Business, Energy and Industrial Strategy Committee & Work and Pensions Committee

Oral evidence: Carillion, HC 769

Tuesday 30 January 2018

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Watch the meeting

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

Questions 1-217

Witnesses

I: Sarah Albon, Chief Executive Officer, The Insolvency Service and Stephen Haddrill, Chief Executive Officer, Financial Reporting Council.

II: Chris Martin, Managing Director, Independent Trustee Services Ltd and Robin Ellison, Chair of the Trustees of Carillion Defined Benefit Pension Scheme.
Examination of witnesses

Witnesses: Sarah Albon and Stephen Haddrill.

Q1 **Chair:** Thank you very much for coming to give evidence on the collapse of Carillion to our two Select Committees this morning. I will start by asking both of you, the FRC and The Insolvency Service, to provide us briefly with an update of your investigations into Carillion.

**Stephen Haddrill:** We announced yesterday that we will have a formal investigation into the audit by KPMG of Carillion and we are looking at the three years from 2014 to the present day. We have said that the scope of the investigation will include the going concern matter, the pensions matter and how the contracts were being assessed, and it will look into other matters as well. There is also the question of whether we launch an investigation into what we call members in business, the accountants who were in the company. That is under different regulations and has a different test for launching the investigation, a misconduct test rather than a breach of regulations test. It is going to take us a little bit longer to work through whether there is a proper basis for launching the investigation but we hope to do that very soon.

Q2 **Chair:** What does “very soon” mean, Mr Haddrill?

**Stephen Haddrill:** I would hope certainly within a matter of a few weeks. We have managed to launch the investigation into the audit very quickly and that would be our intention with that as well.

Q3 **Chair:** How long would you expect your investigations into KPMG and then potentially into the accountants at Carillion to last?

**Stephen Haddrill:** I fully understand that the public, and in particular those people who have been heavily disadvantaged, lost their jobs and so on, as a result of this, want the most rapid possible conclusion to this investigation and, if it points that way, any prosecution thereafter. I think it would be wrong of me to set a firm timetable on this because, first, the scope of the investigation is very wide, going back a number of years, and, secondly, it is absolutely vital that we do this thoroughly. We have the resources we need. We have expanded the resources of our enforcement team considerably over the last few years and I have made it clear to the executive counsel that if she needs any further resources we will provide them. We are absolutely committed to doing it as fast as possible but if I give a date and then, for reasons of making sure that we are on really solid ground, we cut corners and made mistakes I think that would be intolerable.

Q4 **Chair:** I ask because it is 19 months since the FRC announced that it will investigate PricewaterhouseCoopers’ audit of BHS and we have still had nothing from the FRC. The FRC investigation of audit failures at MG Rover, audited by Deloitte Touche, was announced in August 2005 and the outcome was not finalised until April 2015. Might we have to wait 10 years to get the outcome of this inquiry?
**Stephen Haddrill:** No, certainly not. The Rover one was deferred while other inquiries were going on. We are starting this one absolutely now and, as I said, we will do it much faster than those timescales.

**Chair:** When might you expect the work on the audit of BHS to be completed?

**Stephen Haddrill:** It is very close to completion.

**Chair:** It might report within two years, might it?

**Stephen Haddrill:** I think we will see a report faster than that.

**Frank Field:** One year?

**Chair:** No, it has already been 19 months.

**Stephen Haddrill:** I really must not be drawn on things.

**Chair:** No, Stephen Haddrill, the point of a Committee hearing is for us to try to draw out evidence from you and there is a public interest here. BHS was a huge collapse that cost jobs, people’s pensions and livelihoods. It has been 19 months and there is still no report. We are trying to find out whether there is any chance that the report that you announced yesterday, ahead of coming to our Committees to give evidence, might be published in a timescale that allows learnings to be made and also to have some resolution for people who worked there and receive pensions from Carillion.

**Stephen Haddrill:** The object of the investigation is to consider whether to bring a prosecution. That is a legal process and it has to be done thoroughly to make sure that a prosecution, if we proceed with it, is on an absolutely firm basis. We have to go through all the rules of the court processes, the rules of disclosure and so on. Very often—and this was the case with some of the other ones you mentioned, the Rover one for example—you can end up with the other side bringing judicial review hearings and so on. We need to be absolutely firm that we have the right basis for taking a case if we decide to do that.

**Frank Field:** The Prime Minister is waiting for your report on BHS before she decides how and when she might act on the unanimous recommendation of the Commons that Sir Philip Green should lose his knighthood. I know there is lots of things on the Prime Minister’s mind but we are here to help encourage memory. When do you think that will be delivered?

**Stephen Haddrill:** What we are doing is producing a basis, if the facts support it, for a potential prosecution. We are not delivering a report to the Prime Minister.

**Frank Field:** No, you are delivering a report but she is waiting on your report before she decides to act on the resolution of the House of Commons that Sir Philip Green should lose his knighthood. I know it is not the most important thing in the world but it is a reflection about the
pace at which you work.

**Stephen Haddrill:** The most important thing in the world is that we produce a solid report and that if—and I stress “if”—anything goes to tribunal that that tribunal is successful. That is what matters.

**Q11 Antoinette Sandbach:** Mr Haddrill, it is also a principle of law that justice delayed is justice denied.

**Stephen Haddrill:** Yes, I agree, but the worst thing that could happen is that we cut corners on any case, bring a case to tribunal and it is thrown out on those grounds.

**Q12 Antoinette Sandbach:** Are you saying that you do not have the resources within 19 months, which is a significantly long period of time, to have a speedy and in-depth investigation?

**Stephen Haddrill:** We do have the resources and we certainly have the resources to commit to the Carillion case, including whether we expand it into the members in business.

**Q13 Antoinette Sandbach:** We are talking about BHS here. Has there been a change in position in the last 19 months that means that you are better placed now in relation to Carillion than you were with BHS?

**Stephen Haddrill:** We had expanded the team considerably up until about two years ago but we have had a further expansion since then so, yes, we do have the resources.

**Q14 Antoinette Sandbach:** What does that mean in numbers, when you say you have expanded the team?

**Stephen Haddrill:** We have now 30, 32, a mix of lawyers and forensic accountants primarily.

**Q15 Antoinette Sandbach:** As opposed to what?

**Stephen Haddrill:** As opposed to if I go back two years it was probably something like 23, 24. I would have to check.

**Q16 Chair:** Maybe you could get back to us with the precise details of that, Stephen Haddrill.

**Stephen Haddrill:** Yes, I will.

**Q17 Chair:** Sarah Albon, can you tell us about your investigation into Carillion and perhaps also give us some timescales?

**Sarah Albon:** Certainly. As the Committee is no doubt aware, Carillion and its subsidiaries was made up of 326 companies, of which 199 are based in the UK. So far 16 of those companies are in some form of insolvency. The Official Receiver has a duty to investigate the cause of failure of any of those companies in insolvency and also the conduct of the directors involved in reaching that point. It is probable that more of the companies will also be placed into a form of insolvency, so at the
moment the final scope is not yet determined. There were 169 directors across the whole group at the point of insolvency, 36 of whom were in the different companies that are currently in some form of insolvency. At the moment, the investigation is targeting those 16 companies and the 36 directors but, as I say, may be expanded as further companies become insolvent.

The Official Receiver is under a statutory duty to investigate and the Secretary of State, as you are no doubt aware, wrote to me and asked that we expedite the investigation to the degree that it is possible. In normal insolvencies we would wait until we had a first report from the liquidator, which is due under statute to be sent to us within three months of the date of insolvency, but recognising the genuine public interest and concern in this particular collapse we have put a parallel team of investigators in alongside and underneath the Official Receiver so that the twin duties of liquidation and investigation can carry on simultaneously and immediately.

It is very early to say precisely what the timescale will be. At the moment, we do not even have the full scope of the investigation clear as further companies become in scope, as further companies become insolvent, but we are clear that we want to look at all of the things that have been the subject of public concern at the moment. We will be looking at the treatment of any dividends, any payments into the pension scheme, the levels of remuneration and the appropriateness of those in the context of the failures of the company.

Q18 Peter Kyle: Mr Haddrill, to what extent did poor corporate governance lead to the collapse of Carillion?

Stephen Haddrill: It is something that I hope will emerge through the investigation.

Q19 Peter Kyle: You have been watching them for a while now. Did they break the code of conduct of corporate governance at all?

Stephen Haddrill: I think I would draw a distinction between what we have been doing in looking at the auditing and the financial statements. We set the corporate governance code but we do not enforce the corporate governance code. That is enforced by the shareholders. What we will want to understand is how the directors reached the decisions that they took, particularly towards the end of the last financial year, how they took the decision in relation to going concern and whether that was soundly based. That is the sort of thing that would underpin any investigation that we conduct into the directors.

Q20 Peter Kyle: In your opinion, at these early stages do you feel that there is cause for concern about the way the company was governed?

Stephen Haddrill: I think there must be enormous cause for concern about how the company was governed. That is not a conclusive point of view because we need to look into these matters.
**Peter Kyle:** We are not expecting conclusive anything at this point in time.

**Stephen Haddrill:** No, I agree, but I think we all look at what has happened with a degree of incredulity, so we certainly need to understand on what basis the directors were taking those decisions.

**Q21** **Peter Kyle:** What difference could better reporting and enforcement have played in this? You will be aware that the BEIS Select Committee last year released a report on corporate governance. We suggested a whole raft of increased enforcement, declarations and powers for your organisation. To what extent do you think that some of those recommendations, had they been implemented, could have made a difference?

**Stephen Haddrill:** I think that there are areas where our powers need to be strengthened. One of the things that arose from that report was that the Secretary of State agreed that the regulatory bodies should work more closely together and we have been doing that. We have a new memorandum of understanding between us and The Insolvency Service and with the FCA. The intention there is to make the best possible use of our powers in combination. I think we need to go a bit further than that because goodwill takes regulators a certain way but as we saw before the financial crisis, regulators can collaborate and then they stop collaborating. I would like to see some structure around that.

**Q22** **Peter Kyle:** To give you an example, in our report we said that, “Given the broader powers that we have recommended in this report, the Government should consider reestablishing, renaming and resourcing appropriately the FRC to better reflect and expand its remit and powers”. The Government rejected that. Do you think that that needs to be relooked at now?

**Stephen Haddrill:** I do think that some aspects of those powers need to be looked at. Our powers in relation to enforcement should be looked at, particularly the point I made earlier about members in business being subject to enforcement only if there is misconduct needs to be looked at. The misconduct test is a very high bar for us to pass to prove a case there. I think that there are aspects of our ability to review the report and accounts ought to be expanded. We review the financial statements and the strategic report but governance statements elsewhere and the annual report are not within our remit.

**Q23** **Peter Kyle:** We are going to come back to this. You mentioned the MOU a second ago. When will that be in place?

**Stephen Haddrill:** It is. It has just been signed.

**Q24** **Peter Kyle:** Good. Will you be talking to institutional investors to find out why they sold their shares and how they engaged with the board and the reasons why they were—
Stephen Haddrill: Yes. The issues around stewardship are perhaps not part of the formal investigation but I think they are certainly the sort of thing that we need to explore. We have announced that we will be reviewing the stewardship code during the course of the coming year. We have already put out some questions that we want answers to and I think this is a very good case to inform that consideration.

