equity issue away, particularly against the backcloth that I was an interim chief executive. We had not yet, at that juncture, appointed a permanent successor, and investors will always want to know, "Who are we backing?"

Q337 **Heidi Allen:** You are the one in the hot seat.

Keith Cochrane: I was.

Heidi Allen: "Interim" means that you are doing the job.

Keith Cochrane: I am, absolutely. I agree with that, but that was the advice from our brokers and our financial advisers. Alongside that, at the end of September, we were also in advanced discussions to sell our Canadian business, against which we had a very high confidence level, and indeed, on the back of that, there was the potential for that buyer to take an investment in the PLC company as well.

Q338 **Heidi Allen:** Emma and Zafar, can I turn to you two, and particularly, perhaps, Zafar, given that you say that when you came in, a key part of your remit was to bring the debt down? I do not see how that happened, and you were there nine months. I would be interested to know why you



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left so soon, but perhaps starting with Emma and then turning to Zafar, what are your views on the decisions to raise more debt—essentially, it seems to me, to keep dividends going—and not raising equity to make sure that the number of shareholders, and therefore the beneficiaries of dividends, was kept to quite a small pool? What are your views, Emma, first of all, on whether or not that was the right approach?

Emma Mercer: Within the company, the cash control mechanism and the way that the businesses forecasted cash was very well-controlled. Under all of the CFO reigns of Richard, Zafar, and then myself, the attention to detail in cash forecasts in the business was huge, and a lot of effort went into that across all of the different businesses.

Heidi Allen: I am talking about the strategic decisions, about going for equity rather than debt as a means of keeping cash flow going.

Emma Mercer: I cannot comment on the board decisions, or what the board looked at in order to decide around dividend distributions or equity raises. I do know that equity was looked at earlier in the year, which Zafar can touch on as well. From my perspective, the way of getting the debt down was two-fold. First, there were the routes of other mechanisms like debt for equity, for example, or even raising additional equity, but, more importantly, it was collecting the debt that we were due from our customers. That was all around the world.

We talked earlier about one particular contract, and it would be nice to pin this thing to one instant completely, and say, “It was that that broke Carillion”, but actually, this is a series of unfortunate events on some very large contracts that meant that there was huge cash pressure. The drive of getting those receivables back from organisations was, for me, on an operational level in a division, the key to trying to make a success of this business in terms of cash flow. We talked about Qatar. Huge amounts of money were owed there on one particular contract, and there was a huge amount of effort to try to drive and collect that cash. Actually, that was viewed at that point in time as one of the easiest things to do: to get the receivables that we were due from our clients.

Q339 **Heidi Allen:** We have obviously heard that Brexit was another big issue—let us blame everything on Brexit—but apart from that, Antoinette has reminded me that the Qatar contract was only about £200 million, so I do not really think that that was going to transform your fortunes.

Emma Mercer: Across the largest contracts in our group, if you take the ones that were mentioned in the contract provision alongside the Qatar thing, we had huge amounts of debt locked up in each of those contracts.

Q340 **Heidi Allen:** What I am trying to get to the heart of is the company’s approach generally to how it raised funds, going for more loans. £242 million in 2009, rising to £1 billion in January 2018, is not just about how successful we are in collecting our cash from our customers. Zafar, can you say something about your view on how the company behaved in terms of debt and triggering dividends, as opposed to pushing for equity,



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for example?

Zafar Khan: By the time I had started my discussions with the board through the selection process, debt was the number one topic.

Q341 **Heidi Allen:** Did they make the right decisions? Did they prioritise the right way of dealing with that?

Zafar Khan: Historically, things had developed to the point where we understood that we had to reverse the trend on that. Dealing with that through the time that I was on the board, the key priority for me was to get the debt down.

Q342 **Heidi Allen:** Did you do that?

Zafar Khan: Yes, we did.

Q343 **Chair:** What was the debt when you came into the business as CFO and when you left?

Zafar Khan: The year-end debt would have been, I think, around £218 million, but the year-end position is not always reflective.

Q344 **Chair:** What happened to debt, Mr Khan? You just said that you got the debt down.

Zafar Khan: The debt increased through 2017.

Q345 **Chair:** So you did not get the debt down. You just said to Heidi Allen that you got the debt down, but actually the debt went up.

Zafar Khan: We were unable to get the debt down.

Heidi Allen: Did the debt go up or down when you were in the position?

Zafar Khan: But it was not because we were oblivious to—

Q346 **Chair:** Mr Khan, you are a CFO. You just said to Ms Allen that the debt went down. Did the debt go down, Mr Khan?

Zafar Khan: No, it did not. No.

Q347 **Chair:** I just wondered, because you said to Ms Allen that it did. It did not.

Zafar Khan: No, the debt did not go down.

Q348 **Heidi Allen:** What was the reason, do you think, that you left after just nine months? Although you had a handsome pay-out, so that must have been helpful.

Zafar Khan: We discussed the reason why I left. Keith touched on his perspective of it.

Q349 **Heidi Allen:** What is your perspective?

Zafar Khan: Post the July trading update, we were continuing to focus on a range of initiatives to try to improve the overall position of the



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group. Trading continued to go against us, and the next update that I gave to the board showed a deteriorating position again.

Q350 Heidi Allen: Can I turn your attention to a more general question, about suppliers? We have talked a lot about the importance of cash flow and collecting from customers. What about suppliers? You signed up in 2013 to the Prompt Payment Code, yet notoriously you were known within the industry for being exceptionally late payers to your suppliers—around about 120 days' payment. No business can exist like that, as you indeed have proven yourself. Perhaps we can start with Keith.

Keith Cochrane: From my perspective, all I can really comment on is my period as chief executive.

Heidi Allen: You keep saying this. Just answer the question, please. Every time anybody answers a question, you start with, "In the time I was there".

Keith Cochrane: There were very different roles, with respect, in terms of being a non-executive director and being chief executive.

Heidi Allen: When you were chief executive.

Keith Cochrane: When I was chief executive, I was very clear: no instruction was issued to change payment terms to suppliers. Indeed, in discussions with Government, they highlighted their sensitivity, and I reported back to the divisional MDs that we should take particular care to continue to meet the payment terms of our suppliers. Clearly, maintaining supplier confidence over that six-month period was going to be critical to secure the future of the business, and therefore, from my perspective, we made no changes and there was no change in the approach taken.

Q351 Heidi Allen: Did you think that paying in 120 days was acceptable?

Keith Cochrane: Perhaps I could let my colleagues explain. That was not my understanding of the basis on which we paid.

Q352 Heidi Allen: But you were. Emma?

Emma Mercer: There are a lot of facts around this, and I would like to take a moment to explain some of the facts behind this, because I think it will be useful for the Committee to understand. We have two ways of paying our supply chain: first, through direct payment to them, and, secondly, through our supply chain factoring scheme, where we have arrangements with various different banks. Effectively, invoices go onto the system and they can draw down at will over whatever terms they want.

Q353 Heidi Allen: Suppliers pay extra for that privilege, do they not?

Emma Mercer: I will come back to that. Not quite, no. Effectively, we give suppliers the choices of being on either. With those that go on to the supply chain factoring, we do ask them to sign up to terms of 120



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days, but they have the ability to be able to draw down a payment within 45 days—which I will come back to in a second—or anything above 45 days is not at their charge. We get the benefit of the working capital facility associated with that up to 120 days.

Q354 **Heidi Allen:** Does that mean that you were using suppliers like a loan? You were borrowing.

Emma Mercer: The reason we introduced it is because when we went back to the Prompt Payment Code, and we went back to discussions on government contracts—and also on other contracts with our other customers as well—what we found was that we were being pushed to drive supplier days, obviously, down to 45 days, but our customers were not necessarily paying us on 45 days.

Q355 **Heidi Allen:** Just because you have a weak grip on your customers does not mean that it is right to push that down on to your suppliers. That tells me you were not in control of your customers.

Emma Mercer: Exactly. I agree with you, which is why we asked the banks for support, and we talked to Government a lot about this as well, when the payment code came in, about how we could effectively start paying our suppliers on those 45 days without damaging our own working capital. We put this scheme in place with the banks as a mechanism of being able to pay the suppliers promptly, but without damaging the working capital of the business.

Frank Field: You do not have much working capital, do you? It is all make-believe; it is goodwill.

Q356 **Chair:** Can we just give you a quote, Emma Mercer, from the Federation of Small Businesses about this? They said, “These payment terms”—your payment terms—“are far below the standards expected of a company signed up to the Prompt Payment Code, or any responsible business. They are an abuse of Carillion’s dominant position, and have contributed to the perilous situation whereby many of Carillion’s small business suppliers now face the prospect of next to no payment for four months’ work.” Do you agree with the FSB?

Heidi Allen: That was July 2017, was it not, when they wrote to them? That tells me that your system clearly did not work.

Emma Mercer: I have looked back at our record of paying suppliers. During 2017, our average payment days to suppliers was 43 days, and during 2016 it was 45 days. We do have some outliers on the 120 days that I have reviewed over the last few weeks.

Q357 **Chair:** How many outliers are there, Ms Mercer?

Emma Mercer: Depending on the timeframe, it was about 5% of our supply chain.

Q358 **Chair:** How many were being paid in more than 60 days?



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Emma Mercer: Less than 10%, from recall. When you look at those outliers, they were derived from two things, really, in the main: first, the fact that suppliers were not always complying with documentation when they submitted their payments. What we have done with regard to that in the last six months is that we have actually put clearer guidelines on our website, to try to help suppliers make sure that they have all of those. In our organisation, we do have tight controls over fraud, in particular with payment of suppliers, and therefore we have to have robust documentation. Secondly, there were some outliers on a particular services contract with Government, where we have been working with Government, and also ourselves, to try to get that contract speeded up.

Q359 **Chair:** How quickly were Government paying you, Emma Mercer?

Emma Mercer: On core fees, where they are fixed and agreed, fairly quickly.

Q360 **Chair:** What is "fairly quickly"?

Emma Mercer: It varies, contract by contract. Normally, it was under 45 days. Where you get into the term where you are talking about variable works or things that you have to apply for separately out of process, we found it very difficult to get paid on a timely basis.

Q361 **Chair:** Government were paying you within 45 days, but you had 5% of businesses that were being paid 120 days later, and 10% that were being paid after 60 days.

Emma Mercer: On that one services contract, for example, everything that was paid late was all to do with variable works and not fixed works.

Q362 **Andrew Bowie:** Good morning. We are going to move on now to talk about the pension deficit, and the exact deficit of the pension scheme is at this stage unknown, although it has been suggested that it will be just under £1 billion for the five main schemes, which I think everybody would agree is a vast amount of money. In fairness, all of you took up your executive positions within the last year, although, of course, we have heard that Mr Khan was the financial controller before that. What was your assessment of the sustainability of the pension scheme deficit when you took on your executive positions? We will start with Mr Cochrane.

Keith Cochrane: From my perspective, the company had committed to pay £50 million a year. We had continued to make those payments through the first part of 2017, albeit I recognise that we were in discussions around the triennial review at the end of 2016, to set what the payments would be for the next few months. That obviously got somewhat overtaken by events in the post-July period. Post July, it was very clear to me that we needed to work very closely with our pension funds. They were a critical stakeholder, and they were very much in a similar vein to our banks and our other key financial creditors.



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Stepping back to your question in terms of the scale of the deficit, one should not forget that the largest single influence and driver on the deficit position at the end of 2016, and indeed in 2017, was the discount rate that is applied. It is the financial rate assumptions, and what we had seen between 2015 and 2016—which has been commented upon in other places—is that that change in the discount rate made a very meaningful difference to the deficit position. Equally, a change in the other direction would have essentially reduced the deficit in a commensurate way.

Frank Field: It did not make any difference to your payment of dividends, did it?

Q363 **Andrew Bowie:** The pension had been in deficit since 2003, and yet you say you only really began to notice this in July.

Keith Cochrane: I am not saying that. I am saying that it was something that I recognised as a very serious element of the overall position when I took on the role. The pension position had been discussed by the board previously. The board was cognisant and was aware of the £50 million a year that the company was putting into the pension scheme. It was cognisant that there would be a further review on the basis of the 2016 position, and that very much was work in progress as we got to 10 July.

Q364 **Andrew Bowie:** Mr Khan, what is your assessment of the sustainability of the pension scheme, coming from the financial controller and chief financial officer?

Zafar Khan: The pension deficit had grown to those levels because we were not putting a sufficient level of funding in. Clearly, we had a finite level of cash flow, and you had to come to a view on the allocation of that between the pension scheme, the dividend and re-investment in the business.

Q365 **Andrew Bowie:** You were prioritising the share price and dividend over funding the pension scheme. The deficit in 2014 was £406 million, in 2015 £318 million, in 2016 £663 million—for the reasons that we have just heard—and in the interim, in 2017, it was £587 million. You were still paying out dividends that you could not afford.

Zafar Khan: The way the pension deficit contributions are arrived at is essentially through the triennial valuation process, and the last triennial valuation took place at the end of 2013. That required us to put about £47 million into the scheme in 2016, and, as I said, our plans for 2017 showed that we could put the £50 million into the scheme in 2017 and maintain the dividend.

Q366 **Andrew Bowie:** It was not really sustainable, though, was it?

Zafar Khan: In the end, it became unsustainable due to a number of factors and setbacks that we experienced in 2017.

Q367 **Andrew Bowie:** How would you describe your relationship with the



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pension trustees?

Zafar Khan: It is constructive and open. In fact, one of the first people that I met after I took up the role was the chairman.

Q368 **Andrew Bowie:** You would describe it as an open relationship.

Zafar Khan: Yes. As I said, one of the first people that I reached out to was the chairman of the pension scheme trustees, to make sure that I understood their objectives and that they understood the company's position.

Q369 **Andrew Bowie:** Mr Cochrane, would you also describe it as an open relationship?

Keith Cochrane: I would. Particularly, as I say, in the post 10 July period, I had a number of engagements with the chairman of the pension trustees, the Pensions Regulator and the advisers to the various pension bodies.

Q370 **Andrew Bowie:** You do not think that you misled them at any time.

Keith Cochrane: No. From my perspective, post 10 July, they were inside the tent and had the same information the banks had, they had the same information our bondholders had, and were fully aware at all stages and a full party to the—

Q371 **Andrew Bowie:** According to the evidence that we have, the trustees were not told that you had no intention to revert to the recovery payment plan, and wanted to negotiate a plan that would have cut members' benefits. They had absolutely no knowledge of that whatsoever. Exactly the same time you were negotiating with the trustees, you were negotiating with the banks a new plan that would have cut the members' benefits, and the trustees had no knowledge of that whatsoever. Yet you think the relationship was open.

Keith Cochrane: I think it was. I am not sure what time period you are referencing.

Andrew Bowie: August 2017 through to December 2017.

