National Audit Office

Report
by the Comptroller
and Auditor General

Cabinet Office

Investigation into the government's handling of the collapse of Carillion

HC 1002 SESSION 2017–2019 7 JUNE 2018

Our vision is to help the nation spend wisely.

Our public audit perspective helps Parliament hold government to account and improve public services.

The National Audit Office scrutinises public spending for Parliament and is independent of government. The Comptroller and Auditor General (C&AG), Sir Amyas Morse KCB, is an Officer of the House of Commons and leads the NAO. The C&AG certifies the accounts of all government departments and many other public sector bodies. He has statutory authority to examine and report to Parliament on whether departments and the bodies they fund, nationally and locally, have used their resources efficiently, effectively, and with economy. The C&AG does this through a range of outputs including value-for-money reports on matters of public interest; investigations to establish the underlying facts in circumstances where concerns have been raised by others or observed through our wider work; landscape reviews to aid transparency; and good-practice guides. Our work ensures that those responsible for the use of public money are held to account and helps government to improve public services, leading to audited savings of £734 million in 2016.

National Audit Office

Cabinet Office

Investigation into the government's handling of the collapse of Carillion

Report by the Comptroller and Auditor General

Ordered by the House of Commons
to be printed on 5 June 2018

This report has been prepared under Section 6 of the National Audit Act 1983 for presentation to the House of Commons in accordance with Section 9 of the Act

Sir Amyas Morse KCB
Comptroller and Auditor General
National Audit Office

4 June 2018

HC 1002 | £10.00

This investigation describes the government's exposure to Carillion before the company's collapse in January 2018, and the actions the government took to protect public services.

Investigations

We conduct investigations to establish the underlying facts in circumstances where concerns have been raised with us, or in response to intelligence that we have gathered through our wider work.

© National Audit Office 2018

The material featured in this document is subject to National Audit Office (NAO) copyright. The material may be copied or reproduced for non-commercial purposes only, namely reproduction for research, private study or for limited internal circulation within an organisation for the purpose of review.

Copying for non-commercial purposes is subject to the material being accompanied by a sufficient acknowledgement, reproduced accurately, and not being used in a misleading context. To reproduce NAO copyright material for any other use, you must contact copyright@nao.gsi.gov.uk. Please tell us who you are, the organisation you represent (if any) and how and why you wish to use our material. Please include your full contact details: name, address, telephone number and email.

Please note that the material featured in this document may not be reproduced for commercial gain without the NAO's express and direct permission and that the NAO reserves its right to pursue copyright infringement proceedings against individuals or companies who reproduce material for commercial gain without our permission.

Links to external websites were valid at the time of publication of this report. The National Audit Office is not responsible for the future validity of the links.

006378   06/18   NAO

Contents

The National Audit Office study team consisted of:
Jeremy Gostick, Sarah Taylor,
Harry Hagger Johnson,
Andrew Denney, David Betteley
and Marc Adams, under the
direction of Joshua Reddaway

This report can be found on the National Audit Office website at www.nao.org.uk

For further information about the National Audit Office please contact:

National Audit Office
Press Office
157–197 Buckingham Palace Road
Victoria
London
SW1W 9SP

Tel: 020 7798 7400

Enquiries: www.nao.org.uk/contact-us

Website: www.nao.org.uk

Twitter: @NAOorguk

What this investigation is about

1 On 15 January 2018 the Carillion group of companies (Carillion) declared insolvency and the Official Receiver, an employee of the Insolvency Service, started to liquidate its assets and contracts. Carillion was a British multinational company that provided facilities management and construction services. It operated in the UK, Canada and the Middle East and employed around 45,000 people. At the time of liquidation it employed around 18,200 people in the UK.

2 At the point of liquidation Carillion had around 420 contracts with the UK public sector including direct contracts, sub-contracts and special purpose vehicles to deliver private finance schemes.[1] These included services for hospitals, schools, the armed forces, prisons and transport. Some of these contracts were joint ventures with other companies.

3 The Cabinet Office asked the Insolvency Service to continue to operate Carillion's service contracts through the Official Receiver to ensure continuity of public services. In return, it gave the Official Receiver £150 million of initial liquidity. The Insolvency Service told us that this was the first example of a public limited company continuing to trade while being wound up.

4 Carillion's collapse has triggered several Parliamentary investigations and inquiries by: the Work & Pensions and Business, Energy & Industrial Strategy Select Committees, focusing on Carillion's corporate governance and the consequences for its pensions schemes; the Public Administration and Constitutional Affairs Select Committee and Committee of Public Accounts, focusing on the lessons for government outsourcing more generally; and a hearing of the Liaison Committee.

---

[1] Although these use a variety of private finance funding models we refer to them in the report as 'PFI' schemes for ease of understanding.

5 This report focuses on the role of the UK Government in preparing for and managing the liquidation. We have not assessed the actions of Carillion, its directors, or its advisers. Investigations into the conduct of the company and its board members are being carried out by: the Financial Conduct Authority; the Official Receiver; the Pensions Regulator; and the Financial Reporting Council. This report has five parts:

- Carillion's role in the market for government services (Part One);
- the Cabinet Office's monitoring of Carillion as a strategic supplier (Part Two);
- the government's contingency planning for Carillion's possible failure (Part Three);
- the government's response to Carillion's request for support (Part Four); and
- Carillion in liquidation (Part Five).

6 Our methodology is set out in Appendix One.

Summary

Key findings

Carillion's role in the market for government services

1 **Carillion was a strategic supplier to government with around 420 contracts with the UK public sector.** These included contracts for facilities management, catering, road and rail maintenance, accommodation, consultancy, and construction. By value, Carillion was central government's sixth largest supplier in 2017. Public sector contracts accounted for 33% of Carillion's total revenue and 45% of its UK revenue. However, its total government revenue was not growing, and was lower than it had been before 2012 (paragraphs 1.2 to 1.5 and Figures 1, 2, 3 and 4).

2 **The value of Carillion's public sector contracts varied widely, from those that were highly profitable to those that incurred significant losses.** Carillion's business unit which provided facilities management services to central government was only just profitable (1% operating margin projected in 2017). However, its local government contracts were generally more profitable (13% to 15% operating margin). Set against these were several high-profile PFI projects expected to incur significant losses. In 2017 Carillion faced estimated annual losses of £91 million on its joint venture project to build the Aberdeen bypass, £83 million on building the Royal Liverpool University Hospital and £48 million on building the Midland Metropolitan Hospital (paragraphs 1.6 to 1.7 and Figure 6).

The Cabinet Office's monitoring of Carillion as a strategic supplier

3 **Government monitored Carillion as part of its risk management system for strategic suppliers.** Up to August 2017 the Cabinet Office had rated Carillion as either green or amber since it published its risk assessment policy for strategic suppliers in 2012. Since February 2016, Carillion had been rated as amber because of performance concerns on important central government contracts. Since 2013 the Cabinet Office had regularly raised with Carillion its delayed payments to sub-contractors, and the short selling of its shares. The Cabinet Office did not have a crown representative in place for Carillion from July to October 2017. In the meantime, the role was taken on by the Director for Markets and Suppliers, who is responsible for the relationship with all strategic suppliers (paragraphs 2.2 to 2.6 and Figures 7 and 8).

4 **The scale of Carillion's 10 July 2017 profit warning was a surprise to the government.** Carillion's 2016 accounts were published in March 2017 and showed the company as profitable and solvent. Carillion made three profit warnings in 2017: on 10 July Carillion announced a £845 million provision for losses on its contracts; on 29 September it increased this to £1.05 billion; and on 17 November it announced that it expected to breach the terms of its loans. The scale of the losses announced on 10 July came as a surprise to the Cabinet Office as it contradicted previous discussions with Carillion and market expectations (paragraphs 2.7 and 2.11 and Figures 9 and 13).

5 **The Cabinet Office raised its risk rating of Carillion to red in September 2017 but did not raise Carillion's rating to its highest risk category before it collapsed.** The Cabinet Office raised Carillion's risk rating to red in response to the July 2017 profit warning. It took steps to improve its information about Carillion's financial health, including regular access to some of Carillion's internal financial information and it had regular contact with Carillion. Following a further profit warning in November 2017, the Cabinet Office wrote to Carillion to say that it proposed rating Carillion as its highest risk category, 'high risk'. Carillion replied that the Cabinet Office already had access to the financial information required by this rating, and the rating would risk precipitating its financial collapse. The Cabinet Office accepted these arguments (Figure 7, paragraphs 2.5 and 2.13 and Figure 14).

The government's contingency planning for Carillion's possible failure

6 **Carillion announced £1.9 billion of new government work after the 10 July profit warning.** Two joint venture defence contracts had been signed before the profit warning. HS2 Ltd approved two joint venture contracts worth £1.3 billion before 10 July but signed them afterwards. Network Rail confirmed the next phase of one contract worth £63 million after the second profit warning in September. In total eight contracts and variations were announced. None of the contracting authorities believed they had grounds for disqualifying the bids under procurement rules and in all but one case joint venture partners were obliged to finish the contracts if Carillion failed (paragraphs 3.10 and 3.11 and Figure 16).

7 **The Cabinet Office's coordination of contingency planning in case of Carillion's failure began in July 2017, gained momentum from October, and was complete for central government by mid-January 2018.** It started contingency planning within central government as early as July, but first had to carry out additional work to establish a complete list of government contracts. The process accelerated in October, but some departments did not respond until the minister for the Cabinet Office wrote to them in December. The Cabinet Office was still seeking information on schools and local authorities at the point of liquidation. Ultimately, the Cabinet Office received 65 contingency plans from 26 public bodies, fewer than the number sought. We found that 16 public bodies out of 26 (62%) did not provide costed preferred options as requested. Of the £238 million estimate from the others, £147 million related to Network Rail contracts. Network Rail told us that this was a worst-case scenario and it expects actual costs will ultimately be much lower (paragraphs 3.2 to 3.9 and Figure 15).

Post publication this page was found to contain an error which has been corrected (Please find Published Correction Slip)

The government’s response to Carillion’s request for support

8 **In early January Carillion asked the government for £223 million to help it through to April 2018 and additional support with its financial restructuring.** In December 2017, Carillion’s main creditors had told it that they would not give further short-term funding unless Carillion also approached Government. Carillion asked for a £160 million loan or guarantee of bank lending from the Cabinet Office (which could be partly offset if government paid disputed claims of £39 million) and a £63 million temporary deferment of tax. Repayment of the loans and ending the government guarantees was contingent on a successful financial restructuring of the company by April 2018. Carillion also requested help with the longer-term financial restructuring including: asking the Cabinet Office to provide up to £125 million towards the completion of Midland Metropolitan Hospital PFI scheme in return for an equity stake; favourable settlement of claims with public sector customers; and support in arranging a solution for the £2.6 billion pension liabilities with the Pension Protection Fund, Pension Trustees and Pensions Regulator. Not all items were quantified or quantifiable (paragraphs 4.2 to 4.7 and Figure 17).

9 **The Cabinet Office decided it was better that Carillion enter into a trading liquidation than to provide financial support.** The Cabinet Office discussed Carillion’s request for support with Carillion and its creditors up to the 14 January, but decided it would not support Carillion because it had serious concerns about: Carillion’s business plans; the legal implications; the potentially open-ended funding commitments created; the possibility of setting a precedent, and the concern that Carillion would return with further requests. The Cabinet Office carried out an options appraisal and concluded that the best result for government across a range of criteria would be a trading liquidation – that is, where Carillion entered liquidation, but would continue to provide services until other arrangements could be made for each contract (paragraphs 4.10 to 4.14 and Figures 18 and 19).

10 **The Cabinet Office made final preparations for the liquidation of Carillion before it told Carillion it would not provide support.** The Cabinet Office set up a crisis management centre to handle communications, briefed and received permission from both the Chancellor and the Prime Minister and prepared to inform Parliament of the financial consequences in the week beginning 8 January. Officials made the final decision on 14 January to tell Carillion that it would not provide support but would fund a trading liquidation. When Carillion’s main creditors then told Carillion they too would not provide any further support, this left Carillion’s board with no choice but to file for liquidation with the High Court on 15 January (paragraph 4.15 and Figure 18).

Carillion in liquidation

11 **Carillion staff continued to provide public services.** The Cabinet Office agreed to fund the continuation of public services and successfully conveyed the message to Carillion staff that they should report for work as usual. Carillion's joint venture partners took over many of the larger construction projects. The Ministry of Justice established a new government company to run the prisons facilities management contract. The Cabinet Office believes almost all services continued uninterrupted. However, some of the construction contracts, including the two PFI hospitals, are mothballed until the PFI investors find alternative construction companies (paragraphs 5.5 to 5.6).

