



Rt Hon Greg Clark

22 May 2019

Secretary of State,

BRITISH STEEL FINANCIAL SUPPORT

This letter summarises the advice we have provided to you, respecting commercial confidentiality and legal privilege.

Over the last few weeks and following extensive meetings between you and all relevant stakeholders, we have examined numerous ways in which we might provide financial support to British Steel Limited (BSL). You have made strenuous efforts to examine all the options and challenged us to find a solution. This advice is our official assessment, incorporating external professional advice.

Having carefully considered a range of evidence, including independent assessments that we have received from our financial advisers, and despite extensive efforts to find further evidence, we still cannot demonstrate the necessary commerciality required by State aid law to provide such support. There is no evidence of sufficient funding to bridge to a sale, nor sufficient collateral value, nor a 'super senior' security position ahead of other creditors, nor sufficient evidence of market participants willing to invest alongside HMG. Neither our analysis nor the independent views we have received have given sufficient confidence that a market operator would be willing to make a similar investment to HMG.

To be clear, this advice holds for all options that we have examined or that have been discussed with the company and the stakeholders over the last few weeks. This includes the options where the shareholder was prepared to offer some level of funding and the option of whole or partial nationalisation of the company whether temporarily or permanently. Our official advice, incorporating external professional advice and based on current cash flow forecasts and available security, is that there is no evidence that any earlier funding options involving Government would have been lawful either. You have been provided with legal advice on providing liquidity loans to BSL which is subject to legal privilege.

It would be unlawful to provide a guarantee or loan on the terms of any of the proposals that the company or any other party has made, or any others we have considered. You must note that such an offer cannot be made legally, and that by making it you would be in breach of the Ministerial Code. Moreover, we do not believe there is currently any

level of investment Government could make (above the State Aid *de minimis* of €200,000) that could be deemed commercial and so legal.

At your request, officials met with the independent Industrial Development Advisory Board (IDAB) yesterday further to test the commerciality of the latest proposition to provide a loan to help fund an administration process, IDAB has confirmed that they agree with the assessment undertaken by our financial advisers that the loan is not demonstrably commercial.

It is worth noting the particularities of the steel sector. Rescue and restructuring aid is uniquely incapable of being provided for companies in the steel sector. Government must therefore be satisfied that any support must be on commercial terms.

We wanted also to record the efforts that have gone into trying to establish commerciality in recent weeks. Led by you, officials have been working with British Steel, its lenders, and its stakeholders since 28 February to explore routes to provide financial support. Initially this support was focused on providing a loan to assist with the liquidity shortfall created by the crystallisation of the EU ETS compliance requirement. Several different mechanisms to provide support were explored but it was not possible to find a traditional loan financing that would be deemed to be sufficiently commercial to meet the state aid commerciality threshold.

The Deed of Forfeiture structure of the EU ETS support was predicated on sufficient security being provided by the future EU ETS credits, a market comparable interest rate, comfort over the likelihood of the future provision of carbon credits to enable repayment, protections to ensure repayment on insolvency, underwriting of potential future downwards price movements and a 50% share of any potential future pricing upside as well as payment of the department's advisory costs. Unlike the initial loan proposition, an independent report confirmed that the Deed of Forfeiture structure was on arms length commercial terms and therefore was permissible under state aid rules.

On 15 April British Steel requested a further loan to cover liquidity shortfalls in the business as a result of adverse trading. Government officials reiterated to management that any liquidity loan would need to be on demonstrably commercial terms and the relatively worse level of security available compared with the Deed of Forfeiture would require it to have materially improved terms.

In the absence of the company, its shareholder, or its advisers being able to propose options to achieve commerciality, officials provided stakeholders with a 'strawman' setting out the parameters of what commercial terms and contributions from all parties would need to be in order to be demonstrably commercial.

Asset Backed Lenders and BSL proposed amended terms on 11 May and our financial advisers provided initial analysis that highlighted that these terms did not reach the parameters and provided no evidence that commerciality could be met. Discussions continued between the parties and BEIS wrote again highlighting that the shareholder needed to be a part of the solution to establish a commercial agreement.

The proposals received from the shareholder on 17 May did not come close to the parameters outlined to enable a proposal to be commercial. Furthermore, they did not deliver sufficient funding to support the delivery of a sales process or restructuring, unlock sufficient security

to give certainty of repayment (including under insolvency) and provide adequate security to give robust asset coverage.

We have received a number of other approaches of varying degrees of credibility and with different conditions attached. We have evaluated each of these and none of them changes this assessment or our advice.

Accounting Officer