Peter Kyle: Thank you. My final avenue of questioning to you is about how effective your organisation actually is. I have been chair of governors of a school for a long time. We could never have got away with doing in the school what Carillion was getting away with in the last couple of years. It was basically trading insolvently; its finances were not robust. If we had been doing that in the school, Ofsted would have known it within months. They get inside the organisation; they look at it from top to bottom; they make prescribed opinions about the way it is being governed and run. Here we have a FTSE 250 company that is integrated within our public service delivery for our country and yet you were not getting inside that organisation, rolling your sleeves up, having a look at how it was being run and being opinionated at the time that it really mattered. We have to ask ourselves what is the point of your organisation if it can’t turn around an organisation at the point it would make a difference rather than just trying to mop up the pieces afterwards?

Stephen Haddrill: That is a very important question and I think what you are effectively saying is that do we want an organisation in relation to the general run of corporations, as opposed to the financial services sector where you have a sort of prudential approach. As far as possible, the PRA will seek to be involved heavily before something goes wrong at a bank, but in the general corporate sector that is not the position that the UK has adopted. We do not have powers to review the quality of corporate governance and our powers to review reports and accounts and audits are there and we use them.

Peter Kyle: Specifically what powers are missing? What is it that prevents you from—

Stephen Haddrill: What we are looking at is what we see after the event, after the company has prepared its report and accounts, and then we take action. We take considerable action with the auditors. We may seek—

Peter Kyle: What action have you taken that could have in any way altered the direction of Carillion in the last two years?

Stephen Haddrill: What we do not have the ability to do is to see into the way the company is running, is developing its business model and so on.

Peter Kyle: Answer the question: what action have you taken that has changed the direction tangibly of Carillion in the last two years?
Stephen Haddrill: We have not been able to take action to change the direction. We reviewed the report and accounts three years ago and we required some additional disclosures in the report and accounts. There were about a dozen things.

Q29 Peter Kyle: So, you are toothless?

Stephen Haddrill: No, we are not toothless. Frankly, I think we are one of the most effective audit regulators in the world. We are much more transparent, much more powerful than any other audit regulator in the world, but an audit regulator looks at the audit that has been done after the event.

Q30 Peter Kyle: You can’t say two things simultaneously, which totally contradicts yourself. You have not had the power to do anything to turn around an organisation that is failing, that you have shareholders fleeing, and on the other hand say that you are one of the most effective regulators in the world. You can’t say those two things.

Stephen Haddrill: I can certainly say that in relation to audit regulation because I think we are one of the most effective audit regulators in the world, but it is the responsibility of the directors. I think that lies at the heart of your point. It is the responsibility of the directors to run the company. The shareholders, particularly the institutional shareholders, have a responsibility to look at that and we have a responsibility to review what happens and to call it out if what we see in those reviews is not satisfactory. That is what we do in relation to audit and in relation—

Q31 Chair: You said, Mr Haddrill, that two or three years ago you asked for some disclosures. What were they and were you happy that they had been met? Did you come back to look at them at any time since? Two or three years is quite a while ago and it seems that perhaps the company deteriorated quite quickly after that.

Stephen Haddrill: There were about a dozen points that we asked for further disclosure on. The company satisfied us on a few of them and then made the extra disclosures that we were looking for in relation to some. I think the most important one was in relation to the range of possible outcomes of some of the contracts. They did make a statement about that in their next set of report and accounts.

Q32 Chair: Were you happy then that their report and accounts were fine? Were you happy last year and the year before?

Stephen Haddrill: We do not have the resources to review the report and accounts every year but we did go back and review it. We looked at what they had done and I think they also made a reference to the fact that they had been in discussion with us.

Q33 Chair: There was no need since that time—was it two years or three years ago? Do you remember when that was, Mr Haddrill?

Stephen Haddrill: I think it was 2015, so two years ago.
**Chair:** You had no cause for concern or to look back?

**Stephen Haddrill:** With hindsight, clearly it would have been better to have had a further look but at the time there was not a basis for us to do that.

**Q34 Antoinette Sandbach:** Your chairman made an announcement that the FRC had been actively monitoring the situation at Carillion for some time. When did that monitoring start?

**Stephen Haddrill:** The monitoring of the audit I think is what was being referred to there. That started after the profit warning in July.

**Antoinette Sandbach:** 10 July 2017?

**Stephen Haddrill:** Yes.

**Q35 Antoinette Sandbach:** But as you have referred to, you had already gone in and raised concerns with KPMG about the audit in 2015-16?

**Stephen Haddrill:** I was talking about the concerns we had with the company about their report and accounts rather than with the audit. I think the last time we reviewed the audit was 2013 with KPMG.

**Q36 Antoinette Sandbach:** Given the concerns that you raised with KPMG in 2015-16, why didn’t you immediately at that point look at the audit?

**Stephen Haddrill:** As I said, in those matters that we raised we were looking for extra disclosure but they did not affect the financial statements themselves. They did not affect the numbers.

**Q37 Antoinette Sandbach:** It turns out that that is an assumption you are making, Mr Haddrill. That is not fact, is it?

**Stephen Haddrill:** It was an assumption that was valid at the time. We shall see as we look back whether that—

**Q38 Antoinette Sandbach:** We don’t know because you have only just launched your investigation so you can’t say that, can you?

**Stephen Haddrill:** I think I can base a view about what happened in the light of the evidence that we had. We had evidence that some of the disclosures were not as full as they should be.

**Q39 Antoinette Sandbach:** How can shareholders look at the governance, as you suggested they should, if some of the disclosures are not as full as they should be?

**Stephen Haddrill:** That is why we asked the company to correct them, which they did.

**Q40 Antoinette Sandbach:** Within two years that company has gone bust owing billions.

**Stephen Haddrill:** Yes, and I think one of the most important questions is how does—
Antoinette Sandbach: Clearly the disclosure was not sufficient, was it?

Stephen Haddrill: The disclosure was in accordance with the requirements of the law and the accounting standards after it was corrected.

Q41 Antoinette Sandbach: You set the accounting standards or the good governance code.

Stephen Haddrill: The accounting standards are established by the International Accounting Standards Board and adopted by the European Union through to the UK.

Q42 Antoinette Sandbach: But we have the power in the UK to set our own accounting standards, don’t we? We can set higher standards.

Stephen Haddrill: Not in relation to accounting, no. They are adopted from the international board by the EU. Those are the standards that apply for listed companies. We can’t set a higher standard.

Q43 Antoinette Sandbach: You are saying that you have no ability to assess whether or not those standards are sufficient to provide enough information to shareholders to hold the board to account?

Stephen Haddrill: We have the ability to assess whether the standards are adequate but we don’t have the ability to change them. If we felt that a standard required attention like that we would have to go back to the European Union or to the international board and persuade them to make a change.

Q44 Antoinette Sandbach: In relation to the code that you can set—

Stephen Haddrill: Yes, the corporate governance code.

Antoinette Sandbach: —which is the governance code, is misconduct assessed against that code?

Stephen Haddrill: No. There is not regulatory enforcement of the code. The code is enforced, if that is the right word, by shareholders.

Q45 Antoinette Sandbach: Basically, what you are telling us today, Mr Haddrill, is that we can’t rely on the audited accounts of any major company because you can’t enforce it, we can’t rely on hidden debt or, for example, the overstatement of goodwill.

Stephen Haddrill: No, that is not right. You are mixing up two things. You are mixing up the enforcement of corporate governance, which is a stewardship responsibility, first of the directors and then of the shareholders, and the report and accounts of the company.

Q46 Antoinette Sandbach: But isn’t the auditor effectively supposed to provide an independent view that can be relied on by shareholders to present a fair and true position of the company?
Stephen Haddrill: Absolutely. The directors must produce accounts that are true and fair. Those are reviewed by the auditor and the audit opinion should confirm that. If the auditor has any reason not to confirm that it must either persuade the company to do something else or report that. We have introduced in the last three years an extended auditor report to make sure that auditors do explain what they have done and what their views are.

Q47 Antoinette Sandbach: Clearly that failed, didn’t it?

Stephen Haddrill: I think there is a risk here that a number of very powerful interventions that have been made are being undermined, in your view, by one failure.

Q48 Antoinette Sandbach: Mr Haddrill, this was the most shorted stock on the stock exchange. At the time of the statement, and indeed before the March 2017 accounts, over 23% of Carillion stock was shorted. Did that not set alarm bells ringing at the FRC?

Stephen Haddrill: We did not review the company as a result of that, no.

Q49 Antoinette Sandbach: Why not?

Stephen Haddrill: As I said, we had reviewed it in 2015.

Q50 Antoinette Sandbach: And found its disclosure to be unsatisfactory.

Stephen Haddrill: Yes, but at that point we did not think that the lack of disclosure was symptomatic of something more serious.

Q51 Antoinette Sandbach: Carillion did operate aggressive accounting practices. Should that have been more of a concern to the auditors?

Stephen Haddrill: I think that since we might be moving into an investigation of the directors, it would be inappropriate for me to comment.

Q52 Antoinette Sandbach: Mr Haddrill, I am sorry, I don’t accept that. You knew that you were coming to this Committee. You did not announce your investigation on 10 July 2017. I do not accept that it is inappropriate for you to answer that question to this Committee, having known that you were coming here to give evidence at the point that you announced your investigation, I think just yesterday.

Stephen Haddrill: We have announced the investigation into the audit. We started our inquiries into the quality of the audit immediately after the profit warning. We have now completed those and we are doing a formal investigation. In relation to the financial statements and the conduct of the directors in that regard, the FCA has been conducting its own inquiries. We have its information and we will be reaching a view as soon as possible on whether to extend our investigation into the directors.
Q53 **Antoinette Sandbach:** Earlier in evidence to my colleague Peter Kyle you said that you had just signed a memorandum of understanding. There is absolutely nothing that would have prevented that memorandum of understanding being signed after the BHS collapse, is there?

**Stephen Haddrill:** No, there isn’t, but we were asked by the Secretary of State to do that—I can’t remember exactly when he did—and we set about doing it straight away.

Q54 **Antoinette Sandbach:** Why did you wait to be asked?

**Stephen Haddrill:** We already had a memorandum of understanding with the FCA. What we have been doing is upgrading it, effectively, improving it.

Q55 **Antoinette Sandbach:** The reality is over £725 million has been lost to a pension scheme really due to the fact that the underlying financial assumptions have changed and it is the taxpayer that has to pick that up.

**Stephen Haddrill:** I think we should start by looking at what the quality of the decision-making of the directors and of the auditor was, and that is exactly what we are doing.

Q56 **Antoinette Sandbach:** You are responsible for looking at the audit standards and reassuring the public that we can rely on those standards and that those give sufficient information to shareholders. What lessons have you learnt after the profit statement that wrote off £825 million in July, within just two years of your last look at Carillion’s accounts?

**Stephen Haddrill:** That is going to be the subject of the investigation. We will explain what we have found when we have completed that investigation.

Q57 **Antoinette Sandbach:** But you have just said that you started on 10 July 2017.

**Stephen Haddrill:** Yes, but we do need to make sure that the investigation that could lead to a prosecution is not prejudiced by statements that we make today on the basis of our initial inquiries. What we need to do is conduct a very thorough investigation, including into why the directors determined to make a going concern statement when they produced their report and accounts and then only a few months later reversed that. Well, not reversed it but included—

**Antoinette Sandbach:** Yes, they reversed it. They wrote off £825 million.

**Stephen Haddrill:** Yes, they wrote off that sum but they did not state at that point that it was no longer a going concern. That is what I meant by reversed.

Q58 **Antoinette Sandbach:** Wasn’t that obvious given that the stock fell, the value of Carillion fell that day by something like 50% and this in a company that, as I said, a year before had been shorted by 23%?
Stephen Haddrill: The question that we need to get to the bottom of is whether the events that ultimately happened in January were foreseeable and the directors should have taken different action and the auditors should have taken different action in July or whether they unfolded in a way that was unexpected.