12 **The Official Receiver currently expects all customers to have ended their Carillion contracts or transferred them to new suppliers by the end of June 2018.** On 23 May, 21 public sector contracts remained within the insolvency regime. At the end of May the Official Receiver expected to be still providing support services for a specified period beyond the termination of the contract for a further 31 contracts (paragraph 5.7 and Figure 20).

13 **The Cabinet Office will ultimately pay the loss on the liquidation, currently estimated at £148 million.** The liquidation is expected to make an overall loss mainly because post-liquidation income will not fully cover the cost of the provision of public services. The estimated £148 million loss is subject to a range of uncertainties, and it will take a long time to establish the final actual cost. This £148 million would be covered by the £150 million the Cabinet Office has already provided to help finance the costs of liquidation. The total cost to the taxpayer will be higher than this because some public sector bodies are paying a 20% premium for post-liquidation services and some customers will incur costs in replacing Carillion as a contractor. Many public sector customers, including the special purpose vehicles delivering PFI contracts, are objecting to paying this, and many dispute outstanding invoices relating to the period before liquidation. The £148 million is lower than the rough estimate made by the Cabinet Office before liquidation of £314 million to £374 million (Paragraph 4.9, 5.8 to 5.10 and Figures 19 and 21).

14 **Former Carillion workers, investors and other creditors will also bear losses.** Thirty-one of Carillion's 198 companies are in liquidation. So far, 64% (11,638) of the Carillion UK workforce have been found new work, 13% were made redundant, and the remainder are still employed by Carillion. Carillion's pension schemes will enter the Pension Protection Fund. Carillion's non-government creditors are unlikely to recover much of their investments. However some creditors will be paid because they are owed money by Carillion subsidiaries with positive net assets. The government has not measured the impact on the supply chain, but there has been limited take-up of lending facilities by affected small and medium-sized enterprises (paragraphs 5.7 and 5.13).

Part One

Carillion's role in the market for government contracts

1.1 This part of the report sets out:

- the scope and scale of Carillion's relationships with government;
- the importance of Carillion to government; and
- the importance of government to Carillion.

Carillion's government contracts

1.2 When it collapsed in January 2018 we estimate Carillion had around 420 public sector contracts across central and local government, NHS bodies, schools and others (**Figure 1** on pages 12 and 13).[2] We had to estimate this number. It was not always clear to what extent contracts extended across a number of organisations, or where there were multiple contracts for one site. Its services and construction work fell into three categories:

- support services, including facilities and energy management, road and rail maintenance, accommodation and consultancy;
- public-private partnerships, including buildings and infrastructure; and
- construction services, including building and civil engineering.

1.3 Carillion reported revenue of £1.72 billion from the UK public sector for the calendar year 2016.[3] **Figure 2** on page 14 shows estimated amounts paid by public bodies to Carillion for the financial year 2016-17, supplemented by additional data from Carillion to indicate the scale of income from other sources such as schools and NHS bodies. We do not have information for local authorities.

---

[2] The number of contracts recorded as entering liquidation, however, is significantly different (paragraph 5.3).

[3] The accuracy of Carillion's accounting practices has been criticised and is subject to investigation by the Financial Reporting Council. We state where we have used Carillion's accounts.

The importance of government to Carillion

1.4 Carillion's accounts record that UK public sector revenue represented 33% of its £5.2 billion global revenue in 2016, and 45% of its UK revenue (**Figure 4** on page 16). Levels of UK public sector revenue were broadly steady over the last four years, although this business declined as a share of total revenue as Carillion's global revenues increased.

The importance of Carillion to government

1.5 Carillion was the sixth largest supplier to central government departments in 2016-17. Most of Carillion's services to central government departments were construction and facilities management, where we estimate Carillion had market shares of 11.3% (£422 million) and 6.3% (£323 million). We believe there were no other markets in which Carillion had more than a 1% share (**Figure 5** on page 17).

The profitability of Carillion's government contracts

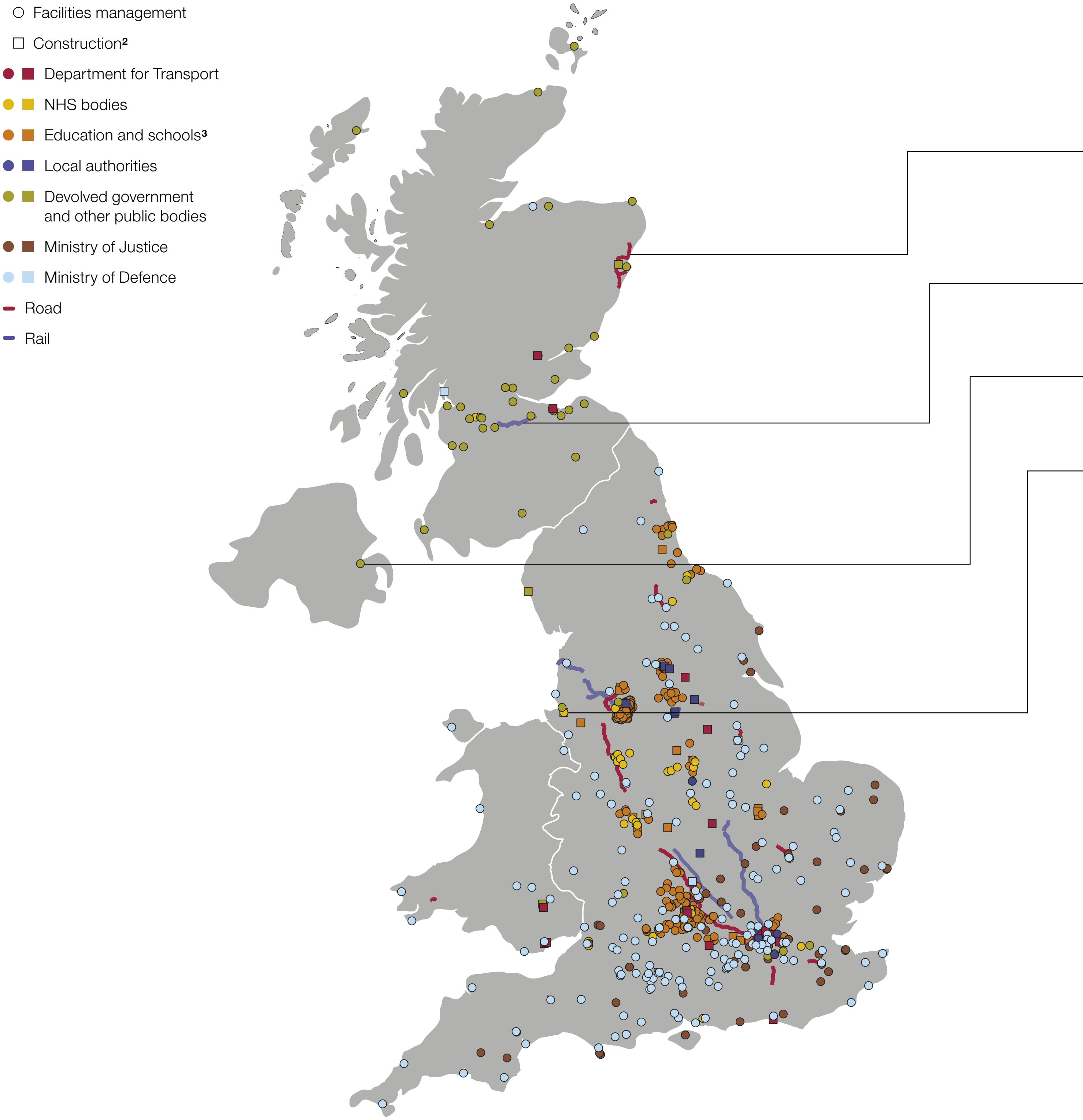
1.6 Carillion targeted a net profit margin of 4.5% to 5.5% on its central government facilities management work. Advisers working for Carillion's creditors found that its 'central government' business unit, which covered Carillion's service and facilities management contracts, was a profitable business, although it had become less profitable over time. Operating profit was forecast to reach £9 million in 2017, from £647 million forecast revenue for the division, or 1.4%. This was low mainly because of losses on a large Ministry of Justice contract (**Figure 6** on page 18). The advisers reported that Carillion was achieving operating profits of 13% to 15% on work for schools and hospitals.

1.7 Carillion's public sector construction contracts and private finance initiative (PFI) schemes were not covered by this business unit. Carillion faced significant losses on three of its public sector construction contracts and one service contract (Figure 6 on page 18).

Figure 1

Examples of Carillion's public sector activity at the time of its collapse

Carillion had a wide range of construction and services contracts on sites across much of the public sector[1]



Roads
Construction of a new 58km ring road, the Aberdeen Western Peripheral Route, for Transport Scotland, working with Balfour Beatty and Galliford Try

Rail
Electrification of the Glasgow to Edinburgh line, for Network Rail

Housing
Facilities management for 49,300 homes owned by the Northern Ireland Housing Executive

Hospitals
Construction and facilities management of a new hospital, the Royal Liverpool University Hospital, under a PFI contract

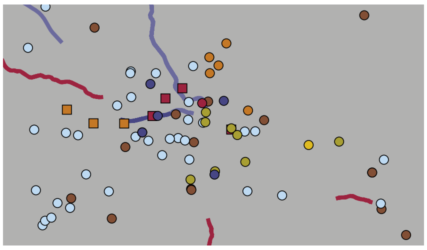
Local authorities
Maintenance of parks, allotments, cemeteries and open spaces in the London Borough of Hounslow

Schools
Facilities services for Oxfordshire County Council schools

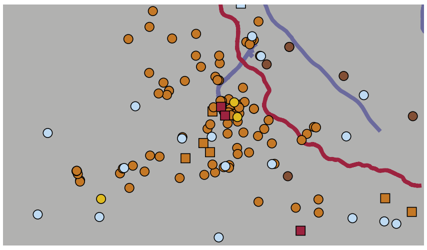
Prisons
Facilities management of 50 prisons across the south of England for HM Prison & Probation Service

Defence
Facilities management of around 320 sites for the Ministry of Defence, working in joint ventures with Amey and Aramark

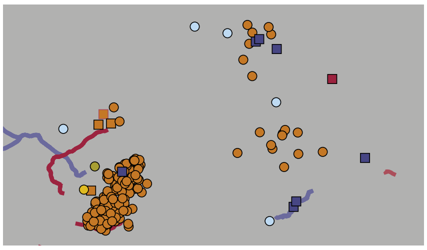
London



Oxfordshire



Manchester, Leeds, Bradford



Notes

1 Map does not show a complete picture of Carillion's contracts due to data limitations. Dates vary. Not all sites are shown.

2 On some construction projects Carillion was also contracted to run the facilities management of the newly-built sites.

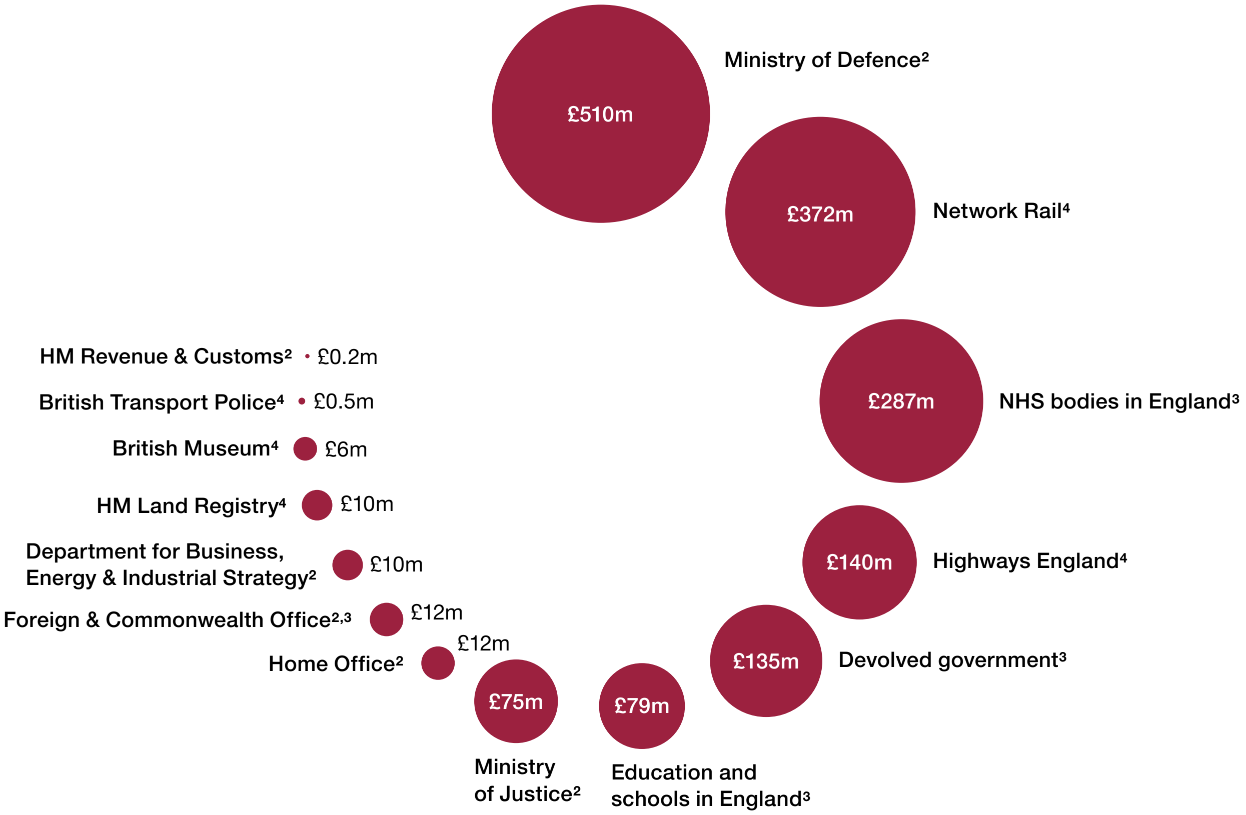
3 Schools are shown, not contracts with schools. Carillion had contracts with 97 Oxfordshire County Council schools, 62 Tameside Council schools, 63 Stockport Council schools, and schools in 23 other council areas. Some schools are local authority schools, others are academies.