Keith Cochrane: Certainly from my perspective, we had an ongoing dialogue and debate with the pension trustees, to the point that towards the end, in early January, I had written to the pension trustees asking for their proposals to help facilitate a managed restructuring. They came forward with some very constructive propositions, and indeed the new money providers we were talking to, which were doing diligence on the company and were looking to put additional funds into the business, thought there was a basis to move forward with the pension fund.

Q372 **Andrew Bowie:** You got an agreement from the trustees to defer contribution payments in August and September, and only then proposed a plan that would have made it clear that there was no intention to revert to the existing recovery payment plan, and then wanted to negotiate a



deal that would cut members' benefits. So you did mislead the trustees.

Keith Cochrane: No, I would not agree with you at all. The reality is that the pension deferral was attached to the raising of new funds from the banks, the deferment by bondholders of repayments and additional funding provided by the surety providers for the bonding lines that we needed to support contracts. That was all at the end of September. There was an agreement attached to that. We would do a business review, all parties would have access to the same information, and on the back of that we would develop a restructuring proposal. At the end of September, the shape that restructuring proposal would take was not known. That evolved over the subsequent few months, so at that juncture the final proposition for the pension fund was not known, because we had not sat down and worked out what it would look like. Obviously, part of what it would look like would be driven not necessarily by what the company sought, but would be driven by what those providers of new funds to the company would require to support their investment into the business. It was very much an engaged negotiation by all parties.

Q373 **Frank Field:** You were offering up pension cuts, were you not?

Keith Cochrane: No, we were not offering up pension cuts. We asked the pension fund to engage with us. Our desire was to sustain the pension fund. This gets back to my opening remark: this is the worst possible outcome, and frankly it did not need to be like this. There was a way through this—

Q374 **Frank Field:** What could have changed so that we would not have had these hearings? What is the key?

Keith Cochrane: The key was that we were at an advanced stage of putting together a restructuring package. We had presented our lending plan to our banks, and, on the back of that, that business plan going forward. We were having diligence discussions with potential providers of new funds. What we were seeking in that short period before liquidation arose on 15 January was additional short-term funding to help facilitate and ensure a longer-term solution. We believed that longer-term solution was possible, on the back of where we had got to at that juncture. That longer-term solution, without doubt, would have been the best possible outcome for the pension fund, for suppliers, for customers and for employees.

Q375 **Frank Field:** Back to Andrew, because you were actually planning to dump the scheme, were you not?

Keith Cochrane: No, we were not.

Q376 **Andrew Bowie:** The restructuring plan that the company had—and I quote here—"had the primary aim of reducing the amount of the group's required pension contributions". That means you are cutting.



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Keith Cochrane: The restructuring plan required us to look at the shape of the pension fund. There were two options attached to the restructuring plan. One was to go down a route called an RAA—a regulated apportionment arrangement—with the Pension Protection Fund. The alternative was to come to a consensual arrangement, and my point is that in response we essentially said to the company, “Look, the company would have preferred a consensual arrangement”, but it really would have boiled down to whether the new money providers and the banks would essentially require the company to—

Q377 **Frank Field:** The alternative was therefore to kick the pension scheme out of the company and leave it orphaned, was it not? You keep talking about this consensual business.

Keith Cochrane: A regulated apportionment arrangement would have put the pension fund into the PPF, you are right, and detached it from the company.

Q378 **Frank Field:** The alternative was to desert it, and just say, “We are not a sponsor of it”; is that right?

Keith Cochrane: No, that is not right. The options were, essentially, a regulated apportionment route, which would have detached the pension fund from the company and put it into the PPF, or for the pension fund to remain attached to the company but on slightly different, better terms for members.

Q379 **Frank Field:** Not better terms than they had.

Keith Cochrane: Better terms than they would have had under a PPF arrangement and under an RAA arrangement.

Q380 **Andrew Bowie:** Do you accept the trustees’ view that if they had not agreed to defer payments, the company would have gone insolvent in September?

Keith Cochrane: It was a critical component, because ultimately what happened—and I think Mr Ellison has described this in his evidence—was that there was essentially 24 hours of very intense negotiations with all parties, with the banks requiring some concessions from the pension fund, from the bondholders and from the surety, and every stakeholder group at that point contributed to help facilitate the introduction of new money into the group. That was important for us because it then enabled us to give the additional comfort to sign off our going concerns statement at the end of September as part of our half-year results.

Q381 **Chris Stephens:** The board, in its 2016 annual report, bragged that it had increased the dividends in each of the 16 years since the formation of the company. Can I ask you, Mr Cochrane, whether in your view these dividend payments were to the detriment of the pension scheme and the company’s debt profile?



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Keith Cochrane: I think I have said this earlier. Looking at it through the lens of today, if we had suspended dividends and not paid that £50 million payment that was made in 2017, would that have made a difference? Possibly. I do not think, given all of the moving parts, you can say definitively it would have changed the outlook. However, could it have helped? Possibly. I would have to recognise that.

Did it fundamentally change the position of the pension fund? I do not believe so, because, again, it was against the backcloth of the company paying contributions of £50 million a year, and continuing to do so through 2017, so actually by the time we ceased contributions we had paid £33 million in 2017. It was more driven by the sensitivities of what had given rise to the deficit. The scale of the volatility in that deficit was unusually high, in my experience, so, for example, a 1% movement in discount rates had a £600 million impact on the deficit. Clearly interest rates can move in differing directions.

From our perspective, it was something the board did discuss; we took our pension obligations very seriously, but we felt that we continued to support the pension fund in an appropriate manner. Clearly, as a board, we have not seen sight of what the proposal was for the subsequent years, in turn coming out of that 2016 review. We had not reached that point in the negotiations. However, the pension fund was a very important stakeholder for the board and for the group.

Q382 **Chris Stephens:** If the money from dividends had gone into the pension scheme, then there could have been a better recovery plan for the pension scheme. Is that not the case, Mr Cochrane?

Keith Cochrane: One has to look at it in the context of the reasons why you pay dividends and the shape and profile of what period your proposition would have arisen. Clearly, self-evidently, if one put additional money into the pension fund, it puts the pension fund in a better position. However, back to the point I made earlier, from my perspective the company was fulfilling its obligations. We continued to fulfil those obligations until September, and then, as I have said to Mr Bowie, as part of our roundtable negotiation to seek to secure additional funds to support the company. Let us not forget that the banks gave us those additional funds because, at that juncture, we were all working towards resolving the issues the company had faced in a positive manner and essentially creating a new platform for the business going forward.

Q383 **Chris Stephens:** In answer to Mr Bowie's question, it was quite clear that the only reason you were getting money from the banks was because you had done a deal with the pension trustees to defer payment. In the time you were on the board, Mr Cochrane, what discussions took place about dividends at board level?

Keith Cochrane: As Mr Khan has indicated, we had a wide-ranging discussion on dividends in January and February, for example. Typically, if I think back, in previous cycles one would pay the dividend at the half-



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year point, so you would have a discussion at the July or August board meetings. I cannot remember specifically. There would be a regular debate.

To reinforce the point that Mr Khan made, as we looked at the position at the end of February, we had tested the profit expectations for the year and the forecast from management, and that is not just tested against what the chief executive says. It is tested against what the divisional MDs are saying about their own business. As a board we had tested their confidence in the guidance for the full year of profits. Management were committed to reducing average net debt after paying the dividend, and again we tested that plan to reduce average net debt. Against that backcloth, we believed that a dividend payment could be supported at that juncture.

Q384 Chris Stephens: The board decided that paying dividends was a higher priority than the pension deficit of the company. Is that the case, Mr Cochrane?

Keith Cochrane: No, that is not the case. The board was continuing to fulfil its obligations to meet its pension deficit repair plan. Obviously we were in a period of negotiation, but my point is that we had been paying for the years 2014, 2015 and 2016, circa £50 million per year. We continued in that vein into 2017. There was no cessation, albeit there would then be a period of negotiation to finalise what those pension contributions would ultimately look like.

Q385 Chris Stephens: Can you explain, Mr Cochrane, why the annual financial statements in 2016 suggest that the cash flow operations that Carillion had at that point were minus £38 million and it chose to pay dividends of £78.9 million at that point? Are you seriously suggesting that the company did not put dividends at a higher priority than addressing the pension scheme deficit?

Keith Cochrane: I do not agree with that analysis. The dividend in 2016 was cash-backed. If one looks at the cash flow statement, there are a number of other components, such as foreign exchange movements, because some of our debt is denominated in US dollars, which essentially is just the translation effect. If one looks at the underlying operating cash flows of the business, the dividend was cash-backed.

Q386 Chris Stephens: Are the Carillion annual financial statements correct that the cash left in the financial year 2016 was minus £117 million? Is that the case?

Keith Cochrane: I do not recognise the number you quote.

Chair: It is from the Carillion annual financial statement.

Keith Cochrane: I do not doubt that, but I just do not recognise—

Chair: It is quite an important—



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Keith Cochrane: There are a lot of numbers in those financial statements.

Chair: This is a pretty important one, Mr Cochrane.

Keith Cochrane: Yes, I understand.

Q387 **Chair:** The point that Mr Stephens is making is that you are saying that it is all being paid out of cash, and yet the cash left in 2016 is minus £117 million. When it all went under, just a couple of weeks ago, you had at least a £587 million deficit—probably £800 million or £900 million—in the pension fund. Over a seven-year period, 2009 to 2016, you have paid out dividends of £554 million. You have said very warm words about what an important stakeholder the pension fund was and how it really mattered, and you have talked about all of these conversations you had with the trustees, and yet—this was just a matter of fact—you were paying out much more in dividends, were you not, than you were paying into the pension fund?

Keith Cochrane: Certainly the quantum of dividends versus pension fund payments, absolutely. That is a statement of fact. I accept that.

Q388 **Chair:** In terms of when you look at the priority of a business or an individual or a Government, you can tell what the priority is by where they put their resources. Is it not fair to say, when you take two things compared—plugging the pension deficit or paying out dividends—the fact that you were paying more out in dividends than you were paying into a pension fund that had a deficit at the end of probably £900 million shows that the priority was dividends, Mr Cochrane?

Keith Cochrane: I would not agree with that from my perspective.

Q389 **Chair:** If that was not true, Mr Cochrane, you would have been paying more into pensions.

Keith Cochrane: We were paying into pensions what I understood to be an agreed arrangement between the pension fund and the company.

Q390 **Chair:** If I have two children and I pay one of them pocket money of £1 per week and I pay one of them 50p per week in pocket money, and the one who gets 50p says, “Mum, I think that your priority is the other child, because you are paying her twice as much as you are paying me”, and I say, “I do not think that is the right way to look at it, dear”, do you think that the child who is getting 50p has a point, or do you think that they do not?

Keith Cochrane: That is an interesting perspective.

Q391 **Chair:** It is a similar perspective, is it not? I am simplifying, but I am really trying to get to the heart of the issue, because you say that this is a very important priority. There are lots of things that are important priorities, but which one was the more important priority, Mr Cochrane: paying out those dividends or plugging that pension deficit? Which one,



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at the board, did you think in the end that you had to put more money into?

Keith Cochrane: From my perspective, I would just reiterate what I have said already: we had an agreed payment profile with the pension fund. It had been in place for 2014, 2015 and 2016.

Q392 **Chair:** But you deferred it.

Keith Cochrane: We deferred it as part of a restructuring arrangement, alongside suspending dividends, alongside asking for new money from our banks, alongside some of our financial stakeholders deferring theirs, because some of our bonds were due to be repaid in December 2017, and they were deferred and pushed out. This was about all parties.

Q393 **Chair:** But only for one year, did you not? In the final year. In fact, dividends are paid, really, right up until the end, and yet the pensions deficit was increasing.

Keith Cochrane: In the context of 2017, as I say, we continued to pay pension contributions up until September. Perhaps the most important point to make here is that there was common recognition, from both the company and, I believe, the pension fund, throughout the post 10 July period, that the best possible solution for the pension fund was a successful restructuring of the business, and, on the back of that, an enhanced employer covenant going forward.

Q394 **Frank Field:** Are you a shareholder, or were you, rather? You keep referring to it as though this company is still living, and I am falling into the trap with you. Were you a shareholder in this company?

Keith Cochrane: No, I was not a shareholder.

Q395 **Frank Field:** Were you a member of the pension scheme?

Keith Cochrane: No, I was not a member of the pension scheme.

Q396 **Frank Field:** How many people around the board were members of the pension scheme?

Keith Cochrane: I cannot comment on that.

Q397 **Frank Field:** How many were shareholders?

Keith Cochrane: A substantial number of board members. I think probably all board members were shareholders, other than myself.

Q398 **Peter Kyle:** Very quickly, Mr Cochrane, Mr Khan has said that you fired him because he gave a presentation to the board that spooked them. What was it that he said the directors that spooked them?

Keith Cochrane: At that juncture, we were concerned at some of the revisions that were being made to our cash flow forecasts, which seemed to have come as a surprise. There was a broader debate happening at that stage around the nature of or need for financial restructuring. It was



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obvious to me that the business would require substantial restructuring, and I articulated that to the market in the September results presentation. I also wanted to have someone in the role that had come out of one of the business units, and therefore had first-hand experience—

Q399 **Peter Kyle:** I did not ask that. I asked specifically what had spooked them. Was the presentation that Mr Khan gave to the board, which spooked them and led you to fire him, accurate? Was it honest?

Keith Cochrane: Yes, it was an honest assessment.

Q400 **Peter Kyle:** So you sacked him for giving an honest assessment to the board, which happened to spook them?

Keith Cochrane: No. We did not sack him for that reason at all. As I said, it was a change in perspective. Our concern coming out of that was about whether he was fully on top of all of the cash flow arrangements. Back to my point, there was a desire to bring someone in who was closer to the business units and therefore closer to what was actually happening on the ground, in terms of cash collection, which Emma was in her role as CFO of the construction business.

Q401 **Peter Kyle:** So his presentation was accurate. It spooked them. He was being honest. Those three categories were enough to summarily dismiss a director of Carillion.

Keith Cochrane: No, as I said, it was a broad—

Peter Kyle: You did say. These are your words I am repeating back to you.

Keith Cochrane: Those were factors, but I am saying it was against the backcloth of a broader reorganisation of the business. I think there were a number of other senior management changes that we made at the same time, and alongside that the scale of financial restructuring that was required was becoming more evident, and the need to essentially change the nature of the finance director's role became obvious to me.

Q402 **Peter Kyle:** Mr Khan, were you under the assumption that it would have been appropriate for you to not spook the board, using your words? That you could have done so, kept your job by telling them the truth but perhaps either mitigating or not telling them the whole truth of what was happening to their company?

Zafar Khan: I would be speculating.

Peter Kyle: Go ahead. Speculate.

Zafar Khan: I am not sure it is a sensible thing to do.