Q59 Antoinette Sandbach: But you had been investigating in that period between July and before the company went into liquidation.

Stephen Haddrill: We were reviewing the audit. I want to distinguish between the legal process and the investigation and our review of the audit. We have done a thorough piece of work on reviewing the audit but these audits are thousands of documents. This company is made up of hundreds of different subsidiaries and so on. It is a major piece of work.

Q60 Antoinette Sandbach: But that is why the auditors are there, to reassure shareholders or pension recipients in my constituency whose hard-earned money has been lost.

Stephen Haddrill: You are absolutely right, it is the responsibility of the auditor to provide an external view on whether the directors have taken the right judgment on going concern. It is our job then, if there are issues around that, to look into it and look into that audit, which is what we are doing.

Q61 Chair: I want to explore slightly further what exactly has happened between July and the middle of January. Stephen Haddrill, your chairman wrote to the Business Secretary of State on the day of the collapse of Carillion saying that, “We have powers to investigate the circumstances relating to the audit of Carillion as well as the actions of the relevant accounting professions”. For six months I presume, and in your answer to Antoinette Sandbach, that you have been looking at the KPMG audit.

Stephen Haddrill: Yes.

Chair: You have now announced that you are doing something formally but for the last six months you have been actively monitoring. From the work you have done in the last six months, do you think that KPMG’s audit was found wanting, just 10 months ago?

Stephen Haddrill: If I answer that I would prejudice the investigation. Can I put it a different way? Perhaps that would help the Committee. What we have said is that we believe there is a good reason to investigate and we have identified the auditor’s work on going concern, the auditor’s work in relation to pensions and the auditor’s work in relation to whether the assessments by the directors of the outcome of the contracts was satisfactory.

Q62 Chair: For six months, as in the words of your chairman, you have been actively monitoring this situation in close consultation with other relevant bodies. Antoinette Sandbach has made the point, I think very powerfully, that you have a responsibility to investors, people with a pension with the
company, and so on, to actively monitor but then also report. For six months you have been looking at this situation. I guess it comes to the point about are you properly resourced to do your job and do you have the powers to do your job. For six months you were presumably so worried about this business that you were actively monitoring it and yet in those six months did you make any public statements about Carillion or about its audit?

*Stephen Haddrill:* Not specifically about Carillion. We put out each year some guidance to audit committees and that is public guidance seen by investors, about the—

Q63  **Chair:** Was it public knowledge that you were actively monitoring?

*Stephen Haddrill:* No.

Q64  **Chair:** I guess this is part of the problem, isn’t it? Peter Kyle made the point about the school where he is a governor. If Ofsted had concerns about a school in any of our constituencies, parents would know about that. I feel that investors in the company had the right to know that you were actively monitoring a situation, presumably because you were concerned about it. Why wasn’t that information in the public domain and why didn’t you, over those six months of actively monitoring, the most critical six months probably for that business in its short 19-year life—nobody knew you were actively monitoring, no one knew what you were monitoring or whether you had found anything.

*Stephen Haddrill:* That is a very good point. The reason is that we are not able to disclose the individual companies that we look into and the audits that we look into because there is a confidentiality requirement built into the companies legislation. We have sought to get round that in some respects. We can talk about it now because the company has failed and because we have launched an investigation.

Q65  **Chair:** That is sort of like closing the gate after the horse has bolted, isn’t it? We can have a very great discussion now. That is not going to get the money back for anybody who worked for the business or anybody saving for a pension or any shareholder who lost money or the subcontractors that have not been paid for six months. The best time, Mr Haddrill, for you to have been speaking about this would have been the time where you were actively monitoring because then decisions could have been made.

*Stephen Haddrill:* I think that the requirement in companies legislation for confidentiality needs to be reviewed.

Q66  **Chair:** Thank you. Which of your directors is responsible for the review that is happening into the KPMG audit of Carillion?

*Stephen Haddrill:* We have a director called an executive counsel, a lawyer, and she is responsible for taking that case forward.

Q67  **Chair:** What is her name?
**Stephen Haddrill:** Claudia Mortimore.

Q68 **Chair:** I was looking at your annual report and accounts for 2016-17 and it says in the experience for your executive director for corporate governance and reporting that he had a 17-year career at KPMG. What is his responsibility?

**Stephen Haddrill:** First, he left KPMG about 2000, maybe even slightly before, so he has been a long time out of the firm. His responsibility is in relation to accounting standards, corporate governance and the review of reports but he is not responsible for taking these investigations and cases forward.

Q69 **Frank Field:** Two of the last three finance directors of Carillion came from KPMG. KPMG has conducted the audit for the last 19 years. Did that not sound a warning to you? Given the oligarchy that now exists among the accountancy firms, shouldn’t we be considering a recommendation to the Government to break them up?

**Stephen Haddrill:** I will answer that one first. We feel that there should be more competition in the major accounting and audit area. We asked the Competition Commission in something like 2012—I can’t remember exactly—to do a review and they did. They made a number of recommendations that have been implemented. To some degree, there is more competition among the big four themselves but there has been no entry to the market by other firms at that top end of the corporate sector.

Q70 **Frank Field:** There would be if you broke the companies up.

**Stephen Haddrill:** I think the Competition Commission—the CMA now—at some point will need to review the effectiveness of what they recommended and look at it again.

Q71 **Frank Field:** And the first question?

**Stephen Haddrill:** Sorry, can you remind me?

**Frank Field:** It was that two of the last three finance directors came from KPMG. KPMG has been the auditor for the last 19 years. Following Rachel’s question, didn’t that put up a signal to you?

**Stephen Haddrill:** There are rules about the extent to which auditors can join companies. I think there is a two-year cooling-off period. I would need to check what the situation is.

Q72 **Frank Field:** But they are all mates, aren’t they? This is going back to your previous problem. There are four companies dominating the scene. They appear in all papers in one guise or another. You are going to recommend that the relevant body looks at breaking up these companies?

**Stephen Haddrill:** We are going to propose to the CMA that they look again at whether there can be more competition in the sector. What the
remedy is I think is for them. We have strengthened what we call the independence rules in relation to the extent to which an audit firm can be engaged with a client to provide non-audit services and the extent to which auditors and company directors can move between those institutions. They were changed in 2016 and they are certainly much stronger than they were.

Frank Field: We will come back to that. Thank you.

Q73 Peter Kyle: Mr Haddrill, less than three years ago Carillion changed the rules by which it could claw back directors’ pay. Should that not have sounded a klaxon in your organisation?

Stephen Haddrill: Again, it comes down to this point that we don’t have powers or responsibility to look into governance matters and that is really a governance matter, not an accounting or an audit matter.

Q74 Peter Kyle: They changed the rules from previously that directors’ pay could be clawed back if there was corporate failure. They changed it to one of gross misconduct. They raised the bar into the heavens. Why would a company do that?

Stephen Haddrill: I think it is important, as we are doing the investigation, to look into whether that was a factor that has led to some of the events that have happened and whether it is a factor that the auditors should have taken some account of.

Q75 Peter Kyle: But once again this points to something that we, in retrospect, see was a very clear indication of a company in distress, one that the regulator did not detect, did not act on, did not get involved in, did not make public the information or draw attention to it in a way that could have allowed the different actors who have control over the organisation to act in a way that could change things.

Stephen Haddrill: I think what you are highlighting is a rather fragmented oversight of companies in this country. That information about remuneration packages is something that ought to be scrutinised by the shareholders as the stewards of the business. That is why I come back to: is the stewardship code that we operate effective?

Q76 Peter Kyle: I think what I am highlighting, to be blunt, is that the FRC has been useless when it comes to Carillion.

Stephen Haddrill: Well, I reject that. What the FRC has done is—

Peter Kyle: It did collapse.

Stephen Haddrill: I know and companies do collapse. We do not have a system where regulation is designed to stop companies collapsing. It is designed to set certain standards of behaviour for directors for accounting and for audit and to make sure that those standards are complied with.

Q77 Peter Kyle: But clearly the standards were not complied with. You are
the organisation that is tasked with monitoring and regulating those standards.

**Stephen Haddrill:** But what we do not have is the ability, that say Financial Services or the PRA would have, to look inside the business. We do not know what is going on inside the business more than what is evident from what they publish.

**Q78 Peter Kyle:** Would you welcome those powers?

**Stephen Haddrill:** I would welcome stronger powers to be transparent about the sort of things that we are finding.

**Q79 Peter Kyle:** Is that a yes?

**Stephen Haddrill:** It is a yes for some. I don’t think that we would be well served in this country by having a corporate regulator that can go into every company and say, “How are you doing it?” There has to be a degree of enterprise here and a degree of acceptance that there will be failure sometimes.

**Q80 Peter Kyle:** But the market works on information and clearly things were hidden within Carillion. This rule of changing the clawback of directors’ pay in the event of failure was buried deep in the small print of an annual report. These are the things that most people would not know about. I am not asking you to go in and run the company for them if you think a few things have gone wrong but having the power to highlight, to point to, to allow the market and the actors involved in a company to act is the kind of thing that we do need to be doing.

**Stephen Haddrill:** I think that takes us back to what I was saying earlier on about powers. Remuneration is an area where our ability to scrutinise the company through its report and accounts—our writ does not run there.

**Q81 Peter Kyle:** Have you ever asked for these powers in the past?

**Stephen Haddrill:** Yes, we have.

**Q82 Peter Kyle:** But they have been rejected?

**Stephen Haddrill:** It was when we said to the Select Committee that we wanted the ability to review the report and accounts as a whole, not just certain bits of it, and we have not yet had a positive response to that.

**Q83 Antoinette Sandbach:** Mr Haddrill, can you explain to us the section of the Companies Act that requires companies not to pay dividends out of capital?

**Stephen Haddrill:** I am sorry, you are getting beyond my ability as a non-accountant. Let me write you a note on that.

**Q84 Antoinette Sandbach:** I am not an accountant either. Are you saying that you are not aware of that provision?
**Stephen Haddrill:** I am aware of the general provisions of the Companies Act in relation to the company’s responsibility on paying dividends.

Q85 **Antoinette Sandbach:** We know that Carillion paid £376 million in dividends for the period of 2012 to 2016, despite making just £159 million in cash from its operations. Was that something that you were aware of when you looked at the accounts for 2015-16?

**Stephen Haddrill:** I would have to check whether we looked at that particular thing. I imagine that we would have done but let me confirm that. The dividend policy—

Q86 **Antoinette Sandbach:** How quickly could you confirm that to us? That is rather key to the issue as to whether or not there was misconduct and whether or not the company was acting legally or its directors were acting legally. How quickly can you confirm that to us?

**Stephen Haddrill:** We will come back in the next couple of days.

Chair: I think it would be very helpful to the Committees if we could have answers to all the questions that we put today by the end of this week.

Q87 **Antoinette Sandbach:** Do you accept that concerns have been raised by the Local Authority Pension Fund Forum and others that your accounting standards do not enable anyone to have a meaningful assessment of a going concern, which effectively is the issue with Carillion?

**Stephen Haddrill:** I don’t accept that it is impossible to have a meaningful—I think that is too broad a statement. I think where the problem lies is that the going concern judgment is thought by the public and by many investors to be a judgment over the next year or the year after.

Q88 **Antoinette Sandbach:** Did you receive a copy of the counsel’s opinion that confirmed the substantial legal flaws with the International Financial Reporting Standards?