Source: National Audit Office analysis of data from the Cabinet Office, the Education and Skills Funding Agency, the Ministry of Justice, HS2 Ltd, Network Rail, Highways England, the Office for National Statistics, and the Ministry of Defence

Figure 2

Estimated UK public sector spending with Carillion in 2016-17

Carillion reported £1,719 million of UK public sector revenue in 2016[1]



Notes

1 Some of the figures for individual bodies should be taken as indicative rather than actual values, as explained in the notes below. The total of the bubbles shown, £1,685 million, differs from £1,719 million shown in Carillion's 2016 annual report. This is due to differing time periods (see note 3), incomplete Cabinet Office data from arm's-length bodies, differing revenue recognition policies in Carillion's accounts, and the fact that we have no combined figures for local government spending.

2 Source is the Cabinet Office's spending portal data. We combined figures for Carillion plc with figures for Carillion joint ventures which are recorded separately in the portal. For CarillionAmey, Aspire Defence Ltd, Carillion Kier JV, Balfour Beatty Carillion JV, and Costain Carillion JV we added 50% of reported revenue to the Carillion total, representing what we assume to be Carillion's share of the JV revenues based on ownership shares disclosed in Carillion's annual accounts.

3 Source is revenue data Carillion provided to the Cabinet Office in July 2017, covering the first 6 months of 2017. We have doubled the figures to represent a whole year.

4 Source is the named public body, for 2016-17.

Source: National Audit Office analysis of data from multiple sources

Figure 3
Carillion's UK public sector contracts

Information compiled from a number of sources indicates that Carillion had around 420 contracts with public bodies at the point of insolvency in January 2018[1]

Organisation	Number of contracts identified
Schools in England	312
NHS bodies in England	25
Network Rail	22
Local authorities in England	14
Highways England	11
Ministry of Defence	10
Department for Education[2]	6
Fire and rescue authorities	6
Devolved government	5
Ministry of Justice	3
HS2 Ltd	2
British Museum	1
British Transport Police	1
Department for Business, Energy and Industrial Strategy	1
Foreign & Commonwealth Office	1
HM Land Registry	1
HM Revenue & Customs	1
Home Office	1
Total	**423**

Notes

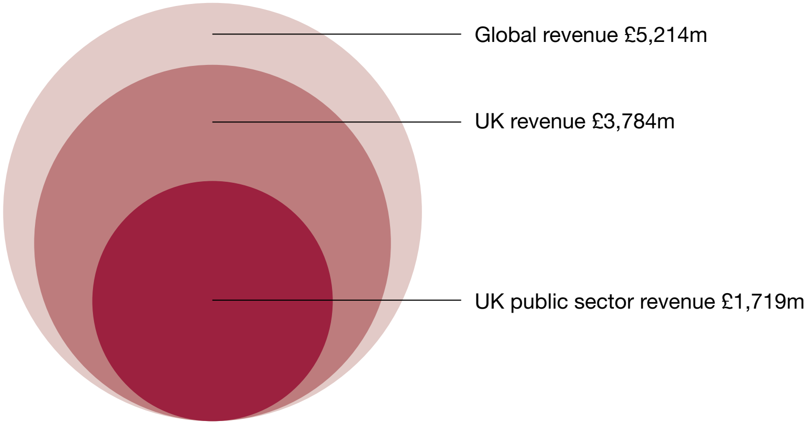
1 Data varies in quality and completeness. We have included contracts with no information on dates.

2 Department for Education contracts include two Priority Schools Building Programme contracts. There may be an overlap between these contracts and the 312 schools contracts.

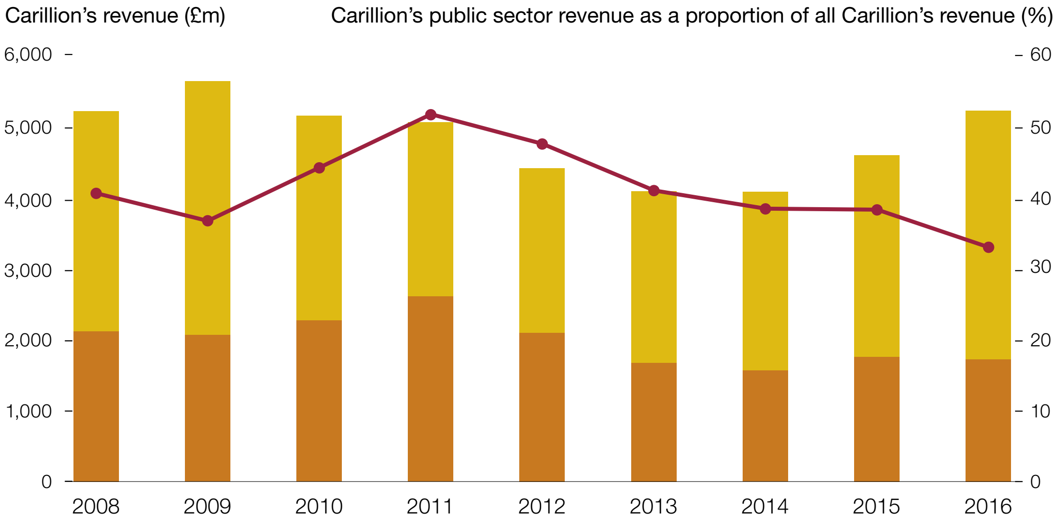
Source: National Audit Office analysis of data from the Cabinet Office, Education and Skills Funding Agency, Department for Transport documents, and Department for Education

Figure 4
Carillion's revenue

Carillion's UK public sector revenue represented 45% of its UK revenue



Carillion's UK public sector business declined over the last four years as a share of its total revenue



	2008	2009	2010	2011	2012	2013	2014	2015	2016
● UK public sector revenue as a proportion of all revenue (%)	40.6	36.7	44.1	51.6	47.5	40.9	38.4	38.2	33.0
🟨 Other revenue	3,095	3,565	2,871	2,443	2,313	2,411	2,509	2,833	3,495
🟧 UK public sector	2,111	2,065	2,268	2,608	2,090	1,670	1,563	1,754	1,719

Notes

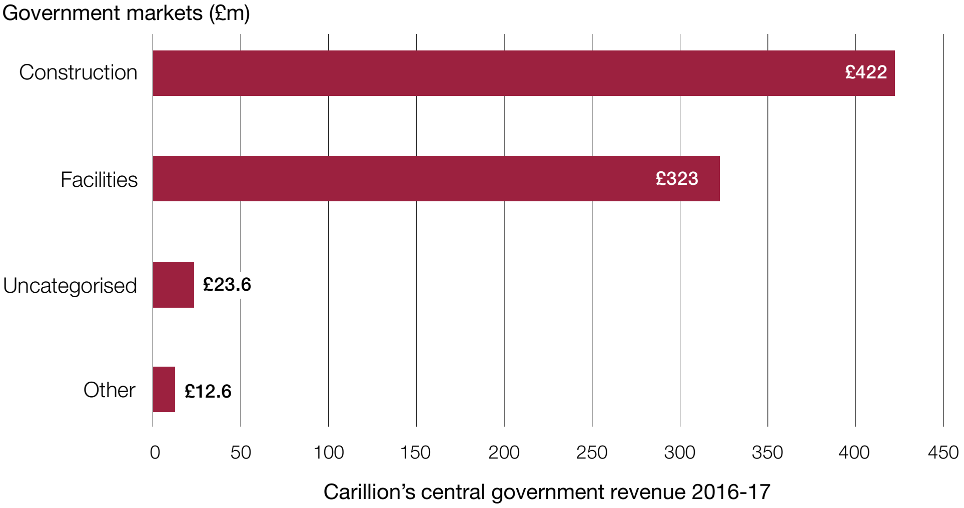
1 Public sector revenue is described as revenue from 'UK government' in Carillion's accounts.

2 Carillion's published accounts cover calendar years.

Source: National Audit Office analysis of Carillion's published accounts

Figure 5
Carillion's key markets and share of central government business

Carillion's business with central government departments was mostly construction and facilities management



Note

1 Data are from the Cabinet Office spending portal for 2016-17, representing £781 million of Carillion revenue.

Source: National Audit Office analysis of Cabinet Office data

Figure 6

Analysis of Carillion's main loss-making public sector contracts

Carillion faced large losses on four public sector contracts

Contract	Expected loss for 2017, as identified by Carillion and its auditors (£m)[1,2]	Comments (taken from the work of advisers to Carillion's major lenders)[3]
Aberdeen Western Peripheral Route	91	A joint venture contract to design, build, finance and operate a new 58km ring road and associated infrastructure. Lenders' advisers identified that the primary causes of the losses on the project included: ● project selection – the bid price was very low and there were not enough resources for the project; ● ground conditions – issues with water and peat that were not foreseen and needed more time to rectify; and ● oil pipelines – oil companies had to approve any changes to construction and areas of significant protection.
Midland Metropolitan Hospital	48	A PFI contract involved building a hospital and providing facilities management services for a 30-year term. Lenders' advisers identified the reasons for delays and increased costs included: ● critical design elements of the project were 17 months late; ● structural designs were poor; and ● spatial constraints made it difficult to fit all the plant machinery necessary.
Royal Liverpool University Hospital	83	A PFI contract to build a new hospital, demolish an old hospital and build a car park. In addition to the construction contract, Carillion also won a 30-year facilities management contract from April 2015. The advisers identified that the reasons for delays and increased costs included: ● a 14-week delay when asbestos was identified; ● material delays to the design of the new hospital; ● structural deficiencies that required repair, due to poor design; and ● a lack of due diligence undertaken before the construction work started.
HM Prison & Probation Service	12	A contract originally with the Ministry of Justice to provide facilities management services in 52 public sector prisons in England and Wales. The lenders identified that the reasons for costs included: ● it being a 'first generation' outsourcing contract; and ● inaccurate tender assumptions.

Notes

1 Construction contract losses are inclusive of expected claims recoveries but not full claims lodged.

2 Government does not necessarily agree with the size of the losses, which may have implications for future claims.

3 Former Carillion directors told us that reasons for losses are multiple and complex and the above only reflects a number of these issues.

Source: National Audit Office analysis of FTI Consulting report and information provided by Carillion's former directors

Part Two

Cabinet Office monitoring of Carillion as a strategic supplier

2.1 This part of the report covers:

- the Cabinet Office's policy for managing strategic suppliers and how it applied that policy to Carillion from 2012 onwards;
- Carillion's reported financial position before July 2017 and its underlying financial health; and
- Carillion's declining financial performance in the second half of 2017 and the government response.

The strategic supplier risk management policy

How the Cabinet Office monitored performance and financial health

2.2 The Cabinet Office introduced a new approach to strategic supplier management in 2011, and started monitoring the performance and financial health of strategic suppliers, including Carillion, following publication of its risk management policy in 2012.[4] The policy applied to bodies classified as central government by the Office for National Statistics. Its aim is to ensure suppliers fulfil their contractual obligations to central government and that public services are maintained. Strategic suppliers, of which there are now 27, are shadowed by 16 crown representatives (normally part-time senior officials with a commercial background), who are supported by partnership managers (senior civil servants). The management of each contract is done by the individual procuring departments.