Q403 **Peter Kyle:** We are trying to get to grips with this, bearing in mind we have three directors in front of us. There are also, in the room, frontline former workers who have lost their jobs as well. I think it is a perfectly



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good time to speculate. Do you feel that you lost your job because you were telling the naked truth of what was happening at that particular point? You lifted the veil and perhaps spoke too boldly about the truth of what was happening at Carillion at that time.

Zafar Khan: As I said, I recounted the feedback I got from Keith, as it was given to me. That was a factor, but clearly, as Keith has said, the board had broader things to consider in their decision, and I accepted the decision and moved on.

Q404 **Peter Kyle:** Mr Khan, you said that you did not see the collapse coming at all. You said you were surprised when the collapse actually came. As far back as 2015, when you were financial controller, Standard Life had sold all of its shares and very explicitly said that they had concerns over financial management. Is it not just a fact that there were shareholders—investors in your company—that knew what was going on in your company better than you did?

Zafar Khan: I do not know the background to why Standard Life sold their shares.

Q405 **Peter Kyle:** We do, because they said so. It was about concerns over financial management, strategy and corporate governance. They said this to you at the time. This was reported to you at the time.

Zafar Khan: It was not reported to me. In terms of picking up the role in 2017, the concerns, the priorities and the issues I felt in the business were the issues we have talked about—essentially, a higher than desirable level of debt, the pensions deficit going up, and some difficult market conditions—and I set up priorities at that point to address all three of those.

Peter Kyle: Your investors took action but you did not.

Q406 **Chair:** Mr Field and I just have a last question each. I just wanted to follow up on something that you said, Mr Cochrane. You said that the collapse of Carillion was the worst possible result, and I think you apologised for your role in that. You said, though, that it was not inevitable and that you needed short-term funding. On 13 January, you wrote to the Government, making a final request in relation to the guarantee of limited short-term funding to provide the company with liquidity for a period of four months, to allow it to carry out the restructuring plan. Did you expect the Government to grant you that short-term funding, Mr Cochrane?

Keith Cochrane: We remained very hopeful of the Government granting us that short-term funding. Our final proposition that we sent to the Government—I think it was at 7.00 on the Saturday evening—was for a staggered support funding.

Q407 **Chair:** How much was it for?



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Keith Cochrane: Essentially, in total, over a four-month period, it was for support of £160 million, but we had also put forward a proposition that was almost on a week-by-week basis: that the following week, if the Government put forward £10 million and then we had reached agreement with our banks by that stage, they would put forward another £10 million. There would then be a review at the end of that week, about whether we were making progress with the longer-term restructuring, and then the same would happen the following week, and then the Government would underpin the supplier payment facility.

From our perspective, we got the banks on board for certainly another £20 million. It was all about creating some runway to see and to get to the point that we could launch the full-scale restructuring programme, where we were having very constructive discussions with potential providers of funding for the long term, and indeed constructive discussions with the pension fund as to how they could support, in a consensual manner, the shape of that restructuring.

Q408 **Chair:** Most businesses, if they got into the difficulties that Carillion got themselves into, would not be able to go to Government to seek a bailout. Did you think that you would get a bailout because you thought that you were too big to fail, or for another reason?

Keith Cochrane: No, I certainly did not think about it as a bailout.

Q409 **Chair:** You were asking for £160 million of taxpayers'—our constituents—money from the Government. The Government's money is from ordinary working men and women.

Keith Cochrane: Indeed.

Q410 **Chair:** That is a bailout, is it not, Mr Cochrane?

Keith Cochrane: Those funds would have been repaid in April out of the proceeds.

Q411 **Chair:** If you had succeeded in restructuring. They were going to get a better payment plan than your subcontractors were. Just on a substantive point, you were asking for £160 million of taxpayers' money to bail you out of a situation you found yourself in.

Keith Cochrane: The second point I was going to make was that, essentially, the Government were our largest customer. They accounted for 45% of the revenues of the business. It is entirely natural for one to approach your largest customer. We have had an example recently with P&H, where the customers of P&H supported the business for a period of time to help it secure; ultimately, that was unsuccessful. This was about reaching out to all our important stakeholders and asking them to secure the future. We all recognise that the reality was that the restructuring plan was not to benefit the shareholders or the banks. They had lost already. The restructuring plan was to benefit the employees, the customers, the suppliers and indeed the pension fund. From our



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perspective, it made a lot of sense, in terms of being the least-cost outcome, if I can describe it as such, relative to other potential scenarios.

Chair: In the end, the Government did not believe that you could deliver on that and so decided not to give you that £160 million of taxpayers' money.

Q412 **Frank Field:** Keith, throughout this, people have been talking about restructuring, which has largely meant throwing people overboard, from what I can see. Did any of the NEDs come to you and say, "One of the people we should overthrow is the chairman"?

Keith Cochrane: No.

Chair: Thank you very much, the three of you, for coming to give evidence today.

Examination of witnesses

Witnesses: Richard Howson, Philip Green CBE, Richard Adam and Alison Horner.

Q413 **Frank Field:** Thank you very much. We will go down the panel. Richard, could we begin by your stating your name and the length of time you have been involved with the deceased firm?

Richard Adam: Good morning. My name is Richard Adam. I joined Carillion as group finance director in April 2007, and I retired from Carillion in December 2016. Could I just say, because I have been out of the business for over a year, how saddened I am by all of the events?

Richard Howson: Chairman, I would also like to say a few words. My name is Richard Howson. I worked with Carillion for just over 22 years. I joined as a design co-ordinator, and I was appointed as chief executive in 2012, something I was very proud of. I left the business at the end of September last year.

I too would like to say how deeply saddened and how sorry I am for what has happened to the business. It was a great business. It delivered hundreds and hundreds of projects very successfully, all around the world, with the highest standards of health and safety, sustainability and quality. But for a few very challenging contracts, predominantly in the Oman and one in Qatar, I believe Carillion would have survived. I wish I had had the opportunity to stay after the end of September to help. Thank you.

Philip Green: Philip Green. I was a non-executive director of Carillion from June 2011, and non-executive chairman from May 2014. I would say I am deeply sorry for the impact that the collapse of the company had on employees, pensioners, customers, suppliers and all stakeholders,



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all the more so because we felt that even on 14 January a restructure was possible, but we are very sorry for the impact it had.

Alison Horner: I am Alison Horner. I joined the board in December 2013, and was appointed head of the remuneration committee in May 2014. I too am very sorry for what has happened.

Q414 **Frank Field:** Philip, can we start with you, and then go straight to Rachel? All of you have rightly expressed your sorrow at what has happened. Can you give us some idea of the depth of despair that you have inflicted on people? How many jobs have been lost or may be lost? How many pensioners will suffer uncertainty and cuts in their pensions? How many suppliers have gone under or are waiting for payments?

Philip Green: Chair, we had approximately 25,000 pensioners, I believe. We had between 45,000 and 50,000 employees, approximately 20,000 of those being in the UK. On the depth of despair, words cannot describe the depth of my despair. I am devastated by the impact that the collapse has had, as I said, on the pensioners, on customers, on suppliers and on staff. It is very difficult to say how sorry or how desperate we are at the situation. We are.

Q415 **Frank Field:** You were there from 2011, and it crashed. How much did you draw out of the company, Mr Green?

Philip Green: My fee as a non-executive was about £50,000, and my fee as a chairman was £220,000.

Q416 **Frank Field:** So in total, since 2011, what have you had?

Philip Green: I estimate it to be about £900,000 over seven years.

Q417 **Rachel Maclean:** Can I ask all of you whether you think the culture of the board was effective?

Alison Horner: I joined the board in 2013. It is a small board. All board members attend all committees. As a non-executive board member, I felt that we had open access to the business. The role of the non-exec was clear: we were there to provide oversight and challenge, and we were able to do that effectively.

Philip Green: I agree with what Alison has said. It is at the heart of good governance, and I believe we had a board that had the right skills, the right level of experience and the right values to conduct the affairs of the company.

Q418 **Rachel Maclean:** What were your values as a board?

Philip Green: Honesty, openness, transparency and challenging management robustly, but in a supportive way. I believe that despite the outcome, and despite looking back and saying that of course there are decisions we would have taken differently—and as Keith mentioned, we also added two divisional executives to join the board meeting as well—the makeup of the board gave us the right skills and the right values for



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the role. Looking back, clearly there are decisions that could have been made differently. They were all made at the time because we believed they were the right decisions.

Richard Howson: In my 22 years within the business, wherever I worked—on a building project, in a business unit, or at group level around the board table—the values, the culture as you described it, was consistent. I was brought up with a culture within Carillion of openness, mutual dependency and collaboration. Those were our three behavioural values, and I believe in my time on the board, from early 2010, that those were values exhibited around the board table, particularly in Philip's time. Certainly, reporting was open, honest and transparent.

Q419 **Rachel Maclean:** Richard Adam, do you have anything different to say?

Richard Adam: No.

Q420 **Rachel Maclean:** Right. Can you give me some examples, Philip Green, of times when there was constructive challenge? Your 2015 annual report states that, "The diverse range of skills and leadership experience offered by the non-executive directors means that they are well qualified to scrutinise performance, assess the group's risk management and control processes, [and] provide constructive challenge". Can you give me a concrete example of when that happened?

Philip Green: Yes, I can. I am sure we will come back to it, but on the whole question of debt. As Keith has referenced, during 2016 we were increasingly focused on the level of debt, and the board consistently challenged management on debt, and management then developed a so-called self-help plan to reduce debt. That would be an example. Another example—

Q421 **Rachel Maclean:** No, Mr Green, I am interested in non-executives challenging the executives on the board.

Philip Green: Yes.

Rachel Maclean: That is what I am after.

Philip Green: That is exactly what I am saying. The non-executives, including me, were challenging the executives on the level of debt, the management of debt, during 2016 on multiple occasions.

Q422 **Rachel Maclean:** But you were an executive during that time.

Philip Green: No, I was never an executive.

Rachel Maclean: I apologise.

Philip Green: To be very clear, I was a non-executive director and then I became non-executive chairman.

Q423 **Rachel Maclean:** Your contention is that you were challenging the executive directors at that time.



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Philip Green: With my colleagues, yes, absolutely. That would be one example. Another example, clearly, is the issue of these large contracts, which has already been discussed by the Committee. Richard and his colleagues reported to us throughout 2016 and into 2017, on the state of the contracts. We challenged; we probed; we asked. People did it in different ways. Some people challenged by sending questions in advance by email; some people challenged in the meeting. I would say that it was a board that constructively challenged management.

Q424 **Rachel Maclean:** When we had our evidence from the previous panel, we had a lot of evidence that there were always risks in the construction industry, that the nature of the construction industry is very challenging, and that it led to all sorts of problems. I was surprised that we were told that so often, because everyone who was in front of us had worked in the construction industry for a very long time. It is my contention that you ought to have understood the risks associated with large construction contracts, and put in place more protections to protect the company against that. What do you say to that, any of you?

Richard Howson: I have grown up in construction, and I would like to give a couple of examples, Mr Chairman, if that is in order. It will be a little bit of detail, just to crystallise how construction works, here in the UK, in Canada and in the Middle East. The Middle East is an extreme, which I have already alluded to.

Q425 **Frank Field:** You negotiated that contract, did you not?

Richard Howson: I did not, actually. I had left the Middle East when that was negotiated.

Q426 **Frank Field:** Who negotiated that contract?

Richard Howson: The then managing director of the Middle Eastern business who superseded me.

My example is our contract on Crossrail, which we won in 2012 and had a value of £30 million. We had to finish that contract by the end of 2014. By the end of 2014, our costs and liabilities were in the mid-to-high £90 million, and we had been paid £76 million. So as was normal, we had had to fund the construction of the project up to the end. Within two months of the end, we sought to settle our final account, and we settled our final account at just over £100 million, and the cash came in by year-end. In the intervening period, we had paid our suppliers; I am sure we will talk about Carillion's payments during this session. We had cash-flowed our suppliers, we had funded the project to the end, and then the cash came in at the end. That is normal. That is in the UK, which is the most mature construction market. That is the normal cycle for construction.

When there are inordinate amounts of change, and two or three-year contracts take eight years to deliver and double in value, as Mr Cochrane said earlier, then the amount of energy and effort to make sure that



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there is cash flow each month is extraordinary, even up to chief executive level. So in terms of the contract in Qatar that you have just referred to, I personally visited pretty much every month of the year—certainly 10 times per year—for the last six years. I felt like a bailiff. That was just to try to collect cash.

Q427 Rachel Maclean: You know this is a feature of the construction industry. This cannot have been a new feature for any of you. It cannot have been a surprise that this was the case in construction. What challenge did you provide management on these assumptions at any point?

Richard Howson: I reported to the board, in my board report in November 2016, when I looked into 2017, that there were six or eight contracts, which we had been working through over the last three, four or to five years, that came to an end. If you think about my Crossrail example, by and large you get your cash flows, and the supply chain gets its final cash flows and retentions, when contracts are finished. You have to finish your contract. You cannot walk away, because customers have, in the case of the Middle East and Canada, on-demand performance bonds on you, which are significant sums that they will pull, or they have the right to introduce new contractors to complete the works at your cost, which will be far more expensive than you completing it yourself.

Looking into 2017, I was looking forward to the end of 2017, because we would have completed all but one of our challenging contracts that we had been working through for a number of years. That would enable us to settle final accounts and bring significant cash flows into the organisation. That was my key priority for 2017.

Q428 Frank Field: You had a contract with Qatar, and they actually signed you to such penalties that they could refuse to pay you on time? That is what you are telling Rachel, is it not?

Richard Howson: Working in the Middle East is very different to working anywhere else in the world.

Frank Field: Can we just stay on this point that Rachel has raised with you?

Richard Howson: Sorry, would you mind repeating the point?

Q429 Frank Field: You were saying you could not do anything about the Qatar non-payments, because you had signed penalty clauses, which, if they operated, would cripple you. Why did you actually sign those contracts?

Richard Howson: No. On the Qatar contract, because of the size of the contract, they have performance bonds, and the performance bonds are on demand. So if you wilfully abandon, they would say, the contract and walk away, then they would pull the performance bonds.

Q430 Frank Field: Even though they were not paying you.



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Richard Howson: Even though they were not paying. We did not have suspension rights.

Q431 **Frank Field:** You signed up to that.

Richard Howson: We did sign up to that, in 2011.

Q432 **Rachel Maclean:** We have heard about the complex nature of your business from the official receiver. They said they did not have a full picture of the business's assets. What is your comment on that, Philip Green? Did you ask to have a full picture of the company's assets?

Philip Green: I believe the board was very well informed.

Rachel Maclean: That is not what the official receiver says.