**Stephen Haddrill:** That is the Bompas opinion, I think you are referring to?

**Antoinette Sandbach:** Yes.

**Stephen Haddrill:** Yes, we have that. We have reviewed it. We have had our own counsel’s opinion and, frankly, that does not confirm that. Ministers in 2013 gave their own views on that matter and they thought that our interpretation was appropriate. We think that we have interpreted company law rightly in relation to dividends and the true and fair judgment and we have made that clear.

Q89 **Heidi Allen:** I am going to apologise in advance for being potentially a little bit rude but I want to make a point. I was just reflecting on what Peter was asking and reading your profile here, you were appointed in 2008 as a member of the Financial Crisis Advisory Group, a high level
advisory group set up by the International Accounting Standards Board and the Financial Accounting Standards Board to consider the financial reporting issues arising from the global financial crisis. I am asking the question on behalf of ordinary people. The financial crisis was possibly too much enterprise. You have said in relation to Carillion that perhaps it is not your job to get inside and you can’t stifle enterprise. Private Eye, the magazine, have a thing it calls a non-job. We are 10 years on from your appointment, which was a role explicitly to deal with the sort of financial crashes we saw. Why is it that Peter is still having the conversation with you 10 years on about do you not have the powers you need? Should you not have asked for those more forcefully to make your job mean something?

Stephen Haddrill: That was a short-term advisory appointment I had when I was not in my current role. I was there when I was Director General of the Association of British Insurers and they asked me to give an investor view at that time. Sorry, I don’t know if that answers your question.

Q90 Heidi Allen: The heart of it is that these roles are to assist and help the general public make sure that things like the financial crash don’t happen again. I find it unacceptable that Peter is having to ask you a question about why you don’t have the powers and why you haven’t asked for them. Surely that is your role.

Stephen Haddrill: I can assure you we have been asking for them and regulators don’t always get all the powers that they want. We did seek powers in relation to audit. We got them in the end through the decisions of the European Union and they were implemented in 2016.

Q91 Heidi Allen: You have been the chair of FRC since 2009.

Stephen Haddrill: Chief Executive.

Heidi Allen: That is still quite a long time. If that is your role, don’t you bang down the door to get those powers and call it out if you don’t have them?

Stephen Haddrill: Absolutely, and I certainly take that as a criticism. We have not achieved what we want. All I would say is that that has been against a background of a lack of Government interest, frankly, over a period of time until the last couple of years, in expanding regulators’ powers. That is certainly what we have faced. If you take the audit regulations that came in in 2016, for example, the Government issued a direction that we should delegate as much as we possibly could under the European directive and regulation to the professional bodies. We did not find that right at the time. We thought that as the audit regulator we should be able to hold all those powers to ourselves rather than delegate processes to the professional bodies. That is the sort of historical background to where we are today.

Q92 Chair: Thank you, Mr Haddrill. The Liaison Committee is seeing the
Minister Lidington next Wednesday and one of the questions we might pose to him is what lessons could be learnt about the powers available to the FRC.

Before we move on to ask some questions about The Insolvency Service, can I ask a couple of factual questions? KPMG has been the auditor of Carillion since its inception, for 19 years, and has earned £30 million worth of fees during that period. Is it the FRC’s view that it is appropriate or good practice to have the same auditor for almost 20 years?

**Stephen Haddrill:** The law requires the audit to be retendered after 10 years. The incumbent can keep that role for 20 years. That is what the law says.

Q93 **Chair:** I am not saying as the law. What is your view about good practice? Do you have a view about it?

**Stephen Haddrill:** We do have a view and in fact we wrote into the corporate governance code that there should be retendering—we didn’t write “in rotation”—before that law came into effect. We are there to make sure that the companies and the audit firms stick with the law, so that is what we have to do.

Q94 **Chair:** Do you think perhaps that law needs revisiting with fresh eyes?

**Stephen Haddrill:** Those regulations came in only less than two years ago. I think we will need to review them to see how they are working. One of the things that is happening is the combination of rotation and the independence rules means that in some sectors we may well end up with even fewer than four people competing for the job. There are things that we need to review.

Q95 **Chair:** Related to that, are auditors of companies allowed to provide other paid services to the company that they are auditing?

**Stephen Haddrill:** There are quite strict rules around that. There is a whole list of prohibitions that they can’t provide services on and then there is a cap on the value of the services that they can provide, which I think is about 70% of the audit.

Q96 **Chair:** If they received £30 million in fees for the audit since 1999, you are saying that could earn £21 million of other fees from the company they are auditing over that 19-year period?

**Stephen Haddrill:** Yes, except that they have to consider whether in taking on that contract, even within that cap, it could lead to any risk to the audit. If it would do and it can’t be mitigated they should not take that work on.

Q97 **Chair:** Does the FRC have information about what other services KPMG was providing to Carillion? Would you able to tell us that?

**Stephen Haddrill:** We should be able to do that, yes.
Q98 **Chair:** If you could do that and how much they were worth and what sort of services, we would be very grateful for that information. Do you know what the biggest asset was on Carillion’s balance sheet?

**Stephen Haddrill:** Goodwill, I think.

Q99 **Chair:** Goodwill was worth £1.57 billion. That seems quite surprising. Is it good practice to have goodwill as the biggest asset on your balance sheet? Without goodwill, the liabilities would have been greater than the assets. It was only the goodwill that kept the assets higher.

**Stephen Haddrill:** It is not untypical. What is happening is that increasingly companies’ balance sheets are made up of goodwill. They are made up of intangible assets rather than bricks and mortar and all the rest of it.

Q100 **Frank Field:** Can you tell us what goodwill is, Stephen?

**Stephen Haddrill:** I can’t give you the strict accounting definition but it is—

Q101 **Frank Field:** It is an item that disappears once the company is in trouble, isn’t it?

**Stephen Haddrill:** Absolutely. I think this whole issue about how to account for intangible assets and whether too much of the proportion of the balance sheet is in that sort of asset is something that, frankly, we are all struggling with.

Q102 **Chair:** Do the FRC and FCA account for goodwill in the same way?

**Stephen Haddrill:** It doesn’t arise really.

Q103 **Chair:** The FRC allows goodwill to count as capital resource. I don’t believe the FCA does. Is that correct?

**Stephen Haddrill:** I will check that.

**Chair:** If you could check that.

**Stephen Haddrill:** What we do will be consistent with the accounting standards. They may have different financial regulations for banking.

Q104 **Frank Field:** Goodwill appearing in these accounts does not do much good for the pension scheme. Over the time that Rachel has asked you about, with £1.5 billion goodwill, the pension deficit doubled. Shouldn’t that be taken into account? Goodwill to whom?

**Stephen Haddrill:** The question in relation to pensions is what is the company able to afford to pay in to the trustees.

Q105 **Frank Field:** Isn’t it misleading to say goodwill when you have this mega deficit appearing? I still don’t understand what goodwill is. Who decides the sum that Rachel was questioning you on?
Stephen Haddrill: It will be decided by the directors in accordance with the accounting standards and then audited.

Chair: Everything else was written down, all of their other assets were written down apart from goodwill. Would you expect that to sound some alarm bells, that all the other assets of the business were being written down but good old goodwill keeps on giving, £1.57 billion?

Stephen Haddrill: I think that is a good point for the investigation.

Chair: Thank you. We will move on now.

Rachel Maclean: Sarah Albon, with regards to timescale of your inquiry, when will people know whether those directors of Carillion have been guilty of misconduct?

Sarah Albon: As I tried to indicate at the beginning, at the moment the process of putting the companies into some form of formal insolvency has not concluded yet. We do not yet have the full scope of the directors who are in scope of the investigation absolutely clear.

Rachel Maclean: When do you expect to get that?

Sarah Albon: I imagine that the insolvency process will continue for another few weeks, possibly a small number of months. As I say, there are up to 169 current directors across the whole group. We would also want to look at anybody who had recently been a director of any of the failed companies.

I do recognise that this can be incredibly frustrating for members of the public, who have an absolute right to know what has gone on and a completely understandable desire to know that quickly. As with the FRC’s investigation, what we are doing is preparing a case to bring to court, potential misconduct of these individuals, and the companies—

Rachel Maclean: I understand that—thank you for that—but you must have done this sort of work in a large-scale company before. What is your ballpark best estimate, given your experience?

Sarah Albon: The average time that it takes us to conclude investigations and get all the way through to an outcome of disqualification or a decision that there is nothing more to do is 21 months. This is clearly at the more complex end, so one would expect in some ways that it would take longer, but, because it is of such public significance, we are putting considerable resource into doing the investigation. I think—

Rachel Maclean: You are putting more resource in so that it could potentially be faster?

Sarah Albon: It potentially could. One significant constraint that we are already coming across is the incredibly poor standard of the company’s own record keeping. In preparing for this Committee, it took some hours to identify how many directors we may even potentially be targeting
because the company had not kept its own records properly up to date. It is hardly forensic accountancy to find out how many directors there were, but nevertheless it should have been absolutely, straightforwardly available.

Q111 Frank Field: The auditors passed the company.  
Sarah Albon: Yes, I am aware of that, and I guess it is something that we need to now look at.

Q112 Rachel Maclean: You are struggling with that. You talked about 169 directors. How far back will you go to previous directors that may not be directors anymore?  
Sarah Albon: We will go back to previous directors. Essentially, all of this investigation is aimed at understanding the cause of the failure of the company.

Q113 Rachel Maclean: How far back will you go, then? What is the cut-off?  
Sarah Albon: Typically, only two or three years. There is no formal legislative bar on how far you look back. It is just that it is harder to prove a causal link to failure the further back in time you go, when the company obviously kept trading and kept trading. If somebody had resigned from the company 10 years ago, I think it would be almost impossible to say that their actions that long in the past provided a direct causal link to its failure today.

Q114 Rachel Maclean: Yes, I understand. How much will this process cost the taxpayer overall?  
Sarah Albon: There are two processes here. One is the process of liquidation itself, and the other is the investigation. It is important to keep those two separate. Generally speaking, in large companies that fail, whether they go through a form of liquidation or administration, there are sufficient funds in the company to pay for the costs of the winding up.

Q115 Rachel Maclean: That is not the case in this one, is it, though?  
Sarah Albon: The reason, as far as I have been able to ascertain, that uniquely a listed company of this size and scale has gone through compulsory liquidation is because there was not an insolvency practitioner who was prepared to take on the administration because there was not, in their understanding, sufficient certainty that there was enough money left in the company to pay their costs.

Q116 Rachel Maclean: Is that also your understanding?  
Sarah Albon: Yes. It is early days, but it seems to us to be more likely than not that there will not be sufficient assets to meet even the costs of winding up the company.

Q117 Rachel Maclean: What we have also understood from our briefing is that
not only is it not clear how many directors there are, it is also not clear what is the scale of the assets and liabilities of the company. There is a doubt there. Is that right?

Sarah Albon: That is right. Obviously, one of the major things that my team on the liquidation side will be doing is their very best to preserve what value there is remaining in the company and to achieve that for the benefit of the creditors of the company.

Q118 Frank Field: This company was audited?
Sarah Albon: I think the companies were all audited, yes.

Q119 Frank Field: You are telling us this tale past the audit.
Sarah Albon: That is true.

Q120 Rachel Maclean: I want to ask about the role of the special managers that have been appointed. How has that process been managed? Who has made those decisions to appoint them?

Sarah Albon: Special managers can be appointed by an Official Receiver to assist him in carrying out his duties, and essentially we have done that just because of the scale of this. The actual appointment is made by the court, so an application is made to court. That sets out the scope of the special managers, including things like the remuneration and the level of bonding that they have to ensure that they can meet any costs of their own if they fail. That is a process that happens under the governance of the court.