2.3 These crown representatives, and specific officials from the Cabinet Office with the Director for Markets and Suppliers as chair, form the Commercial Relations Board. Once every six weeks, it meets to discuss the performance of each strategic supplier, and assigns each one a risk rating (**Figure 7** overleaf).

---

[4] Cabinet Office, *Strategic Supplier Risk Management Policy*, November 2012, available at: www.gov.uk.

Figure 7

The government's strategic supplier risk management policy

Under the policy, as a large supplier with contracts across many government departments, Carillion was subject to monitoring and risk rating

Process	Rating	Consequences
The Commercial Relations Board meets every six weeks to discuss the performance of 27 suppliers and decide on risk ratings	🟢 No known issues or isolated issues handled through business as usual	Status reviewed at each Commercial Relations Board meeting
	🟡 Material concerns with the supplier across one or more contracts	Status reviewed at each Commercial Relations Board meeting
	🔴 Significant material concerns for the Commercial Relations Board to consider 'high risk' designation	The Commercial Relations Board instructs Cabinet Office officials to assess whether there are grounds to rate the supplier as 'high risk'
The Board can recommend a 'high risk' rating to the minister for the Cabinet Office	● 'High risk'	Providing extra performance information; regular and frequent meetings between the crown representative and a senior staff member; monitoring at contract level; reduction where possible in the extent to which the supplier is given extra work under the terms of an existing contract; and withdrawal of privileges like meetings with ministers.

Source: National Audit Office analysis of Cabinet Office documents

2.4 There was no crown representative for Carillion for the period July to October 2017. Recruitment of a replacement was delayed as the Cabinet Office changed the requirement following Carillion's first profit warning to a person with experience in corporate restructuring. In the meantime, the role was taken on by the Director for Markets and Suppliers, who is responsible for the relationship with all strategic suppliers. There was a partnership manager for Carillion throughout 2017.

Cabinet Office monitoring of Carillion before July 2017

2.5 Carillion's risk ratings between 2013 and January 2018 are shown in Figure 14. Carillion's risk rating changed several times before 2017, because of:

a **poor performance on some contracts**

Carillion's risk rating was green between August 2013 and January 2016. In February 2016 it increased to amber, following poor performance on a Ministry of Defence facilities management contract. This risk rating was then maintained in response to other performance concerns, notably on the contract to provide facilities management in prisons for HM Prison and Probation Service.

b **delayed payments to suppliers**

The Commercial Relations Board increased Carillion's rating in 2013 due to concerns about late payments to sub-contractors, but returned to a green rating in August 2013 as "Carillion have now signed up to the Prompt Payment Code and have helped to promote Supply Chain Partnerships with Number 10".[5] Carillion told the Cabinet Office in April 2015 that it was paying sub-contractors on government contracts within 30 days. Concerns about late payments to sub-contractors continued, and in June 2017 the Cabinet Office asked Carillion to review its payments to subcontractors. Carillion reported that, on average, it was paying its suppliers 45 days after the invoice date in the first five months of 2017. This was 33 days from receipt of validated invoice. Almost one third of invoices were paid more than 60 days later.[6] The Cabinet Office told us it was unable to verify this information. Many sub-contractors were paid through Carillion's 'early payment facility'.[7]

Short selling of Carillion shares

2.6 Since Carillion's collapse some commentators have pointed to short selling of Carillion shares as evidence of early concerns.[8] Short selling of Carillion's shares increased between 2012 and 2018 (**Figure 8** overleaf). The Cabinet Office was aware of this short selling and told us it had raised it with Carillion in the past. Carillion explained to the Cabinet Office in May 2017 that the short selling was due to general pessimism about trading conditions in the sector, an assumption that Carillion's average net debt was too high, and "adverse trends in [its] working capital and its main components".

---

[5] The Prompt Payment Code sets standards for payment practices and best practice for suppliers. It states that 60 days should normally be considered the maximum period.

[6] Under the Public Contracts Regulations 2015 public sector buyers must pay prime contractors within 30 days and must ensure that their prime contractor includes equivalent 30-day payment terms in any sub-contracts through the supply chain.

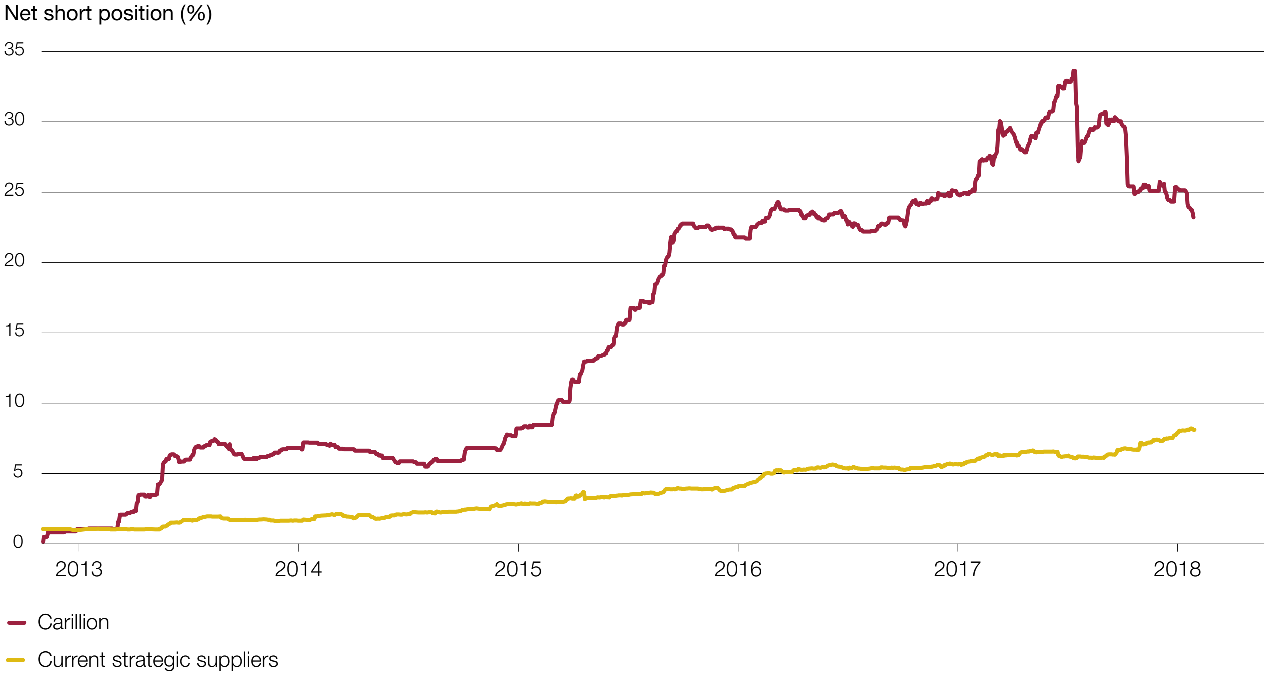
[7] An early payment facility allows a sub-contractor to be paid for a certified invoice earlier than they would otherwise be paid. The bank pays the sub-contractor, deducting a charge from the amount due. Carillion later pays the bank.

[8] Short selling is the sale of shares that the seller does not own or has borrowed, in the belief that the value will fall, so that the shares can be bought back at a lower price in the future for a profit.

Figure 8

Short selling of Carillion shares, 2012 to 2018

Short selling increased from 2012 to a peak in 2017



Note

1 Not all of government's strategic suppliers' shares have been shorted, and many are not listed in the UK, so would not appear in Financial Conduct Authority data.

Source: National Audit Office analysis of Financial Conduct Authority data, October 2012 to January 2018

Carillion's worsening financial health in 2017

Carillion's reported financial performance

2.7 The Cabinet Office monitored Carillion's financial health as part of its strategic supplier management. Carillion's public reporting showed it as a going concern and profitable, although debt and pension liabilities were increasing (**Figure 9**). In the second half of 2017 it became increasingly clear that Carillion was in serious financial difficulty. Carillion issued a profit warning on 10 July 2017, followed by another with its half-year results on 29 September 2017. On 17 November it announced that by the end of the year it expected to breach the terms on which it was lent money. Cumulative provisions made by Carillion for future losses totalled £1.1 billion by the end of 2017 (see Figure 13).

Figure 9
Carillion's reported financial performance

Until Carillion's 2017 half-year results, its published accounts showed it to be solvent and profitable

	2015 (£m)[1]	2016 (£m)[1]	2017 (half-year) (£m)[1]
Revenue	4,587	5,214	2,247
Profit (loss) before tax	155	147	(1,153)
Cash generated from operations	73	73	(290)
Net borrowing at year end or half-year end	170	219	571
Average net borrowing during the year or half-year[2]	539	587	694
Pension deficit[3]	394	805	711
Net assets (liabilities)	1,017	730	(405)

Notes

1 Numbers shown in brackets are negative numbers.

2 Carillion defined net borrowing as cash minus overdrafts, bank loans, finance leases and other loans.

3 As at 30 June 2017 the company had 13 defined benefit pension schemes with liabilities totalling £2.6 billion.

Source: National Audit Office analysis of published Carillion documents

2.8 As a result, Carillion's market value fell substantially during the second half of 2017 (**Figure 10** overleaf) and there was increasing speculation about Carillion's future. In parallel to arranging a new £140 million lending facility, Carillion gave permission for its major banking lenders to form a Coordinating Committee to represent the interests of Carillion's creditors in a restructuring of the company. The Coordinating Committee appointed advisers including FTI Consulting.

Figure 10
Performance of Carillion shares, 2014 to 2018

Shares in Carillion fell in value over time, especially after its first profit warning on 10 July

Source: National Audit Office analysis of Bloomberg data

2.9 Carillion's reported financial results may have understated the problems Carillion faced. The Coordinating Committee commissioned consultants FTI to carry out an independent business review in October 2017. It remained in draft form and was not seen by the Cabinet Office or lenders before Carillion's insolvency. The FTI review reported practices that it described as having "enhanced reported financial performance above underlying operating performance". Former Carillion directors told us that, with the exception of the last point, they believed these were in accordance with accounting standards or had been appropriately disclosed in the accounts. The practices were:

- including profits from equity sales in public-private partnership and PFI projects in Carillion's operating profit and cash flow;
- consolidating the results of some joint ventures wholly into Carillion's cash flow and operating profits;
- short-term management of working capital to reduce net debt at the year end;
- taking out short-term loans with joint ventures to reduce net debt at the year end;
- using early payment facilities to improve supplier payment terms; and
- securing large advance payments on new contracts at the expense of future profitability. This issue was identified by Carillion's management and reported to the board in June 2017, who intended to take steps to remedy the issue.

2.10 In addition, the Work and Pensions Select Committee has published Carillion Board papers showing that in May 2017 the Carillion board received the results of an accounting review of some construction projects.[9] This identified that some accounting practices had understated the costs of some contracts. Following the review Carillion decided that there was also an associated understatement of revenue so it did not need to restate its 2016 accounts. The company's auditors KPMG agreed.

Cabinet Office increased monitoring of Carillon's financial health

2.11 The size of the profit warning of 10 July 2017 came as a surprise to the Cabinet Office as it contradicted: the information and commentary Carillion had given it up to that point; publicly available financial information; and the expectations of the market. It spoke to Carillion on 11 July to discuss the profit warning. It started to enhance government contingency plans for the possible failure of Carillion on 20 July, and told us it notified Carillion that it was doing so. It appointed law firm Dentons on 24 August. It also appointed PwC on 17 September to advise on contingency planning and dealing with the consequences of insolvency (at a final cost of £600,000).

2.12 Over the next few months, the Cabinet Office increased its contact with Carillion. By December it spoke to the company nearly every day (**Figure 12** on page 27). Eight Cabinet Office and UK Government Investments officials agreed to be Carillion 'insiders'. This meant Carillion gave them access to the same information as its major lenders, including access to cashflow statements. It is a criminal offence to disclose insider information to the market (**Figure 11** overleaf). A timeline of these events is shown in **Figure 13** on page 28.

---

[9] We have not seen this review.

Figure 11

Insider status given to civil servants by Carillion

Eight Cabinet Office and UK Government Investments officials agreed to be Carillion 'insiders'

The Criminal Justice Act 1993 created the criminal offence of insider dealing.

The Act prohibits the trading of a company's stock or other securities by individuals with access to non-public information, which would enable them (or those to whom they disclose information) to gain an unfair advantage over those without access to the information.