Philip Green: The reference I heard them make was they were struggling to get a list of the 160 subsidiary board directors. We were certainly aware that there were some issues with our HR database. That did not surprise me. However, in terms of the financial assets and the financial reporting, I have no reason to believe that our systems were not fit for purpose.

Q433 **Rachel Maclean:** They have told us they are struggling to uncover exactly what the financial situation was, so I am asking you whether you feel you had enough information. Keith Cochrane said that Zafar Khan gave a cash flow forecast that came as a surprise.

Philip Green: I believe the board was well-informed financially, and supported by a very high quality group of advisers.

Q434 **Rachel Maclean:** How could a cash flow forecast be a surprise to the board?

Philip Green: One of the reasons that Mr Cochrane was surprised was because the numbers that Zafar presented on that particular occasion were different to what had been presented before.

Q435 **Rachel Maclean:** Were they more optimistic or less optimistic?

Philip Green: They were different. That was at a time when these contracts were deteriorating dramatically.

Q436 **Rachel Maclean:** Do you mean that they were more aggressive? It was more of an aggressive or overly-optimistic picture that he was giving.

Philip Green: No, I mean that the contracts during that middle period of last year were deteriorating very dramatically and very quickly, and therefore the numbers were deteriorating.

Q437 **Rachel Maclean:** Did the cash flow show that deterioration?

Philip Green: We believed that both the profit forecast and the cash forecast reflected management's best view at that point in time.

Q438 **Frank Field:** The picture you are giving, like the previous panel, is that



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everybody was surprised; they were taken by surprise at what happened to this great company.

Philip Green: We were all surprised by the extent and speed of deterioration in those small number of contracts between the spring and the autumn of last year. That is true.

Q439 **Frank Field:** You had a business model in which a few contracts could actually sink the whole company.

Philip Green: Given where we were when we went into the year.

Q440 **Frank Field:** You were there since 2011.

Philip Green: No, given the debt that the company had at the beginning of the year. If you were to ask me, "Why did you get into this situation?" I would say that there were three factors. One is the level of debt that we had in the period from 2013 to 2015.

Q441 **Frank Field:** And you were there since 2011.

Philip Green: Yes. One of the biggest drives of that level of debt was an acquisition made actually before I joined the board, in very early 2011, which cost about £300 million or £400 million. The level of debt in 2013 to 2015 or 2016 was too high. That would be my first explanation. The second explanation is this small number of contracts that went very badly wrong, and the third factor would be the inability to get the short-term financing in the middle of January. Those, to me, are the three key explanations.

Q442 **Frank Field:** You took almost £1 million out of the company while this was happening.

Philip Green: Yes, I was paid by the company for seven years.

Q443 **Rachel Maclean:** Mr Green, Mr Howson has just described that he was acting like a bailiff; he was going to collect cash at every opportunity. Did he not report back to you that these contracts were deteriorating?

Philip Green: He reported in detail. As Alison has said, we had board meetings almost every month. I think we had 10 board meetings a year. We all sat on the various committees.

Q444 **Rachel Maclean:** How could it be a surprise, given what he has just described to us? He was going there regularly, speaking to people. He must have been on the ground. He must have seen for himself.

Philip Green: All of that. He was, very conscientiously.

Q445 **Rachel Maclean:** How do you account for the lack of challenge and preparing for a potentially disastrous scenario?

Richard Howson: I am going to choose Royal Liverpool, which you touched on in the last session. Why did the forecast deteriorate in Q2 on Royal Liverpool? We had found a cracked beam. It was an enormous



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beam in a plant room that was surrounded by plant. If I had walked you around Royal Liverpool a year ago, it looked finished: paint on walls, ceiling tiles in, carpets down. We decided to remodel the whole structural frame, using independent engineers to see if there was the potential for more cracked beams. There were eight cracked beams that needed remedial works, and it took us two months to ascertain that. It then took us four or five months to do the remedial works to these large concrete beams. That caused a delay to the end of the year, which added over £20 million of cost to our completion.

Q446 **Frank Field:** You are making your case worse. This is almost a parable for the company. You complete the contract and then you find cracked beams all over the place, so you had to repair those. That is the model of what we have been getting this morning.

Richard Howson: I am illustrating how the cost projection changed in Q2 of that year.

Q447 **Frank Field:** I am suggesting you are telling us a parable that is appropriate to the whole company's business model: there you go ploughing on, and then at the last minute all these difficulties appear. The idea that you have been doing this major reconstruction and then you find the cracks in poor old Royal Liverpool seems incredulous.

Richard Howson: It is a very exceptional event, to find beams that crack that have been designed by a professional designer. As a competent contractor—and it goes back to my pride in Carillion—we did not just cover it up. We properly rectified, even though it cost, and those beams would probably never fail in their cracked state. We chose to rectify them because that is—

Frank Field: It is a parable for the company.

Q448 **Rachel Maclean:** I just want to come back to the issue of the challenge on the board. Major institutional investors were divesting themselves of your stock. This must have been a red light flashing on the dashboard. We have seen this has happened before. Short-selling is a signal of an underlying company's performance and of issues. Who, on the board, was asking those difficult questions? Were the non-execs asking it? Who was saying, "Look, guys. These people are selling our stocks. What do they know that we do not?" Who was saying that?

Philip Green: It was a very engaged board.

Q449 **Rachel Maclean:** Who asked the question?

Philip Green: All colleagues asked challenging questions.

Q450 **Rachel Maclean:** Did you ask about the institutional investors?

Philip Green: I absolutely asked about the shorting.

Q451 **Rachel Maclean:** In the board.



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Philip Green: In the board, on more than one occasion.

Q452 **Rachel Maclean:** What answer did you get?

Philip Green: The answer was that there were some shareholders who were particularly following one or two analysts who were very negative, and they took a view on the company. There were other analysts and other shareholders who took a different view.

Q453 **Frank Field:** You have this mega-challenging going on. Can you give us an example of one policy being changed as a result of all this challenging?

Philip Green: We believed that the policies that we had—indeed, KPMG in August—

Q454 **Frank Field:** So there was a lot of challenging but nothing changed.

Philip Green: Forgive me. In the August 2016 audit committee, KPMG told us that they “continued to assess the processes, systems and controls in place to be the best in class.” This was in a meeting with KPMG, and also Deloitte, who were doing our internal audit.

Frank Field: We have them in next week, I think.

Philip Green: Their final comment was, “We observe that this is underpinned by a culture of doing the right thing in the business”. This was the context and the environment with both KPMG and Deloitte.

Frank Field: It is the blind leading the blind, is it not?

Q455 **Peter Kyle:** Mr Green, let us take at face value your testimony here. You were scrutinising, you were challenging, you were identifying the correct weaknesses in the businesses, but there were no red lines that were crossed. You have said to us that you identified debt as a major problem from the moment you took over as chair. You clearly gave instructions that the debt had to be dealt with, and yet debt continually went in the wrong direction. My question is simple: why did you not remove Mr Howson as chief executive and get some people into the company who could deal with the debt crisis?

Philip Green: Let us be clear: that is exactly what the board did do. We did remove Mr Howson as chief executive, because, frankly, in the period from May to June, we had begun to lose confidence because the debt was not coming down, the operational difficulties were increasing and we had not been able to successfully do the rights issue. As soon as the board formed a view, we did take action.

Q456 **Peter Kyle:** What other action followed from that? Do you feel that removing Mr Howson was too late? Had the horse already bolted?

Philip Green: If you ask me the slightly different question of what I would do differently if I had my time again, I might have removed him a



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little earlier, but only a month or two. Up until very close to that time, he had the full confidence of the board.

Q457 **Peter Kyle:** That is my problem. It took so long. The writing was on the wall for a long time, and he maintained your confidence. The senior team maintained your confidence—and yet all of the indicators were going in the wrong direction—until it was far too late. Sirens were going off.

Philip Green: As part of the chair's role, you take soundings from investors, you take soundings from customers, and you take soundings from colleagues.

Q458 **Peter Kyle:** And you trust your own instincts.

Frank Field: You changed nothing. At the end you sacked somebody, and then you did all these factors as the chairman, but you did not really change anything in the business model, did you?

Philip Green: Before Richard left, we had a lessons learned session, which was referred to in the earlier session, and, yes, decisions were taken around changing the business model in June, both geographically and in terms of different markets. Yes, there were lessons learned.

Q459 **Peter Kyle:** Thank you, Chair. Mr Green, when you were managing director of Coloroll, which was a FTSE 100 company, that also went bust.

Philip Green: It was never a FTSE 100 company.

Q460 **Peter Kyle:** Okay, it was a large company—one of the hundred biggest industrial companies in Britain. When that went bust, there were findings against you by the Pensions Ombudsman, a finding that there was a breach in trust and maladministration. You have been very honest and open about the learning from that experience. You have said, on the record, "It never comes up in conversation. It is just not an issue. But I am a better manager for having gone through that experience." What experience have you taken from that collapse that demonstrably played a part in how you handled Carillion?

Philip Green: The Coloroll situation occurred almost 30 years ago. As you say, we were criticised. The trustees took a decision on advice. We were then criticised by the ombudsman. I accepted the criticism and I learnt the lessons.

Q461 **Peter Kyle:** None of that was my question. You said on the record that it made you a better manager. What experience did you take from that first collapse that you brought to bear in your role as chair of Carillion, bearing in mind Carillion collapsed?

Philip Green: One specific lesson would be the quality of advice. Clearly, I believe I was not well-advised in the Coloroll situation. We sought very strongly at Carillion to make sure that we had quality advice, whether it was Slaughter & May as our lawyers, Lazard as our bankers or Morgan Stanley as our brokers. We believed we had high quality advice in the Carillion situation, which was a lesson from Coloroll, in answer to



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your question. Those advisers were involved with us, intimately, throughout the last 12 or 18 months.

Q462 **Peter Kyle:** There are only two outcomes: either the advice was wrong, or you did not take the advice on board and act on it, because the company, Carillion, has collapsed.

Philip Green: We took advice every step of the way, from those advisers I just mentioned.

Q463 **Peter Kyle:** Your relationship with the chief execs was supportive. Was it robust enough? That is the key relationship in an organisation. Was it robust enough?

Philip Green: It is a very important relationship, and I believe it was robust, yes.

Q464 **Peter Kyle:** Mr Adam, you left in 2016. You had shares in the company at that point, when you left.

Richard Adam: Yes.

Q465 **Peter Kyle:** Did you have them right until the end, or did you dispose of them?

Richard Adam: They were disposed of on my retirement, in accordance with the procedures that the company put in place for everybody.

Q466 **Peter Kyle:** You sold your shares as soon as you left the company.

Richard Adam: Following my retirement.

Q467 **Peter Kyle:** If you felt that the share price was going to go up for Carillion and that it was a really safe bet, would you have still sold them?

Richard Adam: Yes, I would. I do not have a share portfolio. I do not own shares of any substance in any company. I do not take that sort of risk.

Q468 **Peter Kyle:** At some point on your watch, the company moved from being one where the majority of its contracts were sustainable and bringing in an income, to being one where new business was subsidising failing contracts. At what point do you think that happened?

Richard Adam: I do not recognise that. I believe during my tenure the company was healthy; it was operating in challenging markets but was managing in those markets in a satisfactory way.

Q469 **Peter Kyle:** Mr Green, in 2015 Standard Life divested its investment in the company. It reported to the company that it had done so because of concerns over financial management, concerns over strategy and concerns over corporate governance. That was a 5% holding in the company, disposed of. The company then changed its clawback rules—and this will be carried up by other members—straight afterwards, and then your CFO leaves and sells all of his shares instantly. There are



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many other indicators. There were loud voices telling you that things were going wrong. You are saying that there was no indication that something was wrong until the last minute. I simply say it is incredible.

Philip Green: I am not saying that there was no indication there was anything wrong until the last minute. I am not saying we got all of the decisions right. I am not saying either of those things.

Q470 **Frank Field:** When we had BHS before us, Sir Philip Green began by saying, "I am not going to point any fingers at anybody", and then spent the whole of our six hours, or whatever it was, pointing fingers at other people. We have had one session here where everybody was pointing fingers at other people. Your main evidence so far is that you have had these advisers; you have, in effect, pointed the finger at them. Peter's question is: what is your responsibility for this collapse?

Philip Green: Full and complete.

Frank Field: Total?

Philip Green: Total.

Frank Field: Very good.

Philip Green: There is no question in my mind about that—not necessarily culpability but full responsibility. No question. If I look back, of course there are things we would have done differently.

Frank Field: With the reports we will obviously weigh up some of these judgments.

Philip Green: There is no question about full responsibility.

Q471 **Ruth George:** Mr Adam, Mr Green said earlier that the board felt that the level of debt was too high from 2013 to 2016, and it was growing during that time. You have said that you do not take the sort of risk of owning shares, yet in each of the company's financial statements you were trying to encourage other investors to invest in Carillion. Why was that?

Richard Adam: It was part of my role to present the financial position to all stakeholders, and I did that as any finance director would.

Frank Field: Would you like to actually focus on the question you were allocated, which was on people leaving?

Q472 **Ruth George:** Absolutely, because you left at the end of 2016, just before you needed to account for that high level of debt. Why was it that you left?

Richard Adam: I left because I was approaching 60. I had been a finance director for 30 years. I initially had a discussion with the company about retiring at the time Richard took over from the previous



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CEO. I was asked to stay, to help the transition, and then we got to 2015, and I said to Richard that I now felt that the time was right.

Q473 **Frank Field:** The time was right for whom?

Richard Adam: For myself. I was approaching 60, and I wanted to spend some time with my family. As I say, I had been doing this role in various organisations for 30 years.

Frank Field: As politicians, we understand that answer.

Q474 **Ruth George:** Mr Howson, you said that you wished you could have stayed on to have sorted things out. Do you think that anybody could have sorted Carillion out by July, or did you hand over a sinking ship?

Richard Howson: Certainly the business was in a very challenging position. The reason I made the statement at the start was that when Philip asked me to step down, he also asked me to operate at a different level, not at an executive level, to try to bring cash in on those contracts where we were owed cash—principally in the Middle East, and in Canada—because I had lived with those contracts throughout most of my tenure as CEO. I had relationships with the customers, and, as I explained earlier, when those contracts come to an end that is when you can get the cash coming in.

Q475 **Frank Field:** This is not the question that Ruth asked. Ruth asked you whether you thought you were jumping from a sinking ship.

Richard Howson: I knew the business was in a challenging position. I knew we needed to do a rights issue, in order to strengthen the balance sheet. I felt, on 7 July, when Philip spoke to me, that the business was in a sustainable position because we had support from the banks that we had agreed the day before.

Q476 **Chair:** Richard Howson, you said that you knew the company needed to do a rights issue. From when did you know that the company needed to do a rights issue?