Q121 Rachel Maclean: Is that objective, given that we hear that PwC is going to potentially earn £50 million from its role of having special managers?

Sarah Albon: I think the £50 million is a figure that is potentially the cost that was an early assessment of all of the specialists, so that would not just be the cost for PwC. It would include legal costs and quantity surveyors and other specialists that the liquidator is likely to need to engage in order to assess the value of the assets that remain.

Q122 Rachel Maclean: What we have been told is that is just PwC’s fees. It could be earning £50 million in fees.
Sarah Albon: It is far too early to say. I am aware of one figure of £50 million that has been used as an early estimate of overall costs, but that was not purely PwC fees. It was all professional fees.

Q123 Rachel Maclean: Going back to the scale of the global liability, you are not able to give a figure at all. Can you be transparent with the public as and when you are able to arrive at these figures? Will the public be informed? Will you be making announcements? What is the process of managing that transparency?

Sarah Albon: As part of a process of liquidation, we invite individuals and companies who are owed money by the company to submit what is
called a proof of debt. We also, however, have to take a pragmatic view of the extent to which we want to forensically go through everybody’s claims that they are owed money by the company if the company itself has no money to pay those individuals. There is only any point establishing precisely what is owed to whom at further cost if there is actually some money left to give them at the end of that process.

Q124 Rachel Maclean: The special managers in the liquidation process mean that the people who are trading will continue to be paid as much as possible. Is that right?

Sarah Albon: Yes. The Government have asked the Official Receiver to continue to maintain services as far as possible in the public sector and also into the private sector clients to the extent that they are prepared to pay the full cost of that. What happens is that those individuals and subcontractors who are contracted by the liquidator or his special managers will be paid in full for the services that they provide post the point of liquidation.

However, the thing that obviously is a difficult factor but also an inevitable truth is that there is a bright line drawn at the point of insolvency. Many of those individuals who will now still be paid for continuing to provide services will nevertheless also have a claim in the liquidation for work that they provided before the date of liquidation, and many of those claims will probably find at the end of the day there are not sufficient assets to pay.

Q125 Rachel Maclean: They will not be paid, but will the ones that will be contracted now, after the point of liquidation, be sticking to the 120-day payment schedule that Carillion used to engage in, or will it be a more reasonable payment schedule?

Sarah Albon: We would be looking to use normal industry-standard payment schedules in line with good practice.

Q126 Rachel Maclean: Which is how many days?

Sarah Albon: It varies, but within the normal rules of ensuring that services have been received and not paying in advance and those kinds of things. We would be looking to pay the contractors as quickly as we can.

Q127 Rachel Maclean: Thirty days, 60 days?

Sarah Albon: I would need to write to you on that. We are having to use Carillion’s own financial management system, payroll, and all of the systems that it has in place because there is not an alternative structure you can just import in. The only reason I am hesitating is because I am honestly not sure of the extent to which those systems are manipulable by us now quickly to change payment schedules and those kinds of things.

Q128 Stephen Kerr: Does The Insolvency Service have the powers and
resources it needs to deal with a large failure like Carillion?

**Sarah Albon:** We certainly would not have had the resources without the use of special managers, which is why we made the application to court for that purpose. In the liquidation itself, as I said, there are some 199 UK companies that we need to consider and working with the directors of the companies that are still solvent in the group to consider whether they should also go through some form of insolvency. It is certainly the case that we have needed to quickly boost our capacity through the use of special managers.

In terms of the investigative resource, we have well qualified investigators, and we would routinely—and will in this case—boost their powers through the use of external forensic accounting teams and other legal specialists as they see need to draw that in. In short, I think the answer is yes.

**Q129 Stephen Kerr:** In short, the answer is, yes, you do feel you have the powers and the resources. What about the statutory framework that we currently operate to in this country in respect to insolvency? We are slipping down the world rankings from the World Bank’s perspective in terms of the fitness of that framework. Would you like to comment on that?

**Sarah Albon:** The World Bank a couple of years ago changed some of the ways that it assessed those different forms, and it is certainly the case that a country that has something more akin to the American Chapter 11 procedures would rank more highly. The Government issued a consultation paper, I think a couple of years ago now, looking at those things, and—

**Q130 Stephen Kerr:** In 2016, yes. Have you had discussions with the Government about that consultation?

**Sarah Albon:** I have, although not recently, but I believe that there is still commitment from the Government to introduce some of those changes when parliamentary time allows, but obviously parliamentary time does not allow very much just at the moment.

**Q131 Stephen Kerr:** It seems like this might become a pressing matter, given the events of recency. Do you have an expectation about when the Government might respond to their own consultation paper?

**Sarah Albon:** I am afraid I do not.

**Chair:** That is something we could follow up with the Minister, Stephen.

**Q132 Stephen Kerr:** Right. Lessons that are learned from the investigations that are conducted by the service: what impact do they have? How do they feed back into the ecosystem of business in this country?

**Sarah Albon:** We have close working relationships with officials in BEIS, and would certainly discuss with them and with Ministers anything that we felt was coming out of things that we found were thematic as opposed
to one-off. We have good channels to feed those kinds of concerns back into the team that would be responsible for company law.

Q133 **Stephen Kerr:** Are there any examples of any recent themes that you have fed back in?

**Sarah Albon:** Recently there have not been significant similar themes. We are in the very early stages of this investigation, but, as I said, it is an extremely unusual set of circumstances where you see a company of this size going into compulsory liquidation for lack of sufficient funds to fund any other form of insolvency.

Q134 **Stephen Kerr:** Are there any changes in the insolvency rules, as they currently stand, that you would like to see that could have prevented or lessened the impact of what happened at Carillion?

**Sarah Albon:** I do not think that there is something that is inherent in the insolvency rules that will make a difference. By the time a company has reached insolvency, whatever procedure it goes through, people are going to lose out significantly, unfortunately. This is almost the definition and the nature of it. Whether it is an individual or a company, it is somebody who can no longer afford to meet all of their commitments. To the extent that it is possible to do something preventive, you need to look further up the food chain, not at insolvency but at the rules that are relevant to a solvent company and how it conducts its business in the days prior to any insolvency.

Q135 **Stephen Kerr:** There has been, rightly, a lot of media focus on the remuneration packages and bonuses of the directors. What can the Official Receiver do to reclaim pay and bonuses from directors?

**Sarah Albon:** The Official Receiver has wide-ranging powers as liquidator to seek to reclaim monies that have been paid out inappropriately and to the detriment of creditors. There is no freestanding subsection that says, “Under this section, I can claim your bonus back or the pay”, but it can certainly look at the reasonableness of remuneration packages in the full—

Q136 **Frank Field:** It has looked at these rules?

**Sarah Albon:** Then it is possible to claim. In the event that misconduct is found, then the Official Receiver, as liquidator, can seek to reclaim from directors personally and indeed from any other individual.

Q137 **Frank Field:** Would running your company bust be covered by this?

**Sarah Albon:** No. The simple fact of liquidation does not allow you to seek to reclaim money from company directors, otherwise the limited company status would be meaningless.

Q138 **Frank Field:** Do you have a policy of goodwill to them?
Sarah Albon: No. I do not think that directors investigated by the Official Receiver or The Insolvency Service would ever feel that we had a particular policy of goodwill to them.

Q139 Chair: Is it the case that the changes in the clawback arrangements for bonuses paid at Carillion will make it harder for you to claw back bonuses than it would have been if the rules had not been changed?

Sarah Albon: No. As I understand it, the changes in Carillion’s practice were about Carillion’s ability to claw back bonuses. What I am talking about is the ability of the Official Receiver to claw back any money paid, not just to directors but inappropriately by the firm to any individuals to the detriment of creditors. There is an ability to look at that and to seek to reclaim monies improperly paid away.

Q140 Stephen Kerr: The stopping of future pay. There were a number of directors who had deals that went well into the summer of this year. That has been stopped by the Official Receiver. Is that normal practice?

Sarah Albon: Yes, it would be. The normal practice would be that monies that are not paid at the date of insolvency would be likely to become unsecured claims in the insolvency, along with all of the other people who would be owed money by the company.

Q141 Stephen Kerr: Do they appear in the ranking of creditors? Are they still in the list of people who might get something?

Sarah Albon: I suppose that is technically true. Depending on the individual terms and whether or not the money was actually owed at the date of the insolvency or whether it would have become owed at some future date if a set of circumstances persisted, and in the event that there were sufficient funds to make a distribution to unsecured creditors and in the event they made a claim, we would have to look carefully at whether or not the money was actually owed to them.

Q142 Ruth George: You have explained the situation, or tried to, in relation to directors, but what about other employees of the company? What have they been informed about their position?

Sarah Albon: Forgive me and stop me if I get too technical, because I recognise that some of the law around this is very complex. We have been engaging with the representatives of the employees of Carillion, with trade unions and, because it was not highly unionised, we have also been looking to see what representatives could be elected to represent. We have been engaging with them with a view to potential redundancies and starting that consultation process.

The companies have been put largely into compulsory liquidation and when those individuals come, if they do, to transfer to a new employer to continue with the same service, they will at that point be technically made redundant and entitled to a redundancy payment from the Redundancy Payment Service, which The Insolvency Service also
administers. Clearly, what we are seeking to do is to have clarity of communication with those individuals. In many cases, people who are providing directly, particularly the facilities management services, are quite likely to be offered reemployment by either those contracts being taken in-house by public or private sector service receivers or the contracts will be picked up by a different provider.

For the frontline people providing services, it is quite likely that many of them will continue to be employed. We have been trying to be as clear as we possibly can in communications with them about what we are doing about that, what the prospects might be for their employment to continue with a different employer, as well as being honest that in something as widescale and, frankly, devastating as this, it is unfortunately the case that a significant number of people will lose their jobs.

Q143 Ruth George: Thank you. What about the employees who are not engaged on direct contracts? I have had some evidence from constituents that they have had no communication whatsoever and have no idea of what their employment position or financial position is now, which makes it very difficult for paying mortgages, childcare, all the basic facts of everyday life that hit people.

Sarah Albon: We have been using the company’s existing methods of communication with its employees. It started with a major stand-up of the 1,200 or so most senior employees on the day of the insolvency to give them an oral briefing of what had just gone on and what the immediate implications of that would be and to provide them with materials that they could then use to brief people all the way through the rest of the company.

However, we were certainly aware that there were some particularly remote workers who have tended to use their mobile phones to receive messages rather than have a regular actual conversation with their managers and bosses. We have been doing our very best to give direct information to all employees, but all I can suggest is, for individuals who are contacting you, who are not hearing what they need to hear, if you could put them in touch with us, we would be very happy to make sure that communications do happen with them directly.

Ruth George: Thank you.

Chair: We are going to have to move on now to the next session. Thank you very much, Stephen and Sarah.

Q144 Frank Field: Could I ask a very quick question? It relates to our joint inquiry into BHS. You are doing an inquiry. The Secretary of State said it would be fast tracked. The Prime Minister said, before she moves, she is waiting for this report, as are many other people. Please, Sarah, when is it going to be delivered?

Sarah Albon: I cannot say more than imminently, but it really is very imminent now.
Frank Field: Brilliant.
Chair: Thank you very much.
Frank Field: Goodwill. Thank you very much.

Examination of witnesses

Witnesses: Chris Martin and Robin Ellison.