Under the Act, an 'insider' is a named individual who knowingly holds information that is inside information, obtained from an inside source.

Inside information includes information of which disclosure would be likely to significantly effect the public limited company's share price or other price-sensitive securities.

Insiders may be guilty of the criminal offence of 'insider dealing' if they buy or sell relevant shares, encourage others to, or disclosure the information.

The penalties are unlimited fines and/or imprisonment for up to 7 years.

Under EU law, companies must control access to and disclosure of inside information. They must draw up a list of people with access to inside information.

Companies must try to ensure that these people acknowledge in writing their legal and regulatory duties, and are aware of the sanctions for insider dealing and unlawful disclosure of insider information.

Source: National Audit Office

The risk ratings given to Carillion following the profit warning

2.13 The Commercial Relations Board discussed Carillion when it met on 18 July, eight days after the first profit warning. It discussed raising Carillion's risk rating from amber to red on the grounds of financial distress. This change was confirmed by the Board in September after seeking legal advice (**Figure 14** on page 29).

2.14 On 29 November, following Carillion's announcement that it expected to breach its debt covenants, the Cabinet Office told Carillion that it proposed to increase its rating from red to 'high risk'. Carillion objected on the grounds that:

- the level of engagement between the Cabinet Office and Carillion was already higher than that required by a 'high risk' rating;
- employees were concerned, having heard that government bodies were contingency planning;
- if government customers reacted by denying further business opportunities (particularly if this was to become public), this would make Carillion's financial position even worse, with consequences for its government customers; and
- discussions with lenders were ongoing and were constructive.

2.15 At its 15 December meeting the Board accepted Carillion's representations and decided not to increase Carillion's rating to 'high risk'. It accepted that the rating would unnerve Carillion's lenders at an important point in the restructuring process and could precipitate financial collapse. It reserved the right to increase the rating in future. By its next meeting on 9 January, it was already evident that Carillion would fail unless the government provided it with financial support.

Figure 12

Formal meetings and phone calls between the Cabinet Office and Carillion, January 2017 to January 2018

The Cabinet Office had around 50 formally-arranged phone calls and in-person meetings with Carillion after the July 2017 profit warning, as well as numerous ad-hoc contacts including phone calls and text messages

Date	1	2	3	4	5	6	7	8	9	10	11	12	13	14	15	16	17	18	19	20	21	22	23	24	25	26	27	28	29	30	31
2017																															
January																■			■												
February																											■				
March			■																				■								
April						■																					■				
May			■								■											■									
June		■																													
July											■		■							■											
August																■								■					■		
September						■												■										■			
October										■								2													
November	2									■			■										■	■			■		2	■	
December						■	■	■	■			■	■		■			■	■	3								■			
2018																															
January			■	■	■			■	■	■		■	■	■																	

■ Record of meeting or phone call

Note

1 Based on analysis of diaries. The Cabinet Office also communicated by email with Carillion frequently. The table does not include ad-hoc communications.

Source: National Audit Office analysis of Cabinet Office documents and interviews with Cabinet Office officials

Figure 13

Timeline of events affecting Carillion, July to December 2017

July 2017

10 July: First profit warning. Carillion announced provision for losses of £845 million on three public sector private finance initiative (PFI) construction contracts in the UK (Midland Metropolitan Hospital, Liverpool Royal University Hospital, and the Aberdeen Western Peripheral Route), and construction contracts in the Middle East. These PFI contracts accounted for 27% of the provision. Carillion's chief executive resigned.

14 July: Carillion appointed consultants to help its restructuring, focusing on cost reduction and cash collection.

August 2017

20 July: Government contingency planning began. The process continued through 2017.

11 September: Senior management including finance director were asked to resign. A Chief Transformation Officer was seconded in from EY. A new Chief Financial Officer took over with immediate effect.

September 2017

14 September: Eight officials from the Cabinet Office and UK Government Investments became Carillion 'insiders', giving them access to internal financial information such as cash flow forecasts. This information could not be shared with other departments.

29 September: Advance warning of the second profit warning prompted the Cabinet Office to express forcefully to Carillion its view that Carillion had not been open about the seriousness of its position in the past.

29 September: Second profit warning. Carillion's half-year results showed it made a £1.15 billion loss in the first six months of 2017. This included a further £200 million in provisions. Carillion announced it had agreed £140 million of additional lending facilities with its banks.

October 2017

23 October: Carillion's major lending banks (the Coordinating Committee) commissioned consultants to carry out an independent business review of Carillion's business plan for its restructuring, as and when it became available.

17 November: Carillion announced that it expected to breach the terms of its banking covenants (the terms on which it is loaned money by its lenders) at the end of 2017. Around this time Carillion identified another £60 million of provisions, bringing the total to £1.1 billion.

November 2017

29 November: The Cabinet Office wrote to Carillion to say that its Commercial Relations Board had provisionally raised Carillion's rating from red to 'high risk'. Carillion replied that the Cabinet Office was already in receipt of the financial information required by this rating, and the rating would damage its attempts to improve its finances.

15 December: The Cabinet Office decided not to rate Carillion as 'high risk', as it already had officials acting as 'insiders' receiving detailed financial information, and it did not wish to risk precipitating Carillion's financial collapse.

December 2017

22 December: Carillion's lenders agreed to delay the date to test whether it was meeting its banking covenants to April 2018.

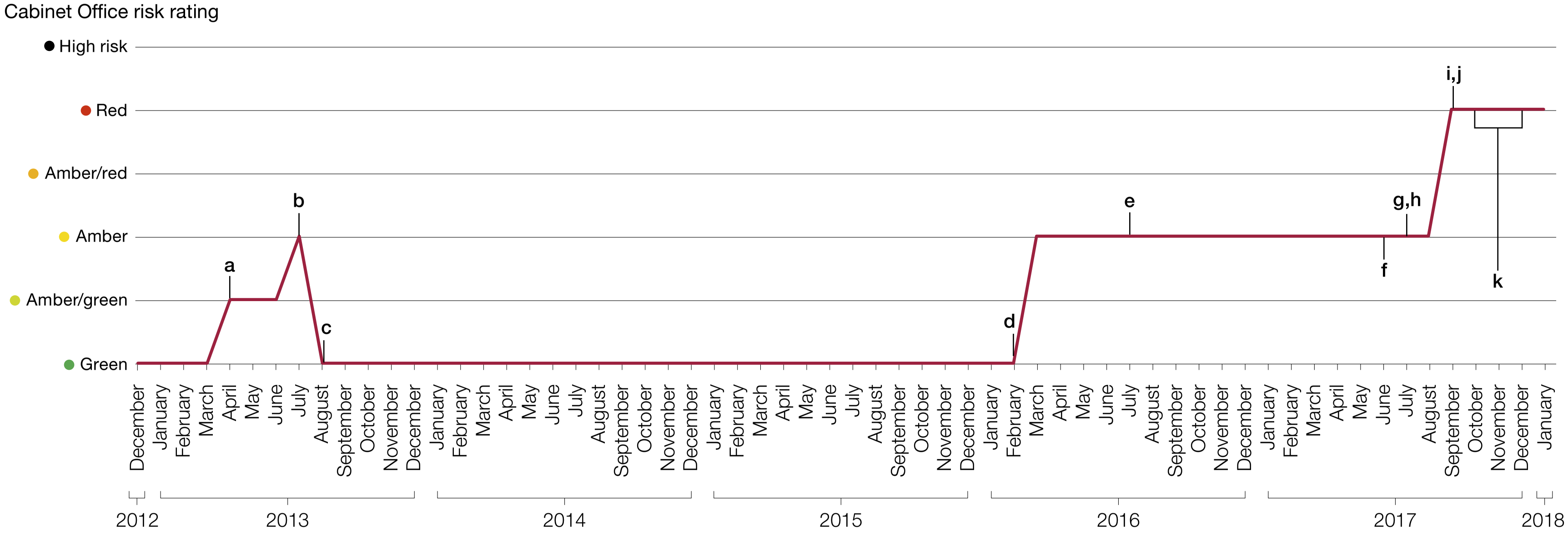
31 December: First formal request to government by Carillion asking for financial support, deferment of taxes, help in restructuring its pensions liabilities and immunity from penalties arising from regulatory investigations.

Source: National Audit Office analysis of Cabinet Office and Carillion documents

Figure 14

Risk ratings allocated to Carillion by the Cabinet Office over time

Carillion's rating rose from green to amber in February 2016, and amber to red in September 2017



a	April 2013	Rating increased in response to concerns about delayed payments to sub-contractors.
b	July 2013	The Cabinet Office discussed increased concerns about delayed payments to sub-contractors.
c	August 2013	Carillion signed Prompt Payment Code and promoted Number 10 supply chain initiative.
d	February 2016	Rating increased in response to poor performance on a Ministry of Defence facilities management contract.
e	July 2016	The Cabinet Office discussed poor performance on HM Prison and Probation Service contract.
f	June 2017	The Cabinet Office discussed delayed payments on NHS contracts.
g	10 July 2017	Carillion's first profit warning.
h	18 July 2017	The Cabinet Office discussed increasing Carillion's risk rating to red subject to seeking legal advice.
i	5 September 2017	Confirmation of rating increase, in response to July 2017 profit warning.
j	29 September 2017	Carillion's second profit warning.
k	October and December 2017	The Cabinet Office decided not to increase rating to high risk.

Note

1 The increase to amber in July 2013 was due to a change in guidelines for ratings.

Source: National Audit Office analysis of Cabinet Office documents

Part Three

The government's contingency planning for Carillion's possible failure

3.1 This part of the report describes actions taken by the Cabinet Office and Carillion's customers across government to protect services and construction projects as the company's financial health deteriorated, and the awarding of further government contracts to Carillion.

Contingency planning

3.2 On 20 July 2017 the Cabinet Office called together Carillion's customers in central government departments and some arm's-length bodies and asked them to provide information on their contracts, including whether they had contingency plans.

3.3 At that stage the Cabinet Office did not have a complete list of public sector contracts beyond central government. The government's main database of contract information, Bravo, does not contain information on important Carillion customers such as local authorities, Network Rail, schools and hospitals. The Cabinet Office asked Carillion for information on these broader public sector contracts. It had a working list by the end of August.

3.4 Following Carillion's second profit warning, on 29 September 2017, the Cabinet Office asked for contingency plans for key central government contracts. It set 17 November as the deadline for submitting contingency plans, covering legal, operational and financial options on a contract-by-contract basis. It provided a template for costing information for bodies' preferred contingency options in the event of Carillion's liquidation. The Cabinet Office carried out its contingency planning coordination activity confidentially so as to avoid making public anything that might influence decision-making by Carillion's lenders and the market.

3.5 The Cabinet Office asked for contingency plans to be ready by the end of November. Many organisations did not achieve this, and the Minister for the Cabinet Office sent a letter to them requiring completed plans by 20 December. Ultimately, the Cabinet Office received 65 contingency plans from 26 public bodies (**Figure 15**).

Figure 15

Total estimated costs of public bodies' contingency plans in the event of Carillion's liquidation

Twenty-six public bodies provided contingency plans to the Cabinet Office

Customer	Total estimated costs of preferred option in contingency plan (£000)
Network Rail[1]	146,650
Ministry of Justice	52,550
Ministry of Defence	27,750
Oxfordshire County Council	3,405
Department for Education	3,000
London Boroughs of Harrow and Ealing	2,617
London Borough of Hounslow	1,468
Leeds City Council	401
Stockport Strategic Partnership	345
HM Revenue & Customs	0
HS2 Ltd	0
Total	**238,186**

Uncosted plans provided

British Museum

Cambridge University Hospitals NHS Foundation Trust[2]

Dartford and Gravesham NHS Trust

Foreign & Commonwealth Office

Great Western Hospital, Swindon[2]

Greater Manchester Police

Highways England

HM Land Registry

James Cook University Hospital, South Tees[2]

John Radcliffe Hospital, Oxford[2]

Metropolitan Police Service

North Staffordshire Combined Healthcare NHS Trust

Queen Alexandra Hospital, Portsmouth[2]

Royal Liverpool University Hospital[2]

Southmead Hospital, Bristol[2]

Notes

1 Network Rail's plans represented a 'worst case scenario' rather than a preferred option.

2 The Cabinet Office received two contingency plans from hospitals: one from the PFI entity and one from the NHS Trust or NHS Foundation Trust.