Richard Howson: From the final couple of weeks in June. The timing of the rights issue was to be decided. If I go back a step, in terms of the chronology of events, Emma talked about the working capital questions that she had, and when she had those questions at the end of April, I instigated a KPMG review of a small number of contracts in the construction business. You talked about that in the previous session. While we were doing that review, there was significant deterioration in the cash flows, in the projection, and we started to prepare, in the event that we needed it, for a rights issue, producing a prospectus. Part of that is to do a contract review of a lot of contracts—50 in that case—to prepare in the event that we needed a rights issue.

Q477 **Chair:** You published the annual report in March 2017, and it was very optimistic. Two months later, you ask KPMG—the very auditors who signed off that report—to do a review into your contracts. They then



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came back to you in June or July, was it? They expressed their concerns, particularly over those four contracts.

Should you, as the chief executive, Mr Howson, have issued that annual report, which was so optimistic, on 1 March 2017? Should you, perhaps, have had KPMG or somebody else to come in sooner and review those contracts? By July, I would argue that perhaps it was too late to attempt a rights issue, which was why it did not succeed.

Richard Howson: In terms of the annual report and accounts that were signed off in March, I believe it was correct to sign off those accounts, given what we knew at that time and the judgments that we made. Things like the concrete beams materialised after the beginning of March.

Q478 **Chair:** Yes, but you had already not been paid for some time by Qatar, had you, at this point?

Richard Howson: I had lived through that for many years, and I had brought significant cash in on the Msheireb contract in July 2016, by settling the first two claims.

Q479 **Chair:** How much were Carillion owed by Qatar when you left the business, Mr Howson?

Richard Howson: If we had completed the contract—

Chair: No. How much were you owed by Qatar—

Richard Howson: —they would have owed us £200 million.

Q480 **Chair:** I would like you to answer the questions I am asking you, not the ones you want to answer. When you left the business, how much did Qatar owe the business?

Richard Howson: Around £200 million.

Q481 **Antoinette Sandbach:** Was that the case in March, when the accounts were signed off?

Richard Howson: That number would have grown.

Q482 **Chair:** What was it in March, Mr Howson?

Richard Howson: Probably about £180 million or £190 million. As contracts drift, costs go up.

Q483 **Chair:** There seems to be a lot of drifting going on. You issued those accounts in March, which, as I said, were very optimistic. You had £180 million or £190 million—what is £10 million between friends?—owed to you by Qatar. By July, when Philip Green asked you to step down, you had £200 million owed to you by Qatar. You had an £845 million provision that had to be made in July, when you left; is that right?

Richard Howson: The Qatar contract was meant to finish in May 2017. That completion during March and April was moved to September or October 2017, because we had not been paid. There were still 6,000



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people on site, but it needed 12,000 people on site to complete it. The projection moves on to the new completion date. It was then meant to finish in December, and my understanding now is it finishes in December this year.

Q484 Frank Field: You were asked to step down. You were then given the responsibility for delivering the payment of the contract, which helped sink the company. Is that a fair summary?

Richard Howson: One of the reasons I was retained was to try to settle the final account on Msheireb, yes.

Q485 Andrew Bowie: Good afternoon. 10 years ago, the company made the first of two major acquisitions, which were described at the time as being transformational for the company. It bought Alfred McAlpine for £565 million, and then in 2011 it purchased Eaga for £306 million. Were these purchases made with the sole purpose of propping up your waning balance sheet, Mr Adam?

Richard Adam: No. The strategy was to look at opportunities that would increase the proportion of the business that related to support services rather than construction. The strategy was aimed at de-risking the group. Of those businesses, Eaga had no construction in it of any consequence, and McAlpine had some construction but was predominantly a services business with longer contracts.

Q486 Andrew Bowie: It was an exercise in adding goodwill to the books.

Richard Adam: A consequence of acquisitions is that in the event that the company being bought does not have substantial tangible assets, it increases goodwill.

Q487 Andrew Bowie: Substantially. The purchase of McAlpine alone added £650 million of goodwill to the business.

Richard Adam: That was a consequence of the acquisition. That was not the reason for doing it.

Q488 Andrew Bowie: That in no way came into your decision-making to purchase.

Richard Adam: Absolutely not.

Q489 Andrew Bowie: Were you aware of McAlpine's major pension deficit of £110 million when you purchased it?

Richard Adam: Yes, we were.

Q490 Andrew Bowie: That was eight times higher than Carillion's at the time.

Richard Adam: The company was aware of that, yes.

Q491 Andrew Bowie: That was transformational for Carillion, because within a year Carillion's deficit had gone up by 348%, to £61 million. That was transformational, certainly in that respect. You would agree with that.



Richard Adam: Yes.

Q492 **Andrew Bowie:** Why did you keep adding to the overall deficit by buying out companies with even bigger deficits than your own? It just does not seem sustainable, really. I now begin to feel sorry for Mr Khan and Mr Cochrane, who inherited this entire mess.

Richard Adam: I do not believe that was the case.

Andrew Bowie: Sorry.

Richard Adam: I do not believe Eaga, for example, had a pension deficit.²

Q493 **Andrew Bowie:** You were warned about this. Robin Ellison has told us that, "the challenge we were facing was: was Carillion a worse covenant than McAlpine? [...] On calculation of the covenant the margins that Carillion were making were so small compared with McAlpine's that it was a real worry for us. We had discussions with the finance director about what he was doing about margins". Do you recognise these concerns, and how did you respond to them at the time?

Richard Adam: I do recognise that conversation with Mr Ellison. At the time, McAlpine was reporting margins that were in excess of the industry average, and our assessment at the time, as a group, was that that was one of the reasons that it was in difficulty, and therefore was capable of being purchased.

In terms of Carillion's own margins, again the strategy was to move the group toward support services, which carries higher margins, usually in excess of 5%, and move the weighting away from the construction business, which on average had margins of around 2.5%.

Q494 **Andrew Bowie:** It was a completely unsustainable model.

Richard Adam: I do not believe that to be the case.

Q495 **Andrew Bowie:** In reality, this is where the rot set in. The £1 billion pension deficit we have today can be traced all the way back to the purchase of McAlpine in 2008.

Richard Adam: If you look at the pension—

Q496 **Chair:** Richard Howson just nodded his head there, so clearly that is something you agree with. Would that be correct?

Richard Howson: 65% of the pension deficit is from the Mowlem and McAlpine acquisitions.

Andrew Bowie: Thank you. Sorry, Mr Adam.

² Mr Adam subsequently clarified for the Committees that Eaga had retirement benefit liabilities (i.e. a pension deficit) of £0.8m at the acquisition date. This is shown on page 92 of Carillion's 2011 Annual Report.



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Richard Adam: I was only going to add that, notwithstanding that point, the pension deficit—and I think it is a point that was made earlier today—is highly sensitive to movements in interest rates, and that—

Q497 **Frank Field:** Or the non-movement of them

Richard Adam: Or the non-movement of them.

Q498 **Frank Field:** This did not blow up like a storm and throw you over. The quantitative easing's impact on pension funds was well-established early. It did not steal up to you like a thief in the night. Every pension fund has faced this.

Richard Adam: I agree.

Q499 **Frank Field:** Could I ask, Alison, what your take on this is, about the disaster for the pension fund and the pensioners? What role did you play in trying to rescue it?

Alison Horner: As a member of the board alongside the others, one of our responsibilities was to consider all of the cash requirements of the stakeholders of the business. I am a pension trustee myself, so I am very aware of the responsibilities.

Q500 **Frank Field:** Of this scheme, or of other schemes?

Alison Horner: No, a scheme of my primary employer.

Q501 **Frank Field:** Is that Tesco?

Alison Horner: Yes. I am very aware of the responsibilities of the trustee to balance the call to protect the promise to members, and to continue to support the sponsor organisation. As a board, we were very active in considering those cash calls.

Q502 **Frank Field:** Could you please give us details of the proposals that you made to the board, which would further that goal, Alison?

Alison Horner: We were coming to the triennial valuation, and one of the challenges to the board was the recognition in our forward forecasting that we may have to provide for a bigger contribution than the £50 million that we had paid for the previous three years, and that we should take that into account in our forward forecasts.

Q503 **Frank Field:** Did you at any time argue with the board that they had got wrong the balance between trying to protect pensioners and paying out to shareholders?

Alison Horner: It felt like that was going to become a very live conversation in this valuation that was coming today. Do not forget, the previous contribution of £50 million had been agreed prior to my joining the board.

Q504 **Frank Field:** But you were on the board while the pension fund was deteriorating.



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Alison Horner: I think our view was that, given the arrangement we had made with the trustees and with the support of the Pensions Regulator, that £50 million contribution was sustainable for the period of the current valuation, but it was something that we were going to have to look for in the next.

Q505 **Frank Field:** Did the chairman of the trustees ask you for more?

Alison Horner: No.

Q506 **Frank Field:** Did he battle for more?

Alison Horner: No.

Q507 **Frank Field:** Did he express disquiet?

Alison Horner: Not directly to the board, no.

Q508 **Stephen Kerr:** Carillion has been criticised for aggressive bidding, for low pricing, and having delivered low profit margins when there was a huge element of risk. Is that a description of Carillion that you would recognise, Mr Green? Is that a fair criticism?

Philip Green: Low profit margins is certainly accurate.

Q509 **Stephen Kerr:** What about aggressive bidding?

Philip Green: I mentioned earlier that in June, with Richard Howson and the board, we had several "lessons learned" sessions, and I think there were lessons learned both in terms of the way bids were formulated and the type of work we were bidding for.

Q510 **Stephen Kerr:** Can you talk a bit more about the lessons in relation to bid prices that you were putting in on jobs that were going to give you less than thin margins?

Philip Green: There were some examples where negotiations around the contract itself were done too quickly, and the lesson learned was that if we had spent longer on the actual negotiation, some of the risks may well have been able to be mitigated. That would be an example.

Q511 **Stephen Kerr:** Why, given the fact that this aggressive bidding and these prices and low margins were not recent phenomena, did Carillion keep bidding so aggressively? Why did you keep picking up such low-margin contract business?

Philip Green: The industry itself is low-margin. This is a very competitive industry.

Q512 **Stephen Kerr:** You had a particular reputation as a business for it.

Philip Green: Forgive me. I do not believe we had lower margins.

Q513 **Stephen Kerr:** You do not recognise that.

Philip Green: No, I do not. I do not believe we had lower margins than our peers.



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Q514 **Chair:** Can I ask what happened to your average margins, both on government work and other work, during the time that you were chairman, Philip Green?

Philip Green: I could not give you the number per year, every year, but I know we compared our margins to peers on a regular basis, and our margins compared favourably.

Q515 **Chair:** Would anybody from the board be able to tell me? Thank you, Mr Howson.

Richard Howson: I have three points, if I may. First, can I answer your question from about 20 minutes ago about policy change? There was a clear policy change in 2013 when we stopped bidding for construction work in Canada, other than PFI, and we stopped bidding traditional construction work in the Middle East, other than with the support of export finance. That was because of challenges in the market, in terms of the risk balance between customers and supplier, and cash flows.

Q516 **Frank Field:** PFI in this country is viewed like printing money. Is that why you were bidding for those contracts, or is it different in Canada?

Richard Howson: Carillion's model is that we spent—

Q517 **Frank Field:** What I am saying is that they proved incredibly profitable. In my constituency, it was 16.3% plus management charges. Nobody could tell us the management charges. They are very profitable contracts.

Richard Howson: The attraction of PFI for Carillion, from 1995 when it started, was the longevity of the contract. We are a construction business and we are a support services business. It gives us the opportunity to deliver both over a 25-year period.

Frank Field: Sorry, I am only questioning it because I was giving you the chance to say how wise you were, going for those contracts.

Richard Howson: We have had a lot of success on PFI. I have forgotten the question now, sorry.

Q518 **Chair:** The question, Mr Howson, which you generously offered to answer, was what had happened to margins in government and non-government work, during perhaps the time that you were chief executive?

Richard Howson: Contracts last for a period of time, usually three years. The contracts at the beginning of my tenure were won in the heart of the credit crunch. In the heart of the credit crunch in the UK, more risk was passed to contractors. There was less two-stage bidding, less collaborative bidding, frameworks, alliances, et cetera. As you move through time and the coalition put its shoulder behind investment in infrastructure, then bidding became more collaborative, as it did in the private sector. Predominantly two-stage bids, alliancing and frameworks give the contractor the ability to work at an earlier stage with the



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customer, de-risk the contract, and protect the margin. I do not believe that margins have moved a great deal over that time.

In construction, as Richard said, margins are between 1.5% and 2.5%, generally. In support services—or the field of support services that Carillion worked in—generally you would bid at around 3.5% to 4.5%, but on a five or seven-year support services contract, as you improved your productivity and efficiency and you understood the services better, we could move the margin to 6% or 7%, but then it is rebid.

Frank Field: Why did this all go wrong? We are left with this incredible puzzle. You are always telling us how brilliant this was—all this advice and so on. We are discussing a disaster.

Q519 **Chair:** Sorry, I am still not sure of the answer to my question. You are saying in the years you were chief executive, Richard Howson, that those margins were tight at the beginning and then they got higher. You talked about 1.5% to 2% for construction and 3.5% to 4.5% for support services; was that at the beginning, at the end, in the middle or an average?

Richard Howson: The contracts that we were bidding at the beginning of my tenure were bid at 2% or 2.5% in construction. Towards the end of my tenure, in infrastructure, we could bid at 5%, 6% or 7%, because demand exceeded supply. Some of the contracts at the beginning of my tenure, particularly prior to me being CEO, in 2010 and 2011, were won in the mid-millennium, so some of the PFIs had much better margins—of 7%, 8% or 9% on big PFI schemes—which we enjoyed the benefit of through the early part of the credit crunch.

Q520 **Chair:** So on Stephen Kerr's point, that it was all because of low margins, you were getting pretty good margins.

Richard Howson: They are the industry margins. To be competitive, to win work, to create future cash flows, you have to win. Winning is a balance of risk and reward.

Q521 **Stephen Kerr:** Is it not the case that you were chasing high-volume contracts in order to get short-term cash?

Richard Howson: No, because we did not bid in 2011, 2012 and 2013, when there was a dominance of single-stage construction bidding. We did not bid any single-stage. We refused. We only bid two-stage. That is why, in 2009, the group strategy was to halve the size of our construction business, from £2 billion to £1 billion, because we did not believe the market that we could survive and exist in would be there. The downside of that, because construction had negative working capital, was a significant outflow of working capital between 2010-11 and 2013. That is why Richard raised additional funding through private placements in 2010, 2011 and 2012, to cope with that descaling of the UK construction business.



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Q522 **Stephen Kerr:** What was the lesson learned? I am not clear in my mind. You had a "lessons learned" session as a board, in one of your meetings. What was the lesson learned about margin, then? You inferred there was a lesson learned.