Q145 Frank Field: We have again Chris and Robin, don’t we? As with BHS, might you introduce yourselves for the sake of the record?
Robin Ellison: My name is Robin Ellison. I am the chairman of the larger group of the Carillion pension schemes.
Chris Martin: I am Chris Martin of Independent Trustee Services. I was appointed as a director of the trustee company on 8 January 2018.

Q146 Ruth George: Mr Ellison, as Chair of the Board of Trustees of the DB Pension Scheme, did you feel that you were being kept informed of the company’s financial issues and corporate transactions transparently enough?
Robin Ellison: Yes. With hindsight, maybe not enough. We have a joint trustee for six of the schemes, all DB and all closed, and there were about seven other schemes that I was not trustee on. I can only really talk to the schemes we were involved with.

In relation to financial information, pretty much from 2007, when I first became involved, and then 2011, when I became chairman of the joint trustees, we engaged with the company continually, looking at its figures. Later on, from 2007, we engaged covenant advisers to help us understand the position of the company, and in particular to explore the level of contributions that we thought they were able to pay to us, which they felt they were not able to pay to us. Did we have sufficient insight? We had the insight that was available to us through the public accounts and through certain management information that was disclosed to the covenant advisers from time to time.

Q147 Ruth George: You were engaged with the company on the payments that it was making into the pension scheme. Did you feel that there was agreement between the trustees and the company in those payments, and when did any conflict over that begin?
Robin Ellison: “Conflict” is probably the wrong word. We did not really ever get to an agreement on the difference between what the company thought it could afford and what we thought it could afford. There was a difference in the pension scheme pretty much from when I became involved in 2007-ish, and the question was how quickly they could discharge that deficit. We had a plan that discharged the deficit, in those days, in about seven or eight years.
Then, as the deficit worsened due to circumstances really outside the company’s control and our control, we sought additional contributions pretty much at every valuation. In all these cases, it is a question of balance between the interests of the company itself, the members of the pension scheme—we all know this in the room—and the shareholders. Trying to get that balance right has been a challenge for us. We thought we were entitled to a bit more than the company thought we were entitled to. That debate continued pretty much for the 10 years I have been involved.

Q148 **Ruth George:** At what stage did The Pensions Regulator become involved, and were you in dialogue with the regulator?

**Robin Ellison:** Yes. The regulator has been involved pretty much from the beginning. My understanding was that Carillion was considered one of those schemes they wanted to keep an eye on pretty much early on.

Q149 **Frank Field:** What did keeping an eye on them mean?

**Robin Ellison:** I was not quite sure, but they took more interest in us than they took in some other schemes. They had a list of people they particularly wanted to look at, and we were one of them.

Q150 **Frank Field:** What do you mean by that, though? They took a bit more interest in you?

**Robin Ellison:** Their term is “proactive engagement”, and they proactively engaged with us more than they had done with other schemes I am chairman of, and they did.

**Frank Field:** God help the other schemes. Sorry.

Q151 **Ruth George:** Across the six schemes, the recovery payments were nearly all backloaded. Why didn’t the trustees push the company? Four were able to more effectively push the company.

**Robin Ellison:** Sure. No, it is a dilemma. I have to say I had and I have a very independently-minded board of directors. We are technically directors of the trust company, but all the directors of the trust company were independently-minded. We fought pretty hard. If you look at our correspondence, some of which has been disclosed, you will see that the negotiations went on in a pretty stern fashion. In fact, for the first two valuations, we did not come to a formal agreement, and in fact we just had to take what the company would pay. It caused a certain discussion with the regulator, who became involved at that time. The powers of pension fund trustees are limited and we cannot enforce a demand for money.

Q152 **Ruth George:** I think at one stage you said that you recommended that the trustees requested a negative pledge undertaking from the company to ensure no security could be granted without notification. Did you seek it?
Robin Ellison: Yes, we sought a number of assurances there. Other pension schemes take different kinds of credits or security on assets and things like that. The difficulty with Carillion, as has just been discussed in the earlier evidence that was given this morning, is that, by and large, there was not much in the company that could be pledged.

Q153 Frank Field: You were not relying on their goodwill.

Robin Ellison: The accounting rules are as complex to me as they are to many others.

Frank Field: They are not that complex.

Robin Ellison: The issue for us was: was there security that we could take? We sought security where there was, but in practice there was not.

Q154 Ruth George: Mr Martin, you have heard that The Pensions Regulator was involved. What was your view on the negotiations between the trustees and the company on the level of deficit reduction?

Chris Martin: I started on 8 January this year, so I was not party to any of those discussions at the time. Since coming on board, it is fair to say it was a stage where all focus was on trying to find some solution over that period—clearly, we were unsuccessful—in the week prior to the liquidation.

Q155 Frank Field: Chris, who suggested you should come on board in January?

Chris Martin: I was first approached at the beginning of October last year.

Frank Field: By whom?

Chris Martin: By the trustees’ legal advisers, and subsequently met, I think at the end of November, with a representative of the company, which I guess you would call an interview process. I was asked to sign a non-disclosure agreement on 21 December, and then first engagement in earnest was on 3 January.

Q156 Ruth George: Your engagement is obviously very limited time-wise. Would you have signed off on a deficit recovery plan lasting up to 15 years?

Chris Martin: We work with a scheme-specific funding regime, which means that each of our trustees sits down and looks at the circumstances of its scheme and the circumstances of its employer, level of investment risk it is willing to take, and it comes to a conclusion on those facts. I assume that the trustees negotiated robustly; I have no reason to think not. If the circumstances were ones that justified a 15-year recovery plan, it is something I could sign up to.

Q157 Frank Field: You have talked about minutes, correspondence and so on, Robin. Might we have your complete set of minutes when you came on to
the board?

**Robin Ellison:** Yes, Chairman. The logistics might be a challenge, but absolutely.

Q158 **Frank Field:** All the correspondence of the company, letters to and from The Pensions Regulator, and the advice you got and from whom about allowing the company to suspend its contributions.

**Robin Ellison:** Yes, we have no problem with that. I will not remember it now, but if the secretary writes to me, we will certainly supply that.

**Frank Field:** Thanks.

Q159 **Heidi Allen:** I do not want to put words into your mouth, Robin, but is it fair to say that you felt a little on the outside looking in? Were you happy with the level of dividends that the company was looking at, the excessive debt-to-equity ratio of 5.1, when normally over 2 starts to raise eyebrows, the fact that—it seems to me at least—they were just buying more and more businesses for the purposes of maintaining cash flow? It was all about jam tomorrow. Is that a fair reflection? Is that how you felt about the way the company was being run?

**Robin Ellison:** It is partly a fair reflection. I would not say it is not fair, but there were other elements to it. Our job was to get as much money in for the pension as we possibly could. Involved in that is not only acquiring cash, which is really important, and managing the money that we have, which is equally important, but also ensuring, within reason, the survival of the sponsor who is going to be paying the money in the future. Getting that balance involves tough calls.

Q160 **Frank Field:** You did not in this case, did you?

**Robin Ellison:** We did not. I would like to come to that in a moment, in the final failure. In relation to the way the company was trading, when I joined the company was hit by two adverse events, which were obviously unanticipated. One was the credit crunch in 2007-08, and that knocked 20% off the turnover of the company overnight and really hit its cash flow pretty hard. At that time, the pension scheme was only taking—

Q161 **Heidi Allen:** Sorry. Did that damage the business or just give a knock to its goodwill? A good business has a good business model and—

**Robin Ellison:** I was not that close to the business, but any external observer would know it would have been a hurt to the business. It obviously damages—

Q162 **Heidi Allen:** My argument, having my own businesses, is if they are built on solid foundations, yes, the mood music and financial markets can fluctuate, but you are still sound.

**Robin Ellison:** Yes. I thought it was robust in dealing with an immediate crisis. I was quite impressed with the fact that it downsized as quickly as
it did. It obviously had an enormous effect on its cash flow and its cash position, but there was not a reason to suspect the company would not continue to trade. In fact, there was a reason to think it would continue to trade because it took robust views. If I can look at a parallel situation, Balfour Beatty, which was a major competitor of Carillion, hit equivalent headwinds but had a much worse financial performance. It had seven profit warnings in a very short period of time. Carillion seemed to do, in those days, better than its competitors in downsizing itself to meet the headwind.

The other headwind it took at that time, which was pretty heavy, was it bought a company, I think called Eaga, which it pretty soon had to write off—it cost £300 million or £400 million, something like that—because of the change in the feed-in tariffs. The company virtually became worthless. The view of the trustees at that time, in 2003, was that if the company was well managed it would survive those headwinds and come out the other end with a stronger ability to pay contribution to pension schemes.

We look at lots of metrics, but there were two metrics that gave us slightly more comfort than perhaps they might have done. One was the margins it was making. Normal construction margins in the industry—and this is debated elsewhere in the press—were around 1.5% to 2%, which are really very small. If you have one mistake on a bridge or something, you are in trouble. The company over time, towards the end of 2016, was edging up those margins from around 2% to 5% and that gave us some comfort.

Q163 **Heidi Allen:** Were they real margins? We have heard about aggressive accounting and saying what they would like the figures to be, not saying what they actually are.

**Robin Ellison:** It is a good question, but the disclosed margins that we were informed about were an improvement in the margins, and that gave us some comfort. Also, the profits were increasing. If you look, for example, at the competitor, Balfour Beatty, which had a really bad time for a while, it had been turned around very successfully—

Q164 **Frank Field:** The profits were going to shareholders and the bosses and not into your funds.

**Robin Ellison:** We can come to the balance between dividend and contributions in a moment.

Q165 **Heidi Allen:** Just on that, if I may, you referred already to advice that you took. Gazelle, for example, was one of the organisations that provided the trustees advice back in 2012. It is absolutely damning, “Carillion has historically prioritised other demands”—that is back in 2012 they are saying “historically”—on capital ahead of deficit reduction in order to grow earnings and support the share price”. It gave you a number of recommendations, “We recommend the trustees request a
negative pledge undertaking from the company to ensure that no security can be granted without notification. Trustees may wish to consider requesting a formal support structure in respect to the investment policy.” Did you do either of those things? Have you paid for this advice that you have received?

Robin Ellison: Yes. We sought a lot of them and, to pick up Chris’s words, we engaged in robust discussions with inadequate results.

Q166 Heidi Allen: What struck me in the response from both yourself and The Pensions Regulator, whom I know we are not hearing from yet, to the Chair’s recent letters, it feels very much to me like in the early days not a lot happened between you, but some of the tone of the letters, as you were describing historically, “We worked closely”, suddenly “closely” seemed to be the thing that you were both doing together. Should that relationship have been closer sooner? You were clearly getting nowhere with Carillion.

Robin Ellison: Yes. I think the sums got greater as time went on, obviously for reasons we all know. In the early days, although we were unsatisfied with the contributions that the company was making, we could understand in part the reasons for the company’s caution and the deficits were not as scary as they later became. You could understand the regulator—

Q167 Frank Field: Caution with you, but not with their shareholders. Like goodwill, it has all gone one way, hasn’t it?

Robin Ellison: Yes. We are in the hands, in a way, of the advice we sought. It is a difficult call for trustees.

Q168 Frank Field: You have a report there, which Heidi has raised, which says that they did not deliver anything to you. Did you report that to The Pensions Regulator?

Robin Ellison: I am not sure that all the reports went over to the regulator, but the discussions were reported to the regulator.

Q169 Heidi Allen: Surely, all this advice would be ammunition for you to say, “Come on, regulator. I need your help here. We are getting nowhere”.