Source: National Audit Office analysis of contingency plans sent to the Cabinet Office

Carillion's contingency planning

3.6 The Cabinet Office had more difficulty in persuading Carillion to do its own contingency planning. It told us it asked Carillion from October onwards to do contingency planning to protect the delivery of services. Carillion provided data to government to support government's contingency planning, but told us it was focusing on developing successful restructuring plans, which it considered to be the best way to protect its creditors' interests. It also engaged EY to undertake financial contingency planning (paragraph 4.13). It then appointed PwC to do operational contingency planning on 4 January. Carillion explained to the Cabinet Office on 13 January that it had been unable to do meaningful contingency planning for its failure because of the complexity of the company and a lack of funds.

The costs and quality of government contingency plans

3.7 The contingency plans varied in length and detail. The hospital plans, for instance, were detailed and gave day-by-day instructions on what would need to be done in the event of Carillion's failure, such as enacting service continuity plans and enabling staff to move to new working arrangements.

3.8 Ten public bodies' contingency plans included cost estimates for their preferred option. These totalled £238 million. The additional costs of enacting preferred options included:

- termination payments to Carillion;
- inefficient working owing to transferring responsibilities to new providers;
- increased staff costs, including management time;
- re-procurement;
- higher prices of alternative providers;
- making construction sites safe;
- purchasing new software; and
- legal advice.

3.9 Network Rail provided the highest cost estimates for enacting its preferred options at £147 million. Network Rail told us that this was a worst-case scenario, and it currently expects additional costs to be only a small proportion of this amount. Some of the customers that procured services through the PFI route did not cost their plans because they assumed that costs would fall to the PFI special purpose vehicle (the private investors) as this was Carillion's customer, not the public body.

New government contracts and variations announced after the first profit warning

3.10 Carillion announced that it had won four central government contracts and three variations after the 10 July profit warning, totalling around £1.9 billion, including £1.3 billion of HS2 contracts (**Figure 16** overleaf).

3.11 Under the strategic supplier risk management policy, departments are asked to reduce where possible the extent to which a strategic supplier rated as 'high risk' is given additional work under the terms of an existing contract (Figure 7). This only applies to discretionary work such as extensions or call-offs under existing contracts, as procurement rules do not allow a supplier to be excluded from bidding for new contracts on the basis of its risk rating. The Cabinet Office does not believe that there was a basis for refusing to award any of the contracts.

- The two Ministry of Defence contracts had been signed and agreed before the 10 July profit warning, but not announced publicly. There were joint venture partners required to step in if Carillion failed.
- The procurement for the HS2 contracts had been completed before 10 July, but the contracts were signed and agreed shortly afterwards. On 12 July, two days after Carillion's first profit warning, HS2 commissioned consultants to re-run the financial tests carried out during the bidding process. Carillion continued to pass the tests based on the latest published accounts (the 2016 accounts published in March 2017, before the profit warning). The contracts were awarded to a joint venture requiring the other parties to step in if Carillion failed, which HS2 told us was part of their strategy to manage risk in the supply chain.
- Network Rail confirmed the next phase of two contracts for the electrification of lines in November 2017. Both electrification programmes had just completed the design phase and were ready for construction to begin. Not awarding the contracts would have meant re-procuring the project, re-doing the design phase, increasing costs and delaying the work. Financial due diligence on Carillion had been carried out in 2014-15, when the contract started. In two of the three variations, Carillion had a joint venture partner obliged under its contracts to take over Carillion's role in the event of Carillion's failure. In the other case, the contract has been re-let, in line with its contingency plans.

3.12 Carillion also won work with local government after its first profit warning. On 3 October Leeds City Council awarded Carillion £4.1 million to construct a cycle superhighway. This was conditional on provision of a performance bond from a third-party financial institution to protect the Council in the event of Carillion's insolvency.[10]

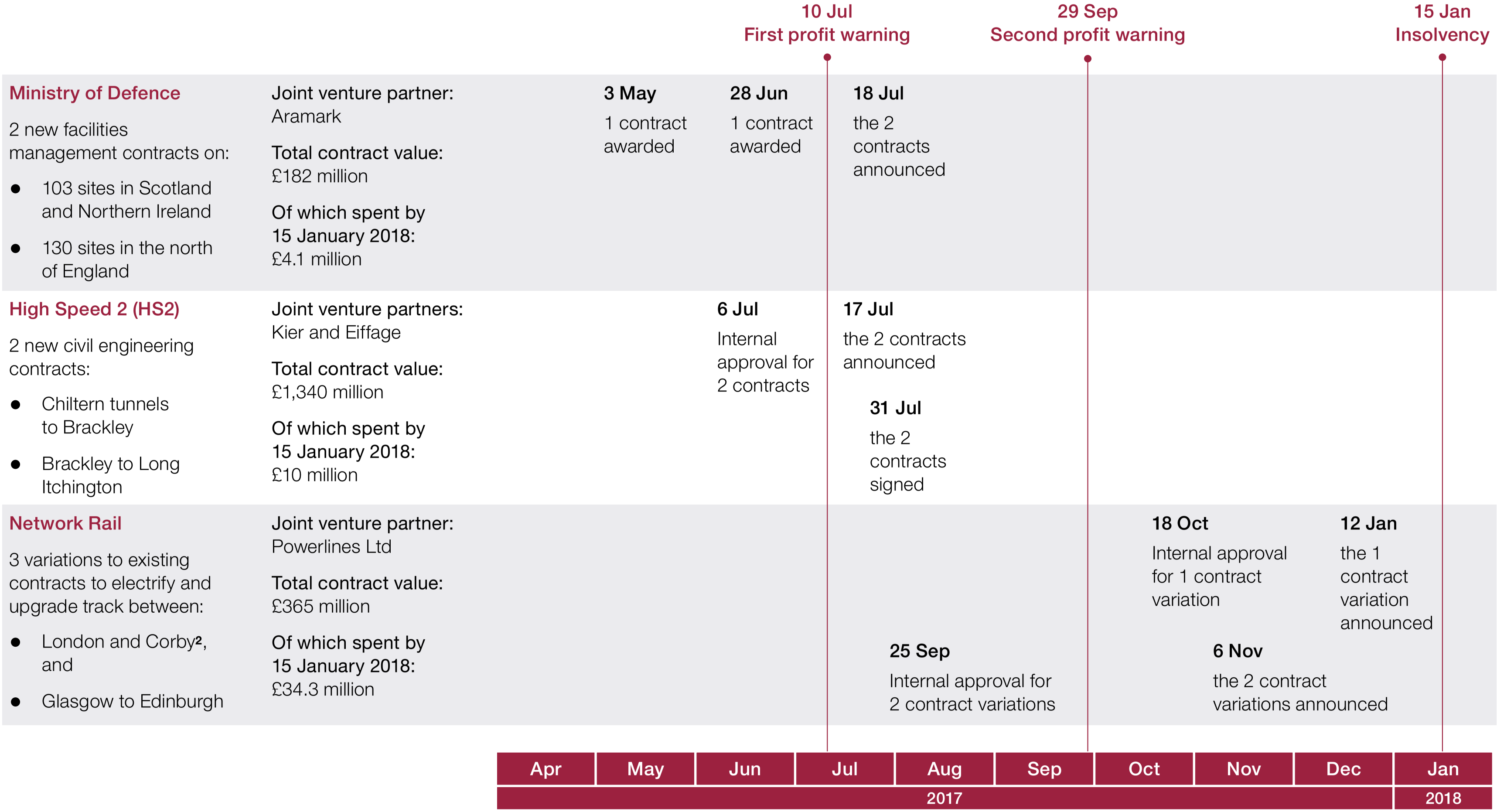
---

[10] A performance bond is a form of security provided by a third party, usually a bank or insurance company, guaranteeing the obligations of the contractor under the contract. The bond constitutes a promise that the guarantor will make a payment to the contracting authority of a set amount.

Figure 16

Work won by Carillion which was announced by the company after its first profit warning

After the July profit warning, five new contracts were announced, and variations to three existing contracts were agreed[1]



Ministry of Defence

2 new facilities management contracts on:

- 103 sites in Scotland and Northern Ireland
- 130 sites in the north of England

Joint venture partner:
Aramark

Total contract value:
£182 million

Of which spent by 15 January 2018:
£4.1 million

3 May 1 contract awarded

28 Jun 1 contract awarded

18 Jul the 2 contracts announced

High Speed 2 (HS2)

2 new civil engineering contracts:

- Chiltern tunnels to Brackley
- Brackley to Long Itchington

Joint venture partners:
Kier and Eiffage

Total contract value:
£1,340 million

Of which spent by 15 January 2018:
£10 million

6 Jul Internal approval for 2 contracts

17 Jul the 2 contracts announced

31 Jul the 2 contracts signed

Network Rail

3 variations to existing contracts to electrify and upgrade track between:

- London and Corby[2], and
- Glasgow to Edinburgh

Joint venture partner:
Powerlines Ltd

Total contract value:
£365 million

Of which spent by 15 January 2018:
£34.3 million

25 Sep Internal approval for 2 contract variations

18 Oct Internal approval for 1 contract variation

6 Nov the 2 contract variations announced

12 Jan the 1 contract variation announced

Notes

1 Also on 3 October Leeds City Council awarded Carillion £4.1 million to construct a cycle superhighway.

2 Two contracts covered the London to Corby track work and Carillion had no joint venture partner on one of the two London to Corby contracts.

Source: National Audit Office analysis of Cabinet Office documents

Part Four

The government's response to Carillion's request for support

4.1 This part of the report describes requests made by Carillion to the UK government for short- and long-term in-kind and financial support between 31 December 2017 and 14 January 2018, which Carillion considered essential to its restructuring plans, and why the government decided to decline the request on 14 January.

Carillion's requests for support

4.2 Between October and December 2017 Carillion's financial situation continued to worsen. Former Carillion directors told us there were a number of reasons for this. These included a hardening of attitudes among: lenders, causing withdrawal of existing lending facilities; customers and purchasers of Carillion's assets, who started to negotiate harder from an increasing position of strength; and suppliers, who wanted shorter payment terms. In December 2017, Carillion's main creditors told it that they would not give further short-term funding unless Carillion also approached government for financial support.

4.3 On 31 December, Carillion wrote to the Cabinet Office with an urgent request for government support. Carillion made further versions of this request on 8, 12, 13 and 14 January (**Figure 17** on pages 36 and 37). The Chief Executive apologised for the "hard edge" to the proposals, which he partly attributed to direction from Carillion's major creditors.

4.4 Carillion told the Cabinet Office on 31 December that its plans for restructuring were not finalised, but that it would need to complete its restructuring by the end of April. It said restructuring would probably need to entail "virtually all" of its £1.5 billion of debts converting to equity, the significant dilution of existing shareholders' stake in the company, the comprehensive restructures of the company's pensions obligations, and a range of other support from its existing creditors.

Figure 17

Carillion's requests for government support

Between 31 December 2017 and 14 January 2018 Carillion developed proposals for short- and long-term support from the UK government

Details of request		Amount, 31 December	Amount, 8 January	Amount, 12 to 14 January
Urgent requests intended to avert liquidation				
Deferment by HM Revenue & Customs of tax payments due in the first half of 2018, to be repaid during 2018.		£91 million	Unchanged at £91 million	Reduced to £63 million
A loan, either to be provided directly by the government or guaranteed by it, to be repaid either at the end of April 2018 or upon completion of the company's restructuring.[1]		Not quantified	£210 million	£160 million (following banks' agreement to increase their contribution)
Potentially net of	Settlement of the HM Prison and Probation Service contract, including settlement of claims and liabilities (which, if paid, would have been netted off the loan amount).	Not detailed	Not quantified	Claims and work in progress, £20 million
	Notice of, and then a detailed list of, other requests for payment of claims or accelerated and advance payments (which, if paid, would have been netted off the loan amount).	Not quantified	Not quantified	£19 million[2]
Requests intended to secure long-term investment				
Help to persuade the Pension Protection Fund (PPF), Pension Trustees and the Pensions Regulator to accept the company's restructuring of its 13 principal defined benefit pension schemes in order to extinguish Carillion's £2.6 billion liabilities.[3]		Financial impact for PPF	Financial impact for PPF	Financial impact for PPF
The government to help fund the completion of the Midland Metropolitan Hospital, in exchange for an equity stake.		Not quantified	Up to £125 million	Unchanged at up to £125 million
Transfer of Carillion's equity stake in the joint venture building the Aberdeen Western Peripheral Route to the government at 'full value', and advance payment of a portion of sums claimed against Transport Scotland.		Not mentioned	Not quantified	Not quantified
Help in negotiating an exit from loss-making contracts in the UK and the Middle East.		No financial impact	No financial impact	No financial impact
Other support				
Protection from the imposition of fines or penalties by regulators for actions taken by the company before July 2017.		Not quantifiable	Withdrawn	Withdrawn
An extension to the Ministry of Defence's existing Next Generation Estate Contracts with settlement of existing claims and liabilities.[4]		Not mentioned	Not quantifiable	Not quantifiable
Longer-term financial support if necessary to supplement support from commercial lenders.		Not quantified	Withdrawn	Withdrawn
A commitment from the government to giving Carillion its 'fair share' of work, and prevent government customers and others exercising their rights to terminate contracts.[5]		Not quantifiable	Not quantifiable	Not quantifiable

Figure 17 *continued*

Carillion's requests for government support

Notes

1 This would be unsecured and without guarantees, which Carillion acknowledged was against the government's stated position.