Philip Green: I said that there were several lessons learned. We decided, over the course of the next few weeks, to withdraw from much or most of the Middle East. We decided to withdraw from certain markets in Canada. We decided to have a stronger central commercial function. We decided to take longer, where we should, to negotiate contracts. Those were all topics discussed.

Q523 **Stephen Kerr:** These would be margin protection measures, from the board's point of view?

Philip Green: Yes, because there were markets in the Middle East or in Canada where we were not making adequate returns.

Q524 **Stephen Kerr:** When the business is eventually capsized by three contracts and an outstanding payment, this is a complete failure of business planning on the part of the board, is it not?

Philip Green: I have said that the collapse is the responsibility of the chairman and the board, yes.

Q525 **Frank Field:** Before you said it was yours. You are rightly saying it is the whole board, is it not?

Philip Green: Yes, but as chairman of the board I take full responsibility.

Q526 **Stephen Kerr:** I have one more question, which is about contingency plans around payments. Specifically the £200 million Qatari debt has been referenced. I am confused as to why you were in a market where there was such complexity and such risk. Secondly, where were the contingency plans around recovering debts in any situation with disputed payments?

Richard Howson: In 2009, the group launched a new strategy: to halve the size of its construction business in the UK, which we did by 2013, and the result was negative capital outflow. In response to that, the group said it was going to double the size of the Middle Eastern business and the Canadian construction business, to offset the reduction, both to £1 billion from £500 million. £1 billion was coming out of UK construction; £500 million was being added to Canada construction, which I stopped in 2013; because I did not like the construction market; £500 million was being added in the Middle East.

How did we end up in Qatar? It was because the group strategy said we were going to expand into new countries. One of those new countries was Qatar; the other was Saudi Arabia. We only won, thankfully, one construction project in Qatar, which was Msheireb in 2011. It will finish at the end of this year. It should have taken two and a half years. The



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customers changed the architect three times. They issued 40,000 drawings within eight months. It has been a very difficult contract.

Q527 **Stephen Kerr:** Before you moved into that very complex commercial environment you must have done some research. As CEO, you must have.

Richard Howson: Yes, we had spent two years. We had a very small team doing market research and understanding who the right customers were. That contract for that customer was identified.

Q528 **Stephen Kerr:** Can you say a word on the contingency planning around outstanding payments?

Richard Howson: In my experience—and I did work in the Gulf for five years, so I have lived with this personally—the only way to ensure that you are paid reasonably in the Gulf is through personal relationships with your customers. There is no point writing nasty letters; there is no point appointing lawyers. It is about being there and the give and take of delivering and receiving cash. Msheireb changed its CEO in 2014, and we had better traction on cash flow once that new CEO was in. Sadly that stopped at the end of 2016, which was damaging.

Q529 **Heidi Allen:** I am interested in the wiggle room, day to day, that the company had, just to cope with day-to-day costs, suppliers, et cetera. Your working capital ratio has never been more than 1.1 since 2004. How is that a sensible way to operate? It strikes me that, for example, in the case of the Royal Liverpool Hospital, with the beams issue, you had no wiggle room. You had no means of dealing with that, because you were absolutely on your knees financially the whole time. I would argue, on that, that you can surely push back to the engineer who designed it and get some recompense that way. Talk to me—particularly Richard Howson and Philip, to start with—about whether you were comfortable working in an organisation that operated in this way.

Richard Howson: The headroom on the facilities decreased over time. You can see that from our financial results. Notwithstanding that, as we looked at the cash flows through each year, they were reasonable in respect of what I was anticipating and what we were anticipating as we were delivering those contracts. Certainly, during 2017, the non-payment on Msheireb, the emergence of problems with concrete beams on Liverpool causing delay and cost, and then the issues with Midland Metropolitan Hospital, where the building services design, which was delivered six months late and then did not work, adding additional cost, put pressure on that working capital.

Q530 **Heidi Allen:** Yes, but to be fair, as I say, 2004 was the last time you had anything vaguely approaching an acceptable cash ratio, so this is not just things that went wrong in 2017. Systematically, with the culture of the company, you were living on nothing. You cannot blame it on contracts that went wrong right at the very end. Going back through all of your time throughout the organisation, was the company run well?



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Richard Howson: The company was run well, in my opinion. There are lots of things I would do differently in hindsight.

Q531 **Heidi Allen:** Such as?

Richard Howson: I would not have bid on the Aberdeen Western Peripheral Route. I would not have joined the bidding consortia, given the losses on that.

Q532 **Frank Field:** Richard Adam, you were producing the figures for the board, over all this period of time. What responsibility do you think you have for presenting data that misled your colleagues, who just drove on, and then there was an almighty crash?

Richard Adam: I do not think I produced data that misled my colleagues. I think the financial data that was presented to the board was fulsome. I believe that it was reported in a very transparent and open way. The information that the board sought was always available.

Q533 **Heidi Allen:** You are not just there to provide information. You are there to give advice and do your duties as a director. Having 30 years, as you told us, of being an FD, did you think this was a responsible way to run an organisation, bearing in mind the duties that directors have under the Companies Act?

Richard Adam: I believe it was, based on the circumstances at the time and the events at the time. If you look at the funding of the group, it had £1.4 billion of funding available to it. Therefore, during my tenure, liquidity was available to the group.

Q534 **Heidi Allen:** Liquidity is not just about your ability to borrow. Let us not even get into the percentage of goodwill on the books. It is about the physical ins and outs of cash every day. I do not care how big or complicated your business gets; it is about whether a business can wash its own face. I do not believe this organisation could do this.

Can I come back to Richard Howson, and then Philip finally? I would like to hear more of your thoughts, Richard, on whether you think this business was well-run.

Richard Howson: The business, because of the markets it serves—support services and construction—was in very difficult sectors. It takes a lot of energy each and every day. Cash does not just come on construction projects from customers. It does not on support services contracts. It takes a lot of horsepower at all different levels to demonstrate you are cash-entitled and to get that cash into the group. There was £500 million coming in and out of Carillion every month. Probably 60% of my time was either on cash calls or, a lot of time, out and about around contracts collecting.

Q535 **Heidi Allen:** Was the chief executive doing that?

Richard Howson: Yes. Particularly in the Middle East and Canada.



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Q536 **Heidi Allen:** Philip?

Philip Green: Going back to your question, you used the expression, “wobble room”. If I understood you correctly, you were talking about lack of flexibility.

Q537 **Heidi Allen:** Sufficient funds coming in—we have not even got on to dividends yet—for the company not to be constantly relying on suppliers, for example, to be like a handy short-term loan to keep the business ticking over.

Philip Green: What I was trying to say was, if I had understood your expression, “wobble room”, correctly, I was going to agree with you, because I think coming into 2017, because of the level of debt, we clearly did not have the capability to easily withstand the knocks that we took. That goes back to the question I answered earlier on: what were the two or three reasons that brought us down? I think the first one was my understanding of what you mean by wobble room. We went into the year with too much debt. Management was focused on bringing it down. We had been given a forecast that it would come down. It did not come down. The four contracts then deteriorated rapidly, and because we did not have that wobble room, that was a very significant factor in the end result.

Q538 **Andrew Bowie:** Throughout all this time, Mr Adam, you were the finance director, and you oversaw, for example, the pension deficit grow by 348%. You oversaw the pension deficit grow from £13.8 million in 2007 to, when you left, £663 million. How much responsibility do you take personally for the amount of debt that Philip found himself having to manage?

Richard Adam: For my tenure in the business, I take total responsibility for the period that I was there. However, I add that at the time I was in the organisation, it had liquidity, it was operating successfully and had, in the terms of the discussion, adequate wobble room to deal with the shocks that it experienced in my tenure.

Q539 **Andrew Bowie:** As Heidi just said, it could barely wash its face sometimes, and year on year on year, under your tenure, you said it was okay. The debt grew—extraordinarily so, actually.

Richard Adam: I believe it had adequate liquidity. At the end of my tenure, the briefing papers you have had show gross debt approaching £700 million. It had on the balance sheet at that time just under £500 million of cash as well, and it had over £700 million of further facilities available to it. It had liquidity at that point in time.

Q540 **Frank Field:** Richard, are you a member of the company pension scheme?

Richard Adam: I asked to be a member when I joined the group, and I was not allowed because it had already closed to new members.



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Q541 **Frank Field:** When did it close to new members?

Richard Adam: I do not know what year before I joined. I do not know.

Q542 **Frank Field:** When did you join?

Richard Adam: 2007.

Q543 **Chair:** Mr Adam, in 2013 when you were CFO, Carillion signed up to the Prompt Payment Code for your suppliers. Do you feel you met the obligations of the Prompt Payment Code?

Richard Adam: I believe we attempted to do that, yes. We were asked in 2012 by, effectively, the then Prime Minister to look at putting in a supply chain finance programme. I think there was a meeting organised at Downing Street, which the chief executive was asked to go along to, and we then put in place those programmes that allowed us to comply, as far as possible, with the Prompt Payment Code.

Q544 **Chair:** How far were you complying with it, Mr Adam? When you stood down as CFO, what proportion of your subcontractors and suppliers were being paid within 60 days?

Richard Adam: I do not remember the exact number. In the earlier session somebody quoted between 40 and 50 days, but I do not recall.

Q545 **Chair:** You are the CFO, so I would have thought you might recall it. Mr Howson?

Richard Howson: We met our crown representative each quarter, and one of the key components of that meeting was to present our payment performance in the preceding quarter. We presented it in two halves: construction and support services. As Mrs Mercer said earlier, in construction, because of the regulation around construction, we paid on time, albeit through our early payment facility. Providers were being paid on either 30 or 45 days. Our issue was on about half a dozen contracts in the support services part of the business, and the issue was, as Mrs Mercer correctly identified, associated with change. Some of that change took up to 18 months for us to agree with our customer. In many instances, we paid suppliers in advance of being paid, but there were longer payment terms around change on support service contracts.

Q546 **Chair:** You do not recognise, then, what the FSB—the Federation of Small Businesses—says: that some suppliers were being made to wait 126 days to be paid as normal practice, and perhaps 10% of your suppliers had not been paid for four months' work?

Richard Howson: No. I do not recognise that. Not from the information which I presented to our crown representative every quarter.

Q547 **Chair:** Philip Green and Richard Adam, do you recognise that? You do not think that people were waiting 120 or 126 days for payment.

Richard Adam: No.



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Q548 **Chair:** Philip Green, were they under your chairmanship?

Philip Green: There may be a very rare example but, no, as a general principle or general comment, I do not recognise that.

Q549 **Chair:** When the FSB said that Carillion was notorious for being late payers, you do not recognise that, Mr Green, Mr Howson or Mr Adam.

Richard Howson: If that had been levied at Carillion in 2006, 2007 and 2008, when our payment terms were 65 days, I could recognise it, but not in recent years.

Chair: It was not levied then.

Q550 **Antoinette Sandbach:** Mr Adam, were you responsible, as the chief financial officer, for making the assessment in terms of the accounts in relation to goodwill.

Richard Adam: During my tenure, yes.

Q551 **Antoinette Sandbach:** Although the accounts were signed off by a different accounting officer—in other words, Mr Khan for 2016—all the detailed preparation would have been done while you were still CFO, in relation to the Carillion accounts.

Richard Adam: It would not for 2016, no.

Q552 **Antoinette Sandbach:** You were not working as the CFO until December 2016.

Richard Adam: I was, but the preparation of the audited accounts predominantly takes place in the period of January and February, leading up to the announcement of the results in March.

Q553 **Antoinette Sandbach:** Do you accept responsibility for the statement of goodwill in the previous years? You are saying you are not responsible for that assessment in the 2016 accounts, filed in 2017.

Richard Adam: Correct.

Q554 **Antoinette Sandbach:** Mr Green or Mr Adam, when you are making that assessment of goodwill, do you agree with the company's statement that your greatest asset is your people?

Richard Adam: Yes.

Q555 **Antoinette Sandbach:** Was that what you were taking into account when you were looking at goodwill?

Richard Adam: It was partly. As a technical accountant, what one has to do is look at the cash-generating ability of those businesses into the future. Then it is an arithmetic calculation that supports the value that is on the balance sheet.

Q556 **Antoinette Sandbach:** No write-down for impairment was made over the period that you were the chief financial officer for the company, in



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terms of goodwill.

Richard Adam: That is correct.

Q557 **Antoinette Sandbach:** There was no assessment, presumably, of the people who had come with your original purchases, which went back, in some cases, over 10 years, for example from Mowlem or McAlpine, who constructed part of that goodwill, about who was still in the company and who had left, thus damaging your goodwill.

Richard Adam: As I say, the calculation of goodwill has to have future projections for the business that generate enough cash to support the value. Clearly you need people to generate the business and the profit going forward, so that was an element, but it is an arithmetic process, which would be reported to the board, reviewed by the auditors and signed off.

Q558 **Antoinette Sandbach:** Was it not a concern? Basically, your auditor's evidence to us is that the workforce and synergies were effectively the goodwill in your companies. Why was there no impairment over a substantial period of time, given that the Insolvency Service has said to us that you did not even have a complete list of directors for all the companies that you or the group were responsible for?

Richard Adam: As I have said, the process in looking at the value of goodwill is at each period end.

Q559 **Antoinette Sandbach:** I am asking specifically about the workforce. I would like you to address that, please.

Richard Adam: As a function of the cash-generating units, clearly people are necessary. They are a fundamental part.

Q560 **Antoinette Sandbach:** Do you accept the Insolvency Service's evidence that Carillion did not have a complete list of all the directors of the subsidiary companies?

Richard Adam: I cannot comment on that. I left the business at the end of 2016. I was not there when they looked at it.

Q561 **Antoinette Sandbach:** You are saying that the records will show that, when you were the CFO, you had that understanding of who comprised the workforce and you did have that complete list. Is that what you are saying?

Richard Adam: I am not saying that, because I do not think the names of the directors would have been the principal factor in looking at the value of goodwill. Did we, during my tenure, have statistics from human resources of the numbers of people who we had in each business? Absolutely we did. A very sophisticated HR system allowed us to have that data.

Q562 **Antoinette Sandbach:** Mr Green, in relation to the rescue plan delivered by the Carillion board on 3 January 2018, do you accept that these key



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issues were identified: that there was insufficient understanding of, and adherence to, contract requirements; that success on construction contracts depended on the performance of others not under your control; that the increasing size and complexity of services contracts, compounded by growth, was not matched by your capability; that contracts were taken on with a high degree of uncertainty around key assumptions; that claims were not pursued in a timely and effective manner; that the portfolio was not balanced in terms of cash generation; that there was ineffective change control, e.g. design changes on construction contracts, agreed without incurring incremental costs; that there was poor planning and lack of effective contract controls and monitoring, leading to inconsistent operational performance management; that there was a lack of ownership of issues; that there was geographic risk; and that there was a lack of effective handover from bid to mobilisation to delivery, leading to a lack of knowledge transfer. Do you accept those were the key risks, themes and issues identified by the board in January?