Robin Ellison: Yes, indeed. We did ask the regulator to call but it is a difficult—I am not here to defend the position of the regulator, but I do sympathise in some ways with the dilemma that the regulator has. We have a dilemma that in one way we want as much money as we can. On the other hand, we do not want to destroy the company. We do our best in getting that balance right. Just bear with me. The regulator has a triple conflict, which is that it has to protect the members, it has to protect the survival of the company—that is its statutory obligation—and it has to protect the interests of the Pension Protection Fund. Getting that right is a challenge for any regulator.

Q170 Frank Field: The regulator got all three wrong, didn’t it?
Robin Ellison: It did the best it could with the information at its disposal at the time, as did we.

Heidi Allen: The other thing I read somewhere was that, again, in the spirit of closer working towards the end, the regulator became involved in meetings where you would have yourselves as trustees, the board, and also creditors to try to find that balance, I suppose.

Robin Ellison: Yes.

Heidi Allen: It strikes me that as recently as September 2017 you were having conditions imposed, “No, you can’t have more pension contributions because the bank, to lend us some more, says that an organisation should not be prioritising pension contributions”. I find that irresponsible lending. Was The Pensions Regulator involved in that conversation? Do you think the bank should have put that condition on that?

Robin Ellison: I would like to take it back a bit. There were two stages in this. The company was trying to manage its cash flow and, as a token of good faith, it asked us would we take a suspension of contributions for six or seven months? We dissembled on that for about a month or two. We were not really very keen on that at all because we could not see the point of it, although we were sympathetic to the company’s cash flow situation and their expectation that they would come out of their cash flow problem by April this year. Later, the discussion changed radically to—

Heidi Allen: Just on that, bearing in mind that every promise of jam tomorrow was broken—

Robin Ellison: Sure, but it was at a price. We imposed a price for that, so there were very heavy interest charges and there was a bullet payment at the end of the seven months. We understood we were bridging them from a difficult situation. We did not agree to it, but we were exploring agreeing to that. I cannot remember the exact time. August, September, something like that.

Frank Field: Robin, we are in this fantasy world, aren’t we?

Chair: You seem to be very understanding, more understanding than I would be, Robin Ellison, of the company’s position. In Carillion’s annual reports for 2016 neither the chairman nor the CEO mentions pensions in their part of the report. The report as a whole on pensions said, “The group’s net pension deficit has increased during the year, primarily due to a reduction in the AA bond yield following the referendum vote to leave the European Union”. Perhaps that was an issue, but it does not explain the huge deficit accumulated over a 10-year period. It seems to me that you are quite understanding of the company’s position but it does not even pay heed to this issue in its annual reports.
Robin Ellison: Yes. I think it is a good point. I do not think we are responsible for the content of the chairman’s report. I can tell you that in meetings we had with—

Q173 Frank Field: It is a pretty big warning to you, though, isn’t it?

Chair: About where you come in the pecking order.

Robin Ellison: Let me just finish the point. I can tell you that in discussions I had with the finance director over the last seven or eight years, I was informed that pensions was the highest risk identified for the board throughout that period. As I was informed—I do not know how true this is but I can tell you that I was informed—we were the highest risk issue.

Q174 Frank Field: You turned out to be the least risk, didn’t you?

Robin Ellison: I cannot comment on that.

Q175 Frank Field: Chris, might you come in here and comment on Heidi’s line of questioning? You are parachuted in late. How do you respond to the answers that we are getting about the pension fund playing soft ball with the employers?

Chris Martin: I would rather not comment on those negotiations in September, although I can understand why the trustees, faced with a situation where a suspension of contributions was necessary for the lender group to continue supporting business, would actively engage in those discussions and would consider the deferral, which they ended up agreeing to.

By the time I came in in the second week in January, we were in the stage of the process where all options had to be considered, however unpalatable they might normally be in the context of pension provision. We were at the point where the only hope of a long-term outcome for these schemes and for the members’ full benefits was for the trustees to contemplate steps that they would not normally do. We were thinking about long recovery plans and contribution holidays for the employer.

Robin Ellison: Chairman, can I make a point for the record? It might be misleading to come to the apprehension that we were soft with the company. The records show—and a lot of the correspondence will show—that we were as tough, within limits, as we could be, and we did not agree any of the contribution plans for two or three years. We were not just sitting there playing patsy to the company’s offer. We absolutely did not.

Q176 Heidi Allen: I am very black and white in life. As a new MP, it makes me smile when I hear of traditional MPs, “Yes, I have written a strongly-worded letter to the Minister”. “Oh, that has dealt with it, then.” Letters are not enough; it is action. Chris, you have just described the trustees having to take steps that would normally be unpalatable. It feels like that was not just in September; that had been happening for a long time.
Robin, are you satisfied with the attempts that the trustees and the board of trustees made, and are you satisfied with The Pensions Regulator's involvement in this also?

Robin Ellison: It is a good question. So far as my board is concerned—and we have obviously reviewed it internally since the collapse—I do not think there is anything more, even with hindsight, we could have done to persuade higher contributions to be paid.

Q177 Frank Field: Could The Pensions Regulator have done more?

Robin Ellison: The Pensions Regulator has the right to compel additional contributions. I am not going through the remedies, but there are several remedies available to it. Sitting with our pension fund hat on, it would have been nice if it had compelled the company to another. We were expecting in the order of £10 million to £15 million in additional contributions a year to do that.

Q178 Frank Field: The company borrowed, though, to pay dividends. Why didn’t you step in at that point with the regulator?

Robin Ellison: The correspondence will show that we did ask the company whether or not it would explore borrowing to pay pension contributions because there was a kind of trend of borrowing to pay—

Q179 Heidi Allen: Sorry. Borrowing to pay pension contributions. Why not just less dividends?

Robin Ellison: A good question. The regulator’s view—and I was not too combative with the regulator on this—is that there is a balance between the amount of money you pay in dividends and the amount of money you pay in contributions. This is not the magic solution, but if you look at the general market, the regulator is, for reasons it will no doubt explain separately, kind of comfortable with paying a ratio between 16%, 17% and 20% to the pension scheme and the balance of 80% in shareholder dividends. There is a reason for paying dividends, which we all know in this room, you have to keep—just bear with me. We were getting around 60% of dividends, which was—

Q180 Heidi Allen: You could give 100% of dividends. If the organisation is built on quicksand, it does not matter what your percentages are.

Robin Ellison: There are tough choices. Making a call is hard. It is a good question.

Q181 Frank Field: Chris, when you came into the company, The Pensions Regulator could have intervened to compel payments, if I have understood what Robin has said, the law, correctly, and yet the company was borrowing, raising money to pay dividends. Do you not think in those circumstances the board should have been incredibly tough to encourage The Pensions Regulator to say, “We want our share of this borrowed money”? Good enough for shareholders; good enough for pension schemes.
Chris Martin: By the time I came into the board, the company was trading on a day-to-day basis, Frank. There was no discussion about additional contributions at that point, and the outcome was binary at that point. Any intervention by the regulator would only have been an intervention that would have caused the members to end up moving into the PPF anyway. There was nothing by that point that regulatory intervention could have achieved.

Robin Ellison: Could I add to Chris’s point? There might be a slight misunderstanding about the chronology of this. Towards the end of last year, beginning of this year, the company was engaged in raising fresh finance, and it needed two bits of fresh finance. It needed immediate cash flow support and it needed fresh capital injection. It was clear; you did not need to be a brain surgeon to realise this was going on. As part of the cash flow protection—

Q182 Frank Field: When you say it needed capital, it just needed money, didn’t it, to keep it going?

Robin Ellison: Whatever you call it. The immediate call, which it was thought at the time would see them over the hump, was for about £140 million, which the regulator and us and everybody else and the banks were involved in rearranging, and the call was from the banks, from all the financier community, that they were not prepared to put money into the company to see it go into the pension scheme because they wanted to see it going for the trading. The question was, would we take a restricted, modest hit for a period of time in order to enable the company to bridge its cash flow problem towards a better future?

Q183 Heidi Allen: Robin, it was not a modest hit, given even the deficit recovery plans that you had signed off and allowed to come into action. Looking at three of the biggest schemes within the six that you managed, Alfred McAlpine and Carillion, twice in 10 years the plan was revised, Mowlem three times, and the average length of those plans was increased from eight to 16.

Robin Ellison: I am sorry. You are looking at the repayment period. Yes.

Q184 Heidi Allen: Yes. In terms of modest payment holiday into the pension scheme, that is just not right. It would have been a payment holiday. An ineffective plan was agreed by the trustees for decades.

Robin Ellison: It was a deferral; it was not a holiday. It was a deferral, with a bullet payment at the end.

Q185 Heidi Allen: If a deferral follows a deferral follows a deferral, that is a holiday.

Robin Ellison: It is a question of balance. If you look at the increase in the deficit, which was beginning to balloon up, the question is: what was the alternative? The reason for the increase in the deficit was partly fiscal compression. In other words, interest rates were being forced out. We
had some longevity issues. We had a longevity swap, which cost us quite a lot of money, which was done to protect the scheme but eventually cost quite a lot. A lot of the protection mechanisms that we built in were paradoxically increasing the deficit. The question is: at what stage do you bring the company down to pay the deficit? That is a difficult call.

Q186 Frank Field: Robin, reading through all the papers we so far have had, there is a huge exercise of pointing fingers at other people. You are saying, “The banks would not allow us to act”.

Robin Ellison: I am not pointing the finger at anyone.

Q187 Frank Field: Who were the banks who were so tough with you but not so with the company?

Robin Ellison: I do not think it was just the banks. I think it was all the finance. There were private placement notes. There was a collection of financial arrangements. The proposal—of which in fact we rejected some of the requirements out of hand—was that we would play our part in helping the cash flow over to a period when they would recover. We thought that was sensible.

Q188 Frank Field: Did the Government know all of this was going on? Did the Government know? The Government were awarding contracts.

Robin Ellison: I do not know. I was part of discussions with the Cabinet Office from early January but not before, so I do not know what happened before then.

Q189 Heidi Allen: A final question and possibly an unfair one, but, Robin, do you think you fought hard enough for the people with pensions?

Robin Ellison: Can you always do better? The answer is, yes, you can always do better. Did we fight pretty hard? I think we overdid it in some respects. We were pretty tough. None of the recovery plans were agreed. They were imposed. Could we have done better? Possibly, but I think we did as much as we possibly could.

Q190 Heidi Allen: Chris, it is very early for you and I do not know whether it is possible to ask you a similar question. Given your experience in this sort of situation before, are there any glaring alarm bells that have been ringing to you already in terms of, “Shouldn’t have done that. Should have done this differently”?

Chris Martin: Other than the highest level of business that was generating perhaps 4% margins, and that was high for its sector. Therefore, it was always going to be fragile, and it seemed to have a history of buying other business with DB pension liabilities. At that level, the warning bells would have been there. In fairness, the trustee board has not spent time forensically examining what went on over the last 10 years because I have to say my focus is on trying to get the members to a better place now.
Q191  Frank Field: Robin, did you at any stage ask the regulator to intervene in specific ways?

 Robin Ellison: There is a letter where we said to the regulator, "We can’t really agree with the company. We are really struggling".

Q192  Frank Field: That is not my question. Did you ask the regulator to use any of the powers of the regulator to help you?

 Robin Ellison: No. We sought its intervention in the way it thought best.

Q193  Frank Field: The answer is no. Chris, are you surprised the regulator was not requested to be more active?

 Chris Martin: My understanding is that the regulator was actively involved in meetings, was sharing all of the information to—

Q194  Frank Field: No, but using the powers the regulator has, were you surprised that it was all about talk and holding meetings, writing letters, recording minutes?