2 Settlement of claims, £8 million; overdue payments, £6.8 million; and payments on account, £4.6 million.

3 Carillion indicated that the most likely solution would be a Regulated Apportionment Arrangement, a restructuring arrangement which allows an employer to detach itself from its defined benefit pensions scheme liabilities when the alternative would be insolvency. The liability is usually passed to the Pension Protection Fund.

4 Work still needed to be done, but normally there would be no assumption work would go to Carillion.

5 On 5 January the Cabinet Office told Carillion there could be no special treatment over future contract awards.

Source: National Audit Office analysis of Cabinet Office documents

4.5 Carillion asked the government for help with both the restructuring of the company, and for a total of £223 million of support for a "bridging" period from January through to April. The £223 million was made up of a request to the Cabinet Office for £160 million and the deferral of £63 million of Carillion's tax liabilities by HM Revenue and Customs. It was also contingent on the banks agreeing to £60 million of further unsecured loans. By 13 January Carillion clarified that it wanted the £160 million to be provided in five stages:

- £10 million of immediate government support (either a loan or a guarantee) for the week beginning 15 January, to match £10 million of unsecured lending by the banks;
- £10 million of government support (either a loan or a guarantee) for the week beginning 22 January, to match a further £10 million of unsecured lending by the banks;
- A guarantee on Carillion's early payment facility, to be capped at £60 million–£70 million and to expire at the end of January and to be replaced with a guarantee as set out below (see paragraph 2.5);
- A £110 million government guarantee to the banks so Carillion could draw down funding at the end of January and continue to operate its early payment facility without the government guarantee; and
- A further £30 million government guarantee for bank lending to be drawn down between February and April, to be matched by £40 million of unsecured lending from the banks.

4.6 The amount needed would reduce if certain disputed claims and invoices for work in progress were settled, which Carillion totalled at £39 million. The Carillion directors were also working on a plan to reduce the level of requirement through asset sales, better working capital management and exiting their business in the Middle East.

4.7 Carillion also asked for additional support with its financial restructuring. It asked the Cabinet Office for support in its negotiations with different stakeholders that would be involved in this restructuring, including helping to persuade the Pension Protection Fund, Pensions Trustees, and the Pensions Regulator to accept the £2.6 billion of pensions liabilities. It also asked for the Cabinet Office to provide up to £125 million to help fund the completion of the Midland Metropolitan Hospital PFI scheme in exchange for an equity stake (see Figure 17). The Cabinet Office told Carillion it could not legally grant some of the company's requests. Others were not quantified but could have had significant additional costs for the taxpayer.

4.8 Carillion told the Cabinet Office that it would fail without support and cause widespread problems for the public sector. It said it had received advice from its insolvency practitioners that the government had no contingency plan that was "fit for purpose" and that any insolvency process would be "very disorderly and value destructive" with "no ability to manage the widespread loss of employment, operational continuity, impact upon customers and suppliers and even the physical safety of workers and the public".

4.9 Following Carillion's initial request for urgent short-term support, the Cabinet Office organised meetings with Carillion and its creditors, and made more detailed preparations for Carillion's insolvency (**Figure 18**). From the middle of December the Cabinet Office produced a weekly dashboard assessing the progress of contingency planning across government. By the time that Carillion entered liquidation, the Cabinet Office was broadly satisfied with central government's readiness, but was still seeking improvements to planning in schools and local authorities.

Figure 18

Timeline of events leading to liquidation, December 2017 to January 2018

December 2017

31 December: First formal request to government by Carillion for financial support, deferment of taxes, help in restructuring its pension liabilities and immunity from penalties arising from regulatory investigations.

January 2018

3 January: a Financial Conduct Authority investigation was announced into the "timeliness and content" of some of Carillion's stock market announcements between 7 December 2016 and 10 July 2017.

5 January: Government representatives and their advisers met Carillion's major lenders, pensions representatives and Carillion. Carillion needed restructuring plans in place by 19 January and had hired insolvency practitioners to help it plan. It thought about £275–£350 million was required. The lenders' advisers said it could well be more, and pensions liabilities could be between £600 million and £1.5 billion. We were told that lenders were concerned by Carillion's slow progress in business and contingency planning, and by the rate at which it was using cash.

8 January: Carillion shared with the Cabinet Office and other creditors a draft business plan setting out its plans for restructuring the company for longer-term sustainability.

Carillion made a more detailed request for support to the Cabinet Office.

10 January: Carillion presented its business plan to its creditors. It reported losing £655 million of cash from operations in 2017. Its future strategy was to: do "fewer things better"; exit non-core businesses, including public-private partnerships; reduce annual operating costs by £100 million; and dispose of non-core assets.

11 January: The chief executive of the civil service, the Chancellor of the Exchequer and the Minister for the Cabinet Office approved the option of a trading liquidation.

12 January: Government met lenders and pensions representatives. Potential private investors stated that any additional finance would be long-term (post-restructuring), without links to loss-making contracts, and with the understanding that they would take priority in any pay-outs to creditors. Major banking lenders would not proceed without government guarantees and pensions liabilities resolved.

The Cabinet Office promised Carillion a decision by 15 January.

Carillion reported to the Cabinet Office that HM Revenue & Customs (HMRC) was not minded to support its request for deferment of tax (see Figure 17) because:

- the proposal did not fit with HMRC's 'Time To Pay' model because of the level of debt accruing;
- it suspected Carillion had other sources of liquidity; and
- it lacked confidence in the viability of the company following the restructuring.

The Prime Minister gave approval for the option of a trading liquidation.

12–14 January: Carillion and the Cabinet Office had further discussions about the nature of government support requested.

13 January: The Cabinet Office submitted the results of its options analysis for Carillion's support or insolvency to the Minister for the Cabinet Office.

14 January: The Cabinet Office informed Carillion it would not provide support.

15 January: Carillion's directors applied to the High Court for liquidation.

Source: National Audit Office analysis of Cabinet Office and Carillion documents

The Cabinet Office's appraisal of the options for the support or insolvency of Carillion

Pessimism about Carillion's plans

4.10 Carillion had prepared a business restructuring plan intended to demonstrate how its management would turn around the fortunes of the company over the next five years. It had originally agreed to present this to lenders on 17 January, but brought this forward to 10 January. The plan was presented first to the major lenders and their advisors FTI, then to the Cabinet Office.

4.11 Lenders had commissioned FTI to produce an independent business review of the plan, (see paragraph 2.9), but this was not shown to lenders or the Cabinet Office. This review remained in draft form as it was still subject to agreement with Carillion's management. Former Carillion directors told us that they did not see a draft of the report's main body until 13 January, at which point they objected to its analysis of their capacity to win future business and the profit margins achievable, which they believed was too pessimistic and overstated Carillion's capital needs. They did not see the executive summary. The executive summary of the review was published by the Business, Energy and Industrial Strategy and Work and Pensions Committee joint inquiry into Carillion.[11] In this draft the lenders' advisers took the view that:

- there were significant doubts about Carillion's true past trading position and cash generation, because of Carillion's focus on enhancing the reported level of profitability and net debt;
- management had in the past concentrated too much on short-term profitability at the expense of long-term viability;
- addressing these issues had meant that Carillion had used up liquidity, and most of £140 million of emergency funding, and now needed more;
- further lending would be highly risky while the extensive pension liabilities remained;
- Carillion's business plan was too optimistic about uncertain items such as disputed claims against customers or other contractors, and the willingness of private sector customers to give Carillion building work in the short term; and
- the sensitivity analysis the advisers applied to Carillion's finances would increase additional funding requirements to £495 million by August 2019.[12]

---

[11] Available at: www.parliament.uk/documents/commons-committees/work-and-pensions/Carillion/Project-Ray-FTI-consulting-15-January-2018.pdf

[12] Former Carillion directors told us that this estimate was reducing in ongoing discussions about the draft review.

Government review of the options

4.12 The Cabinet Office, with the help of PwC, undertook an options analysis at the beginning of January to decide whether to support Carillion. Over the course of a week, working with the Cabinet Office and HM Treasury, PwC produced high-level estimates of the costs of each option on a 'rough order of magnitude' basis (**Figure 19** on pages 42 and 43). The Cabinet Office considered the two cheapest options to be too risky. A pre-sale of assets was not possible in the time available, as it was likely to take months to find a buyer of the individual assets on a break-up basis. The option of providing short-term investment was rejected as the Cabinet Office lacked confidence in Carillion's business case.

4.13 The Cabinet Office also received, on 28 December, an analysis Carillion had commissioned from consultants EY in November 2017. It analysed possible asset values that creditors could receive if Carillion became insolvent. The consultants looked at two scenarios: liquidation; and the carving out of parts of the company for sale, with liquidation for the rest. It described the work as "a hypothetical exercise" and "inherently uncertain". It concluded that in theory a break-up of the company could yield some £364 million (equivalent to less than seven pence in the pound for creditors). However, EY concluded that this was likely to be unachievable as a range of factors would turn the process into a "distressed sale", which would push the company towards a "liquidation scenario".

4.14 The Cabinet Office's options analysis concluded that a trading liquidation was the preferred option on the basis that it met the government's objectives, which were to:

- maintain as many public services as possible;
- minimise disruption;
- maintain job security;
- minimise cost; and
- avoid setting an unhelpful precedent.

4.15 In the week of 8 to 12 January, the Cabinet Office set up a crisis management centre to handle communications, briefed and received permission from the Chancellor of the Exchequer and the Prime Minister, and prepared to inform Parliament of the financial consequences. The Cabinet Office secured the approval in principle of the Chancellor, Minister for the Cabinet Office and Prime Minister for the preferred option on 11 and 12 January.

Figure 19

Options for insolvency or support of Carillion

The government costed four options and decided to select a trading liquidation

Option	Description	Estimated cost	Scores		
			Continuity of public services	Losses for (deferred) pensioners	Contagion (other prime contractors)
Trading liquidation[1]	Insolvency proceedings with the Insolvency Service funded to continue public services	£314m to £374m[2]	✗✓	✗✗	✗
Unsupported insolvency	Insolvency proceedings with no extra funding for the Insolvency Service	£658m to £678m[2]	✗✗✗	✗✗	✗✗
Potential (pre) sale of assets	Buyers are identified for some or all of Carillion's UK business. Residual elements move to the Insolvency Service	-£49m to £51m[2]	✓✓	✗✗	✓
Bridging investment	Government provides a £110 million loan with a potential further £50 million alongside £60 million from lenders. HM Revenue & Customs also defers payments of £30 million until December 2018. Not including potential costs of future insolvency.	£233m to £267m[3]	✓	✗	✓

✓ Positive

✗ Negative

Notes

1 Described as a 'supported insolvency'.

2 Minimum to maximum.

3 Proposed and maximum exposure.

Source: National Audit Office analysis of Cabinet Office documents

Scores						
Contagion (sub-contractors)	Control of outcome	Ease of execution	Avoids setting precedent of government bail-out	Government seen as proactive	Government seen as responsible with taxpayers' money	Government saving workforce jobs, not executives
✗✗	✗	✓	✓	✓	✓	✓✓
✗✗✗	✗✗✗	✓✓	✓	✗	✗✗	✓✓
✗✓	?	?	✗	✓✓	✓✓	✓✓
✓	✗✗	✓	✗✗✗	✓✓✓	✗✗	✗✗✗

4.16 This left it to officials to decide what to do over the course of the weekend of 13 and 14 January. Early on 14 January the government's Chief Commercial Officer set out to the chief executive of the civil service the rationale for not providing support to Carillion as:

- providing the funding would set a precedent for others seeking government support;
- buying the equity in PFI schemes would put them on the UK government balance sheet;
- the changing nature of the requests for funding (see Figure 17);
- the poor quality of the business restructuring plan and lack of confidence in company forecasts;
- the lack of enthusiasm from other lenders and the placing of unrealistic conditions on the lending of new money;
- the government would be carrying excessive risk in the short term, and this could lead to an open-ended funding commitment even if the company survived, as it would have given the company and lenders no incentive to repay the government;
- the risk of funding being used to support non-government projects;
- the lack of enthusiasm from the Pension Protection Fund and HM Revenue & Customs for the aspects of the request requiring their approval; and
- assistance could be construed as State Aid under EU rules.