Philip Green: Some of them I recognise and some of them I do not—lack of ownership of issues, as an example. Of course there was geographic risk and we have said we were trying to reduce the geographic risk.

Q563 **Frank Field:** As you accept your responsibility to the board, do you think the Government should rule that none of you is a fit and proper person to serve on companies?

Philip Green: No, I do not. I believe that all of the board, including myself—I speak on my own behalf—believed in every decision we took at the time we took it. We believed it was right and we had surrounded ourselves with quality advisers.

Q564 **Frank Field:** You should all be let loose on other companies.

Philip Green: With hindsight, if we look back, of course there are decisions we would take differently.

Q565 **Antoinette Sandbach:** Mr Green, those issues were identified by you when you were chairman of the board and were presented as part of the board rescue plan. Either you were misleading people by identifying those risks or those were the risks that had been identified and they were not risks that had only appeared since March 2017, were they?

Philip Green: No, the geographic risk that I mentioned had been there for a long time. We were attempting to deal with it by bringing ourselves back to the UK, as an example.

Q566 **Antoinette Sandbach:** In terms of the way that all of you acted as directors, with your requirement under Section 172 of the Companies Act to act in the long-term interest of the company, how is it that one of the issues established by Mr Cochrane and the changed board was that Carillion had an overly short-term focus, and that it had weak operational



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risk management and too many distractions outside the core?

Philip Green: As he said, when he became chief executive he developed a very different view to what he had as an executive.³

Q567 **Antoinette Sandbach:** Mr Howson, that is your legacy, is it not?

Richard Howson: I do not necessarily agree with all of Keith's points, but he had a different perspective from me. I recognise the points that you read out from Philip's statement in July, and they came from the risk review of the major contracts that we presented to the board in May. We made all of those errors on various contracts. We were delivering 300 or 400 contracts at any moment in time, and some of those errors, yes, we were delivering.

Antoinette Sandbach: Some 14% of them were at risk; 14% of those contracts were in debt.

Richard Howson: Yes, they were, because of the nature of contracting, as I illustrated earlier with Crossrail. I would like to illustrate at some point the nature of risks that materialise on some core service contracts, if I get the opportunity. That needs managing into the long term.

Q568 **Antoinette Sandbach:** I would like to ask Mr Adam, because this is the legacy. In 2015, concerns were expressed about the audited accounts, the transparency and the openness that you claimed were values of the board, which were required changes. The FRC required the board to make changes. Why had you not identified those concerns, as the chief financial officer?

Richard Adam: I would like to put that process into context. The FRC now regularly reviews the annual reports of all companies. That was a regular review. Over a period of time, all public companies will have reviews of that nature. The matters raised were ones of disclosure, and my successor put the relative disclosure matters into the next set of annual reports. It was not an unusual or an exceptional process. The FRC had not picked out Carillion for any particular reason; it was part of their normal cycle of work.

Q569 **Chair:** Can I ask which of you, if any, are executive directors or non-executive directors on other boards?

Richard Adam: Yes, I am.

Q570 **Chair:** Can you tell us which ones?

Richard Adam: I am currently a non-executive director of Countrywide PLC and I am coming off that board—

Q571 **Frank Field:** Tell us about the other ones. You are on it now, are you not?

³ Mr Green subsequently clarified that he intended to say: "As he said, when he became chief executive he developed a very different view to what he had as a non-executive."



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Richard Adam: I am on Countrywide now.

Q572 **Frank Field:** Are there any others?

Richard Adam: There are no others at the moment.

Q573 **Chair:** Which one are you going on to?

Richard Adam: That is the only one.

Q574 **Chris Stephens:** My first question is for Mr Green. You have talked about the board relationship, challenging decisions and that the board were fit and proper people, and yet the board appears to have repeatedly ignored requests from the pension trustees for higher deficit recovery plans to plug the deficit. Can you tell me why the board prioritised dividend payments and share price over the pensions of 28,000 members?

Philip Green: Colleagues have already said that our commitment was to meet our obligation to the trustees—our £50 million a year—which is what we did. We were then going into another three-year review. When we looked at the business in the round, there were a number of stakeholders. Shareholders and pension trustees are two groups; we did not consciously prioritise them. Our business plan for 2017 allowed us to reduce debt, to meet our pension obligations and to meet the dividend.

Q575 **Chris Stephens:** People watching these proceedings, Mr Green, will be confused and will ask for a justification as to why there was a 15-year deficit recovery plan for the pension, at the same time as the company was paying generous dividends and bonuses.

Philip Green: All I can say is the agreement was reached with the trustees, and then our commitment was to meet that obligation.

Q576 **Chris Stephens:** Could you tell me, Mr Green, how a deficit could be plugged with falling total contributions? I am looking at the pension contributions. In 2014, it was £58.5 million. It was then reduced in 2015 to £54.3 million. In 2016, it was £51.6 million, and yet the dividends for those three years increased. How can the deficit be plugged with falling total pension contributions?

Philip Green: The pension contribution was approximately £50 million per year and that was our obligation.

Q577 **Chris Stephens:** You say that was your obligation. Is it not the case, as Robin Ellison said to the Committee last week, that recovery plans were never agreed, but were imposed? Is that not a fair reflection on the relationship between the board and the pension trustees?

Philip Green: In that same interview, Mr Ellison also said that the ratio of our pension contribution to the dividend was actually a lot higher than average.

Q578 **Chris Stephens:** Can I ask Mr Adam to confirm that the pension trustees



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wrote to you on 25 January 2012, drawing key conclusions from a report that they received from yourself? Do you remember that?

Richard Adam: I do not remember the detail of it, but I am sure that is correct.

Q579 **Chris Stephens:** Do you recall that the pension trustees were looking for £67 million in 2014, per annum, to help their pension deficit recovery plan?

Richard Adam: I recall that they asked for sums of that size.

Q580 **Chris Stephens:** Mr Adam, would there be any reason why the competitors of Carillion have shorter pension debt recovery plans than Carillion? Some of them are less than 10 years; some of them are five years. Why would Carillion have a 15-year deficit recovery plan for its pension?

Richard Adam: I do not know the details of competitors of Carillion. I felt the arrangements with the trustees were cordial. Over a period of time, the contributions were agreed between the company and the trustees.

Q581 **Chris Stephens:** Can you confirm to me, Mr Adam, that the Pensions Regulator did not intervene in relation to how the company was tackling its deficit recovery plan? Was this a surprise to you?

Richard Adam: I felt that we had a good relationship with the Pensions Regulator. We had some meetings with them around the valuations and my recollection is that, following the last valuation, we had recommended or suggested to the regulator that it would be useful to have quarterly meetings to update them on the company's progress.

Q582 **Chris Stephens:** Mr Green, could you confirm to me that, by May 2017, discussions with the trustees were such that, in their view, no plan was affordable to the company or acceptable to the trustees for the pension scheme, and that the pension scheme was now a major problem?

Philip Green: I was not aware of a particular conversation in May 2017. I do not recall that.

Q583 **Chris Stephens:** Did you have any dealings with the Pensions Regulator, as the chair of the board?

Philip Green: No.

Q584 **Chris Stephens:** Mr Green, can you confirm that there was a pension sub-committee set up in 2015?

Philip Green: Yes.

Q585 **Chris Stephens:** That was chaired by Mr Howson. Mr Howson, can you tell us how many times that sub-committee met?

Richard Howson: It met each quarter.



Q586 **Chris Stephens:** What was actually discussed at these sub-committees?

Richard Howson: The meetings lasted about an hour and a half, and we went through various subjects. We received a report on meetings during the period with the trustees and the Pensions Regulator. We obviously looked at the deficit and whether it had moved. We looked at opportunities to potentially de-risk the pension deficit or the pension scheme, so things like the mortality swap that we put in place in 2013. We also reviewed adding resources to our in-house pension team so, as the deficit was rising, we could better understand and model ourselves, rather than relying on consultants, opportunities to prevent that rise or de-risk that rise. Those were the general areas that we looked at.

Q587 **Frank Field:** Richard Adam, you present to us a picture that the pension trustees did not present to us. It was all a rather good relationship you had with them. They presented to us that you imposed your will on them. Can you give us any example where they persuaded you to change your policy to the pension scheme?

Richard Adam: I think the clear evidence of that is that, in my tenure, the deficit contributions were increased by about 50%. Clearly the trustees were a major factor, in terms of the increase in those contributions.

Q588 **Frank Field:** Did you ever discuss with them that you might cast the pension scheme adrift from the company?

Richard Adam: I am not aware of that.

Q589 **Antoinette Sandbach:** In relation to contract write-downs, Mr Howson, you said that the contract had stopped at the end of 2016, because of lack of payment.

Richard Howson: Which contract?

Antoinette Sandbach: The Qatar contract. We will check the evidence.

Richard Howson: If I did say that, it is not correct.

Q590 **Antoinette Sandbach:** I have a note of that, but you did say that, in the Middle East, you had only won one contract. Is that right?

Richard Howson: No. Part of the expansion strategy was to expand into Qatar in 2009. We won that contract in 2011. It is the only contract we won in Qatar in construction.

Q591 **Antoinette Sandbach:** Your auditors did a number of site visits, including to Canada, which you subsequently reported issues for, and indeed to the Middle East. Did they go to Qatar?

Richard Howson: Yes.

Q592 **Antoinette Sandbach:** Your auditors should have been aware, for example, of the 40,000 design changes.



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Richard Howson: 40,000 new drawings.

Antoinette Sandbach: Yes, and the two changes of architects. They were aware of those issues.

Richard Howson: I personally discussed it with the auditors, year on year.

Q593 **Antoinette Sandbach:** You personally discussed it with the auditors, year on year. You were aware when the accounts were signed off on 1 March 2017 that there was £180 million outstanding on that contract, but no provision was made in your accounts or the audited accounts in relation to that contract.

Richard Howson: A significant proportion of that value came from a claim. I had personally settled claims 1 and 2, in July of 2016, with the Chief Executive of Msheireb Properties. Those claims had been lodged, working from memory, 18 months earlier than I settled them.

Q594 **Antoinette Sandbach:** Can I just ask if your auditors, because they had been out and inspected that project, were aware that there were claims that had been outstanding from 18 months before, which had been lodged but not paid?

Richard Howson: I agreed those claims, as I said earlier, in July 2016, through negotiation. The cash flowed in August or September, and we felt far more confident about the project at that point. The project would have finished, had we continued to be paid, by May 2017. In order to finish, we had to settle our claims 3 and 4, which took us from September 2013 to January 2014. A significant proportion of the value was in the number that you quoted earlier.

Q595 **Frank Field:** The auditors, in a sense, told the public you are alright as a company, did they not?

Richard Howson: My team and I were negotiating that claim day in, day out.

Q596 **Frank Field:** That is not the question we asked. The auditors still gave to the public the notice that this was the final report. You got a bit of help from them, did you not?

Richard Howson: The claim was valid.

Q597 **Frank Field:** They were plodding around, you have told Antoinette, looking at the project and you were telling them, "They are not paying us".

Richard Howson: Claims take time to resolve.

Q598 **Antoinette Sandbach:** Had they not appeared in the accounts for 2013, because you said this was a 2013-14 claim? It was only effectively declared in your profit warning in July 2017.



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Richard Howson: The reason why—

Antoinette Sandbach: I do not need the reason. Is that factually correct?

Richard Howson: No, because the reason I decided to make a provision against Msheireb in June 2017, announcing the profit warning, was because Msheireb Properties, in June 2017, elected to appoint a third-party contractor to complete the works, which we disagreed with, at our cost.

Q599 **Antoinette Sandbach:** In relation to the Canada inspections, were there any indications about how much of your write-down related to your Canada operations?

Richard Howson: The Canadian provision was, in the main, relative to two railway station contracts, one from 2008 that finished in 2017, and one from 2010 that finished in 2017.

Q600 **Heidi Allen:** Before I ask my question, can I just check who ultimately was responsible for saying, "Yes, they are the dividends we are going to pay"?

Richard Howson: It was the board.

Heidi Allen: It was a collective decision.

Richard Howson: The way it worked is we produced a draft dividend proposal in the January or the June board meeting.

Heidi Allen: I just mean generally.

Richard Howson: And then it was approved in February.

Q601 **Heidi Allen:** Did each of you in front of us today have a say in that, yourself included, Alison, and Richard too?

Philip Green: Yes.

Richard Adam: Yes.

Alison Horner: Yes.

Q602 **Heidi Allen:** Yes. So accepting what you are telling us about the construction industry being different from others and that cash can be very much up and down, if I look back through 2009 to 2016, cash coming in could be at a height £313 million. I am guessing that is perhaps harking back to the PFIs, is it, when, as you say, the good times rolled? That was 2010. At worst, it dropped in 2013 to a loss of £62 million, so the cash was really all over the place.

Yet that particular year, 2013, when cash was at its lowest, negative £62 million income, was the highest percentage of dividends paid. That year, the worst cash income year, was the highest dividend, 70% of profit. Even when a bit more cash came in the following year, 2014, it is still significantly lower than it had been previously. Throughout the entire



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period from 2009, right the way through, every single year we see dividends going up and up and up. Can each of you tell me if that was a responsible decision to take? Was it the right decision to take, given that the debt was increasing and the pension deficit was also increasing? I will start with Richard Adam, please.

Richard Adam: The two years that you quite rightly identify when cash flow did not cover dividends were 2012 and 2013.

Q603 **Heidi Allen:** Cash should not just cover dividends. In a healthy business, cash should also cover debt, debt interest, suppliers and everything else.

Richard Adam: I agree. The cash flow characteristics of 2012 and 2013 were a direct consequence of the strategic decision to effectively halve the size of that UK construction business, which we took after the credit crunch into the recession. The Government cut infrastructure spend at that point by 30% and, therefore, we decided we would shrink the UK construction business to de-risk the group. When you do that, you get an outflow of cash, because with construction you get paid some cash up front. If you are reducing your volumes you are going to have an outflow.

Q604 **Heidi Allen:** Are there not other things you could have done with the cash than just more and more dividends?

Richard Adam: In terms of the dividend profile, we were balancing the needs of many stakeholders. We had pensioners; we had staff; we had shareholders.

Q605 **Heidi Allen:** I disagree with that. I do not remotely see how you were balancing the needs of pension-holders, actually. They were the very last people you were thinking about.

Richard Adam: Perhaps "balance" was the wrong word. We were taking into consideration a number of stakeholders. If you look at the statistics, in the last five years of my tenure, we only increased dividends by 12%. As I said earlier, in that period we added 50% to the pension deficit payments.