 Chris Martin: The basic experience of other cases is that once the regulator is proactively engaged and is attending trustee meetings on a regular basis, it takes decisions itself as to whether it thinks its powers are engaged at that point. I do not think it needs the trustee to call them to do it.

Q195  Frank Field: It was still in the talking stage, wasn’t it?

 Chris Martin: So I understand.

Q196  Chris Stephens: Can I ask you, Mr Martin, on a similar point to the Chair? Do you think The Pensions Regulator should have been more proactive in challenging the behaviour of the company, particularly on the recovery payments and the level of recovery payments?

 Chris Martin: Again, I did not have the benefit of sitting through those meetings and I have not been through the historic correspondence, but it certainly had identified Carillion as a sponsor and its DB schemes as schemes that it would pay close attention to. It was proactively engaged. It means that those schemes were quite exceptional in the fact that the regulator was attending trustee meetings. That does not happen all the time. The regulator does not have the resource to do that. I think it was engaged at a good level. Whether it could have considered exercising its powers at an early stage is something I would not want to comment on without having been there at the time.

Q197  Chris Stephens: Mr Ellison, do you think The Pensions Regulator could have been more proactive?

 Robin Ellison: It is one of those impossible questions. It is a very good question, but as your colleague Heidi Allen said, there is not a bog-standard answer. It makes a judgment call about whether it is the right amount of money or not. Forgive me for being a lawyer for a moment.
There is a principle called the Wednesbury principle, a decision that is made that is so outrageous that a normal human being would not agree to it. I do not think—

Q198 **Frank Field:** In this case?

**Robin Ellison:** In this case, I do not think that the conclusion that came out, while it was not satisfactory or acceptable to us, was so egregious that any ordinary human being would not have come to it. The fact that the regulator accepted the situation did not strike us as so outrageous that we wanted to explode. It was a judgment call that we did not like but we understood.

Q199 **Chris Stephens:** Both of you may be aware of previous Work and Pensions Committee reports where we have suggested that there should be clearance of certain corporate transactions. Do both of you support that, and do you think of that as being available in this case that the situation—

**Robin Ellison:** You mean by the regulator?

**Chris Stephens:** Yes.

**Robin Ellison:** There is a clearance process at the moment for certain corporate transactions— I think they are called class A transactions— which are of such significance that the effect—

Q200 **Frank Field:** That is voluntary, though, isn’t it?

**Robin Ellison:** It is voluntary. The idea is to give you immunity from people coming back to you saying, “You shouldn’t have done it” or “there is a penalty to pay or a price to pay”. It is hard for any external regulator, unless it is a transaction that is transformational, to know whether a corporate transaction is sensible or not. We are watching the GKN story unfold in the press at the moment. It is really hard to know whether a regulator could add benefit to that or just throw fuel on the fire. It is an interesting question, but I am not sure we can add much light to that.

Q201 **Chris Stephens:** Surely it would have challenged the business approach that Carillion would have taken.

**Robin Ellison:** There was continual challenge going on. With some exceptions, it is not for the board of trustees to decide whether the parent company should buy or sell a company or buy a subsidiary. That is outside its scope.

Q202 **Chris Stephens:** Carillion had a large deficit itself, and yet it was purchasing companies like, for example—as have been previously referred to—Mowlem and Alfred McAlpine, which also had large pension deficits. Did that not ring alarm bells to you, Mr Ellison?

**Frank Field:** Like a hospital for sick pension schemes, isn’t it?
Robin Ellison: We do not run the company. The company makes the decisions to buy it. I do not sit in on board meetings. I do not sit in on the business projections. It would be improper for a pension fund to double-guess the company’s strategy on that. I was chairman of the McAlpine scheme when it was brought over by Carillion, and we did a reverse-covenant. In other words, the challenge we were facing was: was Carillion a worse covenant than McAlpine? It was a difficult balance. First of all, we did not have a veto anyway, but on calculation of the covenant the margins that Carillion were making were so small compared with McAlpine that it was a real worry for us. We had discussions with the finance director about what he was doing about margins. History show they might have been misleading but the reports show that the margins were improving. The question you ask is a very good question but there is not—

Q203 Chris Stephens: Alfred McAlpine’s deficit was £110 million and I think some people watching these proceedings would not describe that as—

Robin Ellison: No, it was a comfort to be bought by a big quoted public company, absolutely.

Q204 Frank Field: Given the pension regulator was turning up to your meetings for 10 years—

Robin Ellison: Not for 10 years, for six or seven years.

Frank Field: —and there is this wonderful aggressive policy of acquiring companies with sick pension schemes, what did The Pensions Regulator say to you?

Robin Ellison: I think McAlpine was pretty much the last big pension, which was 2006, 2007, 2008; I can’t remember the exact year. There was not a lot of acquisition going on after that, certainly in the UK. They were buying companies in Canada, I think, and elsewhere.

Q205 Chris Stephens: My last question to Mr Ellison is: in 2014 the company decided to put 2% of its total cash into recovery payments. They were then payments of over £70 million. There were three valuations of which the company were clearly resisting putting in higher contributions and, as you have said yourself, there were robust discussions with the company with inadequate results. The simple question I have to put to you, which I am sure people watching these proceedings are also asking, is: did you consider resigning or did you consider using any whistle-blowing mechanisms to make this more public?

Robin Ellison: I am not sure about resigning. They might have quite welcomed my resignation. I don’t think resigning adds money to the pot. The question is how much money can you get in the pot and we worked as a team to try to get as much money as we could.

Q206 Andrew Bowie: Mr Ellison, you were asked as trustees, we believe in August last year, to agree to defer payments to the pension contributions
for a period, which in September you agreed. We have heard this
morning and read in the evidence that you did so because you believed
that in not doing so you would have rendered the company insolvent. Did
you believe at that stage that the company had a viable and realistic
recovery plan?

Robin Ellison: It is a good question. The answer is we did not know at
the time. We knew that they were working on a business plan and our
present covenant advisers, who were PwC, were reviewing this on a
weekly—I know this may come as an untracked remark but they were
outstanding in the advice they gave us. They were reviewing on a weekly
basis the progress of those plans. There was a series of plans to be done,
one of which was a business plan. It was not really clear until early
January whether there was a robust business plan. In conversations with
the company and its advisers, EY, the—

Q207 Andrew Bowie: You said there was not a robust business plan. What did
you have the right to sign up, given that you had no assurances
whatsoever?

Robin Ellison: We would have agreed to only the deferral on the basis of
the conditions, which were set out. I can't remember if you have a copy
of that document but there was a series of conditions that we agreed with
the banks, the terms on which we agreed that money. It wasn't just we
would give you the deferral and goodbye. There was a process for
repaying that money and provided the banks put the money in we would
get our money at a certain stage. There were two stages; one was April
and one was the following October. We did not roll over and have our
tummys tickled by the banks. There was a robust discussion and we
fought our corner quite hard. To give credit to The Pensions Regulator,
they were involved in those discussions and were pretty robust
themselves before they agreed to that.

Q208 Frank Field: What does robust mean, Robin?

Robin Ellison: I was sitting at a board table at Slaughter and May that
was of gigantic proportion. It must have been 30 or 40 feet long and
because it was such a big table you could not really hear the guys at the
other side. The regulator who spoke was pretty firm in repudiating the
questions of the banks for certain conditions that they wanted in that
request, so they just said no.

Q209 Andrew Bowie: This was just delaying the inevitable with all that you
knew then and know now.

Robin Ellison: The $100,000 question is: was there a business to
recover? The company went bust on Monday, the 15th—I can’t remember
the exact date—and on the Sunday afternoon, the 14th, I was called into
a meeting to see the Carillion board at their lawyers. The impression they
gave me was that they felt that if they could get over the cash flow issue
they thought that by the end of the month they would have refinanced
the company. My understanding was they would not have traded on if
they did not believe the company could continue because they would be personally liable. I believed that they believed that they had a plan for the survival of the company, which was manageable. In the end it was not.

Q210 Andrew Bowie: Do you think the trustees regret the decision in hindsight?

Robin Ellison: With hindsight, no, I don’t think so because if the company had managed to work its way through it and we had not helped it, the recriminations would have been interminable.

Q211 Frank Field: Chris, all the time our Committees are looking at what we can propose and try to persuade the Government to do to prevent these crises, jobs destroyed, shareholder value and pensioners left in the lurch yet again. Do you think one reform that we should consider seriously is that when there are these large deficits, and growing, and a company is very dependent on Government contracts, the regulator ought to have the power to be able to say to the Government, “I cannot give this company that you may be awarding orders to a clean bill of health”? Then the Government starts to take an interest in how companies are governed and the pensions fund deficit is not just a marginal thing that Robin and colleagues and Committee members try to put on to the table, but it becomes a very important part of who is worthy to have public contracts.

Chris Martin: From a pension fund disclosure standpoint, that information is in the public domain on an annual basis. All schemes have to publish and send to all of their members—

Q212 Frank Field: Do you think Chris Grayling was aware of this when he awarded the last big contract to Carillion? Would it not have helped him to have had a note put on by the civil servants, “Beware, this is a company that can’t even fix its pension scheme let alone High Speed 2”?

Chris Martin: I guess my point is that none of this information is kept secret. It is all in the public domain. There has been a lot of focus on what the accounting deficit was or how the accounting deficit moves but the technical provisions deficit, the one the trustees use to fund the scheme, and also the solvency deficit, the much larger number, are published and are available to everybody on an annual basis. Whether it requires the regulator to facilitate the transmission of that information to Government is not for me to comment on but it is out there and available.

Q213 Frank Field: Chris, what reforms do you think we should advocate for the regulator when we come to make our report? A quick answer from Robin as well and then we are finished.

Chris Martin: One that Robin touched on earlier and I think is worth considering is the regulator has four statutory objectives at the moment. I think at least three of them conflict, and quite obviously conflict with
each other, which in fairness to the regulator can’t make its decision-making any easier when it is trying to protect in two directions at once.

Q214 Frank Field: What would you propose on that, please, Chris?

Chris Martin: I would go for a single objective, which is to deliver better outcomes for members of pension schemes. That is it. That is what I think it is there for and that is what members would think The Pensions Regulator is there for. The rest of the framework the regulator works within is too restrictive. We talked a moment ago about binary outcomes. You get to a certain point where the only outcome is insolvency or structured entry into the PPF. From a member’s perspective it is PPF or PPF. There must be something within the legal framework that can recognise that full benefits are not affordable but something higher than PPF could be achieved. At the moment we drive companies and schemes to the wall.

Q215 Frank Field: Chris, might you give us a note on what you think the definition of better outcomes is so we get beyond the goodwill phase in all these discussions?

Chris Martin: I will do my best to do so.

Q216 Frank Field: We are really grateful. Robin, one last point?

Robin Ellison: I back Chris’s final point, which is a really interesting suggestion and I am very supportive of that. One of the things we might explore—and I know it goes against the grain for a Select Committee to do this—is whether the existence of the regulator or the way the regulator operates gives some kind of false comfort to the system and that people rely on it when they can’t rely on it. I wonder whether any regulator, even if it was beefed up to the nth degree, could do the job that it is being asked to do and because it has been given this role people have reposed trust in it that it can’t deliver on. I wonder whether we might have stronger negotiating powers as trustees with a company if the regulator’s powers were restricted in some way. I know that is not the thinking around that.

Q217 Frank Field: Robin, would you give us a note on that as well?

Robin Ellison: I am very happy to do so.

Frank Field: Brilliant. Thank you, Chris and Robin, for coming today. That is the end of our first session.