Q606 **Heidi Allen:** You were mostly using debt to pay for that. Your rivals, Costain, for example, recognising in 2014 the same difficulties in the construction market, opted to raise equity rather than debt. You have always, every single time, gone for debt and not paying your pension deficit duties to be able to continue rising dividends. Shall I move on to Richard Howson and your view on the dividend culture in the organisation?

Richard Howson: In 2016, I think the cash from operations number is wrong. I think it was £115 million, not minus £38 million. Can we clarify that after the meeting, please, Chairman? The way I thought about this was twofold. First, we had no growth in our profitability. In fact, our profitability was reducing in 2012 and 2013, because we had acquired



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Eaga and the first 18 months of my tenure was demobilising Eaga and trying to make a good fist of the Green Deal, so markets were very challenging. We felt at the time that we should show some confidence in the future by slightly increasing the dividend. I very much remember those decisions, as a board. They were big decisions, especially given the cash flow in 2012 and 2013, as you see here.

In subsequent years, the way I thought about this—and it is the way we communicated it in the risk register—is that we had to win work. We did not have any money to buy competitors, as we had done in the past. We had to win our work organically. We had to bid and we had to win, because future cash flows are, in my mind, more important than the deficit contribution.

Heidi Allen: But that is jam tomorrow, is it not? You can only do that for so long.

Richard Howson: No, it is not. Those are the future cash flows that the pension is absolutely dependent upon, which is why winning work is first and foremost in our risk register, delivering it is second and pension is third. That is the way I thought about it

Q607 **Peter Kyle:** It is like a Ponzi scheme. It got to the point that you were bringing in money to subsidise work that was not profitable. It is a Ponzi scheme.

Richard Howson: No, we were bidding for quality work for the British Government and for quality private sector organisations in the UK. We were pulling out of construction in Canada and reducing our construction effort in the Middle East. We were honing back to better-quality customers.

Q608 **Peter Kyle:** All the things you have described were not profitable. You were bringing in new business to try to subsidise the unprofitable ones. It was cash flow. You did not have the money, so you were bringing in whatever it took—any business, any contract—to bring in cash to keep the operation going.

Richard Howson: That is absolutely not true.

Q609 **Peter Kyle:** Why did it fail then?

Richard Howson: You can probably tell from some of the contracts that I have commented on that they are from the long term and from a long time ago. They have been very challenging. We have won some very high-quality work and, as I said at the start in my introduction, the majority of Carillion's contracts are very profitable, with a high degree of customer and supplier satisfaction. We are talking about a small number here, so I cannot take your blanket allegation.

Q610 **Heidi Allen:** Can you all understand how it appears to the average person in the street that an organisation such as yours is making losses,



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very low if no margins and yet the dividends continue to rise? What was the relationship between members of the board's bonuses and their remuneration packages? I appreciate that we are going to come on to remuneration later, but was there any connection there in terms of the reason to vote for higher dividends?

Richard Howson: No, there was no link.

Q611 **Chair:** Mr Howson, when you left the business in July of last year, what was your total remuneration when you finished?

Richard Howson: My earnings were £660,000. That was my basic salary.

Q612 **Chair:** What was your total remuneration?

Richard Howson: I had £28,000 of benefits, £132,000 of pension contributions plus variable pay.

Q613 **Chair:** What was your total remuneration?

Richard Howson: In 2016, it was reported as £1.5 million.

Q614 **Chair:** What was it the year before that?

Richard Howson: I do not know—something like £1.1 million or £1.2 million.

Q615 **Chair:** £1.283 million. What was it the year before that?

Richard Howson: I would have to look in the annual report.

Q616 **Chair:** It was just over £1 million. In two years, your total remuneration increased by 50%. What did you do to earn that increase in salary, Mr Howson?

Richard Howson: The jump in my remuneration in 2016 was as a result of the vesting of LEAP awards, relative to 2014, of just over £500,000. Those LEAP shares did not actually vest in 2016. I received them towards the end of October 2017. Did I receive £1.5 million in 2016? No, but technically those shares will have vested. We were in a closed period, so I did not receive them. My true earnings were around £1 million.

Q617 **Frank Field:** Did you ever get them and sell them?

Richard Howson: I got them at the end of October 2017 and I sold them at the end of November 2017.

Frank Field: So they were part of that package.

Richard Howson: Yes, they were.

Q618 **Chair:** Your total package, in your last year working for the business, was £1.5 million, about 50% higher than it was two years before. Alison Horner, you were chair of the remuneration committee. Why did you



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increase the total remuneration for the chief executive by 50%? What had he done to deserve that increase?

Alison Horner: We increased Richard's basic salary in 2015 and 2016. When he was appointed, his salary was £560,000 and, having done the job for three years, assisted by our remuneration advisers we benchmarked him in the market and he was below median. It was Carillion's policy to pay median, which is essentially mid-table. At the time, we believed Richard was doing a good job, so we took a proposal to shareholders, consulted with many, including BlackRock and Legal & General, and we increased his pay by 8% in 2015 and 9% in 2016.

Q619 **Chair:** What happened to the market capitalisation of Carillion during that period, Ms Horner?

Alison Horner: I cannot give the exact number.

Q620 **Chair:** What roughly happened to the share price?

Alison Horner: The share price was reducing over that period.

Q621 **Chair:** By about how much?

Alison Horner: I do not know.

Q622 **Chair:** Do you think that the chief executive should be rewarded at a time when the value of the business is deteriorating quite sharply?

Alison Horner: As I say, we consulted with the shareholders.

Q623 **Chair:** Yes, but I am asking you. There is a lot of consultation that this business does but, in the end, people like you, Ms Horner, are making decisions. I am asking whether you think it is justified and right, at a time when the share price of the company is falling quite substantially, to increase the remuneration of the chief executive by 50%.

Alison Horner: We felt that it was right at the time, because we wanted to retain Richard Howson as chief executive in that business, at a period when the sector was volatile.

Q624 **Chair:** With the benefit of hindsight, Ms Horner, do you think that those decisions were right?

Alison Horner: I have thought a lot about many of the decisions that we have made and I think that decision, in terms of increasing his pay, was correct.

Q625 **Chair:** You think that, in 2016, the chief executive deserved that.

Alison Horner: The award was made in January 2016, on the back of consulting with shareholders in 2015.

Q626 **Chair:** You have already said that, Ms Horner. I am asking you, with the benefit of hindsight, whether you think a total reward of £1.5 million, when we have heard a huge amount of evidence today about what was



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happening to the business, was justified.

Alison Horner: I completely understand the anger that people will feel about the pay that has been made to executives. In my role on the remuneration committee, I have to balance many factors, including the market and the advice we get.

Q627 **Chair:** You have already said that, Ms Horner, and I heard. I am asking, with the benefit of hindsight, whether you think that that pay packet was justified.

Alison Horner: With the benefit of hindsight, we may have looked harder at some of the elements of variable remuneration. While they were paid against targets that were met, the committee could have considered downward discretion in respect of the overall financial performance of the business.

Q628 **Chair:** While you were chair of the remuneration committee, both the chief executive officer and the chief financial officer were sacked. When they were sacked, what happened to their pay?

Alison Horner: Under the terms of their contract, both were entitled to pay in lieu of their notice for 12 months. Custom and practice in Carillion was that that was paid as a lump sum. The remuneration committee demanded that those payments were made monthly so, in the event that we discovered anything through our investigations, we would be able to suspend the payments. When the company went into liquidation, those payments were suspended. To correct what was said earlier about Zafar, he would have received four and a half months of the 12 months' notice due to him.

Q629 **Chair:** What would Richard Howson have received?

Alison Horner: Richard Howson would have received a similar proportion, around a third.

Q630 **Frank Field:** Does the remuneration committee set the rewards for the whole board?

Alison Horner: The remuneration committee sets the rewards for the executive directors and the fees for the non-executive directors.

Q631 **Frank Field:** Who recommended that you should come on to the board?

Alison Horner: There was a search process to recruit new non-executive directors. A head-hunter was commissioned. They were specifically looking for people who had skills in respect of remuneration, and I went through that process alongside others.

Q632 **Chair:** Can I ask Philip Green what your remuneration was in your final year?

Philip Green: It was £220,000.

Q633 **Chair:** What was it the year before that?



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Philip Green: I do not recollect. It was approximately £210,000.

Q634 **Chair:** What was it the year before that?

Philip Green: It was approximately £190,000.

Q635 **Chair:** Your pay increased not by 50% in two years, but probably by about 30% in two years. Is that about right?

Philip Green: No, I do not believe it is, actually. I had one adjustment of 9%, I believe.

Chair: I believe your fee was £147,000 in 2014.

Philip Green: That would not be a full year, because it was around the time that I became chairman.

Q636 **Chair:** You had two pay increases, so about 20%. Did you have a 9% and an 11% pay rise?

Philip Green: I do not believe so.

Q637 **Chair:** Maybe Alison Horner can shed some light on it.

Alison Horner: We made one increase to the chairman's pay. His fees increased from £193,000 to £215,000.

Q638 **Chair:** Do you think that that pay increase was justified, Ms Horner?

Alison Horner: Clearly in hindsight the same challenge applies to that as Richard Howson, but at the time, based on market benchmarks and our remuneration advice, yes. We believed it was at the time.

Q639 **Chair:** Can I ask about the clawback arrangements? When and why was a decision taken to change the rules on clawback of bonuses, Ms Horner?

Alison Horner: We introduced new arrangements for clawback of cash paid and vested shares in response to the 2014 Corporate Governance Code. Those changes were introduced in February 2015, alongside increasing the holding period for shares awarded on our long-term incentive plan by two years.

Q640 **Frank Field:** What was the reason for that?

Alison Horner: It was in response to the Corporate Governance Code. Again, we took advice, both legal and remuneration. Alongside 80% of the FTSE, we introduced two new conditions for clawing back cash and shares, which were misconduct and misstatement.

Q641 **Chair:** The Institute of Directors and the FRC both criticised Carillion for the change in the clawback arrangements. Do you think that is a fair criticism, Ms Horner?

Alison Horner: I would argue that it was not. We made it easier, not harder, to claw back. Specifically in respect of cash paid and shares vested, such as Richard Adam described on his leaving arrangements,



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those payments are available for the official receiver to consider through those clawback arrangements. In the event of corporate failure, do not forget that any share held or deferred is lost in any case, through the liquidation.

Frank Field: Did you ever propose any cuts? We have been in an economy where most working people have suffered real cuts in their rewards. Did the remuneration committee ever propose any changes that disadvantaged the members of the board that you had stewardship for, over pay?

Alison Horner: We never made a payment that was not justified through contract or through target. As I said in my previous answer, we had an opportunity to apply potentially negative discretion to variable awards that are made for non-financial measures.

Q642 **Frank Field:** Philip Green's increases, which were way above what everybody else was getting in pay, you had to award.

Alison Horner: You do not have to award it, but our policy was to.

Q643 **Frank Field:** My question to you was whether you ever suggested cutting pay?

Alison Horner: We did not suggest cutting pay.

Frank Field: When everybody working for Carillion would have suffered cuts.

Q644 **Chair:** Can I come back to this clawback issue? In 2016, Richard Howson was paid a bonus of £245,000. Richard Adam, I believe, was paid a bonus of £140,000. In the previous year, Richard Howson was paid a bonus of £293,000, and Richard Adam of £215,000. What are the prospects of those bonuses being clawed back? Do you expect any of your bonuses to be clawed back?

Richard Howson: I know there will be a review of whether those bonuses were properly paid, in line with processes. If the outcome of that review says that the bonuses should be paid back to whatever extent, then I will abide by that decision.

Richard Adam: I am not looking to avoid any responsibilities that I have and I am happy to engage with the representatives from the company regarding that matter.

Q645 **Chair:** At the beginning, Richard Adam, the first thing you said—in fact, the first thing all of you said—was how sorry you were and how saddened and distressed you were about the collapse of a company that you oversaw for a long period of time. Do you think that you should give your bonuses back, Mr Howson?

Richard Howson: Bonuses were rewarded for specific things within the rules of the remuneration committee. The awards that have been made have to be reviewed within those rules. If, as I said earlier, it is proven



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that perhaps they should not have been paid, then I will abide by that decision.

Q646 **Chair:** Do you feel comfortable with the level of bonus that you received in the year before the company that you ran collapsed?

Richard Howson: Yes, I do, for the attributes that I earned it for. Half of that bonus is deferred and half of it was paid in cash. Half of it I have lost.

Frank Field: Richard Adam, how do you reply to Rachel's question?

Richard Adam: Could you repeat the question?

Q647 **Chair:** Do you think that you should give the bonus back, and do you think that that bonus in 2016, a year before the company collapsed, was justified?

Richard Adam: As I have said, I am not looking to avoid any responsibilities.

Chair: That was not my question, Mr Adam. You already answered that question.

Richard Adam: I will engage with the company.

Chair: You do not think you should give the bonus back, or do you think you should give the bonus back?

Richard Adam: I need to understand the position. I have been out of this business for over a year. I have had no access to documentation and I do not actually know what the position is today.

Chair: Somebody who has contributed and has worked for the business, say for your period of time, Richard Howson, for 22 years, who every year paid into their pension scheme and now is coming to retirement, will find that their pension will be cut by 10%, not because of anything that they did but because of what you four, the three people who came to us before and the other people who ran this business did. They are not sitting at this table. They do not have a chance to express how saddened and disappointed they are, but they are giving up 10% of their pension. They have to.

All of you are sitting here, with multi-millions of pounds' worth of payment from the company over a period of years, and you say how sad and disappointed you are, but what actions do you take to show that? They are just words, are they not? They are just words: "I am saddened. I am disappointed. I wish I could have done things differently", but the money is in the bank. It is not in the bank for the subcontractors, is it? It is not in the bank for the people who have retired or are coming up to retirement. Instead of words, why do you not actually do something? Why do you not give some money back and try to make a difference, and try to put right some of this wrong.



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Q648 **Frank Field:** Can I put it another way? You have opened up very effectively about how sorry you were, but it does not seem to me that the sorrow leads, as Rachel says, to any way of you putting money back. All four of you have done really rather well out of a company that you then, in different ways, helped to crash. Richard Adam, does that not move you at all? Why should we believe that you feel so sad about all of this, when it does not extend to your chequebook?

Richard Adam: I am genuinely shocked and saddened by the events since I left. I genuinely am. I am very happy to engage with the company and understand what the position is.

Q649 **Frank Field:** Do you not think that your moral actions mean you do not have to wait for somebody to have an engagement with you? It is part of your DNA, is it not?

Richard Adam: It is, but I need to understand what the position is. I do not know what the position is today.

Frank Field: I think it is quite clear, is it not? As Rachel said, pensions are taking cuts. Large numbers of people are not going to be paid for their contracts. Other people have lost their jobs and you are still alright, all of you, are you not? Do any of you want to say anything before I thank you and close the meeting? You walk away and we will be doing a report. Thank you very much for coming today.