4.17 Subsequently, the Cabinet Office explained to us that it believed the conclusions above would lead to Carillion returning with further requests for funding. It also told us that, as government was not being offered preferential treatment over other creditors (known as seniority) or guarantees against Carillion's assets (known as fixed or floating charges), other lenders could have pressured it into providing further iterations of support by threatening to withdraw. It saw this as a particular risk on the early payment facility where demand would increase should suppliers lose faith in the business.

4.18 On 14 January, Cabinet Office officials took the decision to refuse support and informed Carillion. When the lenders were informed of this, they wrote to Carillion later that day to say that they too would not offer further support. Carillion placed itself in compulsory liquidation on 15 January.

Part Five

Carillion in liquidation

5.1 This part of the report sets out the actions taken by government following Carillion's liquidation on 15 January 2018, and the impact of Carillion's collapse.

Establishing a trading liquidation

5.2 Carillion told the High Court that in the absence of funding, it had been unable to identify any insolvency practitioners willing to act as administrators. The only remaining option was a liquidation, in the hands of an official appointed by the court. The High Court appointed an employee of the Insolvency Service as the Official Receiver to manage the liquidation as a trading liquidation, and employees of PwC to act as 'special managers' to support the Official Receiver.

5.3 Almost all public and 90% of private sector customers agreed to Carillion continuing to provide services to them during the liquidation. Services therefore continued to be delivered to schools, hospitals, military bases and so on, which would otherwise have had to curtail operations or close completely. Around 255 public sector contracts were included within the insolvency regime.[13,14] A small number exited from their contracts immediately, and a number of others withdrew from the insolvency regime within a few days.

5.4 The Cabinet Office secured £150 million of funding from Parliament in February 2018 to provide liquidity to the Official Receiver and help to maintain public services. The Insolvency Service told us the trading liquidation would not have been possible without this funding. The Cabinet Office also indemnified the Official Receiver for any proceedings or claims against him in connection with the liquidation.

---

[13] When we talk about public sector contracts in this context we include special purpose vehicles (SPVs) delivering private finance initiative (PFI) schemes for public sector bodies, although the SPVs are private entities.

[14] This number differs from the number of contracts in paragraph 1.2. Possible reasons for this include: the grouping of some contracts for multiple bodies in some sectors; differing understandings about whether contracts mapped onto organisations on a one-to-one basis; the fact that some contracts shown as live in Carillion records were complete; and the fact that not all Carillion companies are in liquidation.

The current status of the liquidation

Immediate impact

5.5 The Cabinet Office's crisis management centre (paragraph 4.15) maintained contact with affected departments from the point that the liquidation was announced, to monitor the impact of liquidation on them directly or on the organisations for which they were responsible, such as schools and hospitals. It communicated the message that Carillion staff should turn up for work as usual. The Cabinet Office promised to pay the January payroll and to continue to pay staff so long as they provided services. It found almost no examples of disruption to services.

5.6 Construction projects either continued uninterrupted, in situations where a joint venture partner was obliged to take on Carillion's share of the contract, or stopped where sites were made safe while awaiting a new contractor. This includes two PFI hospitals where construction work was stopped while PFI investors found alternative construction companies – Midland Metropolitan Hospital and Royal Liverpool University Hospital. Organisations took a range of approaches to maintaining services. For example, the Ministry of Justice established a new government company to provide facilities management services in prisons.

Progress in dealing with contracts

5.7 The Official Receiver is part-way through liquidating Carillion, using PwC as special managers. Thirty-one of Carillion's 198 UK companies were in liquidation.[15] The Official Receiver told us these account for a large proportion of the total contracts. It forecasts that customers will have exited from, or transferred, all contracts by the end of June 2018. This includes PFI construction schemes where Carillion was also an equity investor. As at 23 May, 21 public sector contracts remained within the insolvency regime, while at the end of May the Official Receiver expects to provide support services for a specified period beyond the end of the contract for a further 30. These post-contract 'transitional service arrangements' are expected to cease by the end of August 2018. **Figure 20** shows the actual and planned timelines for contracts transferring to new arrangements.

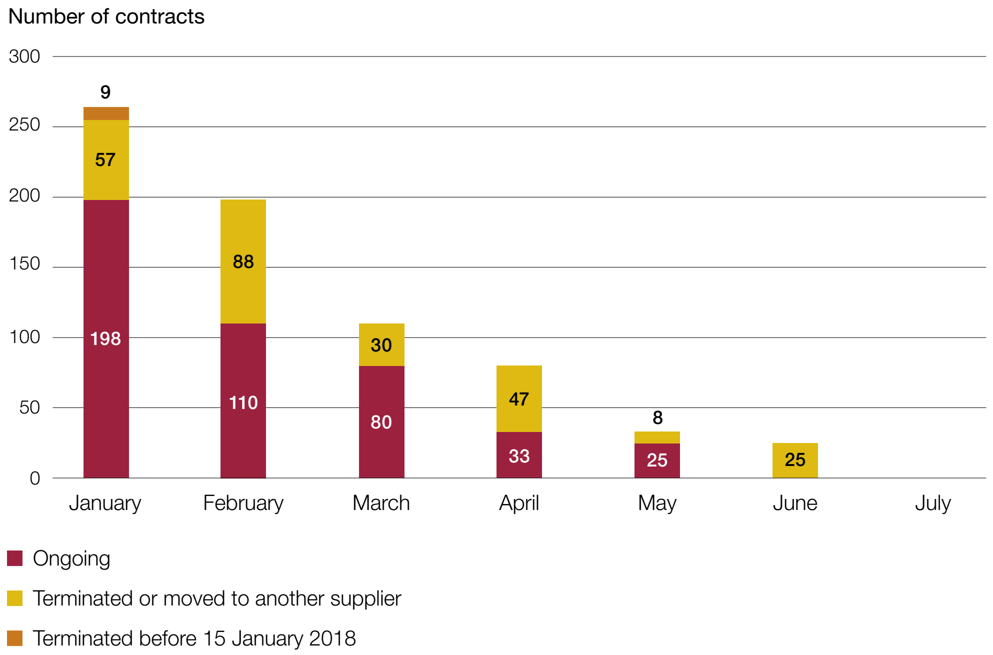
---

[15] As of 30 April 2018.

Figure 20

Timeline for Carillion services transferring to new arrangements, January to June 2018

By July 2018 the Official Receiver expects to have no Carillion contracts left to manage



Notes

1 During the process of transferring or terminating some contracts, Carillion has temporarily retained an interest in the entity supplying the services after disposing of the contract. Until this interest is disposed of, the contract continues to appear in the list of extant contracts, even if the service contract has terminated.

2 Forward pipeline estimated by the Official Receiver as at 24 May 2018.

Source: National Audit Office analysis of information from Official Receiver

The costs of the liquidation

Costs attributable to the liquidation

5.8 The Official Receiver expects the liquidation of Carillion to make an overall net loss. It is fairly usual for a liquidation to make a loss, as the costs of winding up a company can outweigh the recoverable assets, even where the company's debts and contracts are disclaimed. However, in this case the losses are greater because the Official Receiver expects to recover less from customers for continuing services after 15 January than it spends on Carillion's ongoing running costs. The Official Receiver believes that this has increased the likelihood of some creditors receiving money, and has not harmed the position of the rest, because: companies within the group incurring the greater losses above were likely to make a loss on the liquidation anyway; and continuing to run services has helped to preserve the value of those parts of the business it is seeking to sell. Some creditors will be paid because they are owed money by Carillion companies that have positive net assets (see paragraph 5.13).

5.9 The net loss on the liquidation will ultimately be borne by the taxpayer. The government originally estimated that a liquidation would cost £314 million to £374 million (see Figure 19). The Official Receiver currently expects total costs of the liquidation to be £522 million, including a £50 million payment for the special managers (see **Figure 21**). The net costs, which will borne by the Cabinet Office, will be around £148 million (see Figure 21). This estimate is subject to a range of uncertainties, for example the timing and extent of asset sales, and it will take a long time to establish the actual cost. The precise amount owed to Carillion is still not clear due to the complexity of Carillion's business interests. The Official Receiver told us that litigation might be necessary in some cases to recover amounts owed.

5.10 The total cost to the taxpayer will be slightly higher than this estimate as some public sector bodies have paid a 20% premium for provision of post-liquidation services (see paragraph 5.12). Some customers will also incur costs in replacing Carillion (see paragraph 3.8).

Additional costs not attributable to the liquidation

5.11 In addition, the special managers expect to incur around £9 million in other costs that would not be incurred during a conventional liquidation and which must be borne by the taxpayer and not the creditors. One of these costs involves the Construction Industry Training Board (CITB) finding other providers for Carillion apprentices' training. CITB is an arm's-length body of the Department for Education. Carillion had 1,148 apprentices when it collapsed. At the end of March, 729 (64%) had found or started work, or returned to education; 329 (29%) remained without work, but are being paid by the Official Receiver; and 90 (8%) could not be contacted. The Official Receiver expects to spend around £3 million in total on costs associated with apprentices.

Figure 21

Breakdown of actual and forecast costs of liquidation as of 18 May 2018

The Official Receiver's special managers currently forecast that the total cost of Carillion's insolvency will be £148 million

Cost element	Income/(costs) to 18 May (£m)	Forecast for remainder of insolvency (£m)	Total (£m)
Income	327	**90**	417
Of which: Revenue from services provided after 15 January			261
Costs	(249)	(273)	(522)
Consisting of:			
Payments to special managers	0	(50)	(50)
Legal costs	0	(20)	(20)
Statutory and consultants fees	0	(5)	(5)
Payments to subcontractors	(114)	(50)	(164)
Payroll for Carillion staff	(133)	(37)	(170)
Leases	(2)	(3)	(6)
Purchase card payments	0	(14)	(14)
VAT	0	(35)	(35)
Other	0	(58)	(58)
Expected distribution to creditors[2] and reimbursement of fees		**(44)**	**(44)**
Actual/Forecast net income/(costs)	**78**	**(227)**	**(148)**

Notes

1 Numbers may not sum exactly due to rounding.

2 Creditors of the Carillion group.

3 These are the amounts spent and forecast as of 18 May 2018. The precise amounts will not be known for some time to come.

Source: National Audit Office analysis of Insolvency Service documents

Collection of amounts owing from public sector customers

5.12 The Official Receiver's special managers charged Carillion's customers a premium of 20% on invoices for services provided since liquidation, to cover the costs of liquidation. Many of Carillion's public sector customers, including the special purpose vehicles delivering PFI projects, are objecting to paying this premium. The Cabinet Office is helping to facilitate a final agreement on some contracts. The special managers reported that in many cases, customers do not agree that the sums for which they are being invoiced are correct for the period before liquidation.

Wider costs to the economy

5.13 There will be additional costs of the collapse not covered within these estimates. It will be some time before the full costs are known. These costs include:

- **Impact on the supply chain**

  Carillion's sub-contractors will not be paid for some of the work they did before 15 January 2018. The government has not measured how many sub-contractors have experienced difficulties as a result. The Construction Products Association reported that 11,600 sub-contractors worked directly for Carillion. The government has coordinated lending facilities for small and medium-sized enterprises in the Carillion supply chain totalling up to £1 billion. The Department for Business, Energy & Industrial Strategy told us that there had been limited call on the lending facilities to date.

- **Impact on jobs**

  All Carillion staff in post on 15 January will eventually be found new jobs or made redundant.[16] By 29 May 2018 the Official Receiver had found continuing employment for 11,638 (64%) of the pre-liquidation Carillion UK workforce where contracts have been transferred. It has made 2,332 staff redundant without new jobs (13%), and continues to employ around 3,000 on remaining services. A further 1,116 staff have left voluntarily.

- **Impact on Carillion's creditors**

  The companies within the Carillion group had few assets when they entered into liquidation and most of the income from running the contracts and selling parts of the business will go towards the cost of the insolvency. There will be limited funds left after the liquidation to distribute to creditors. However, the Official Receiver is likely to distribute some money to creditors whose debts are with companies in the Carillion group with positive net assets. In practice, this means that a large proportion of any payment will go to settling tax liabilities, and the companies' pension schemes. When a company becomes insolvent and there are insufficient assets in the pension scheme to cover its liabilities, the Pension Protection Fund provides compensation to the scheme's members. Members of the scheme who have not yet retired will receive 90% of the value of the pension as compensation from the Fund.

---

[16] In a compulsory liquidation all staff are technically made redundant, but in most cases Carillion staff have moved on to new contracts.

Appendix One

Our investigative approach

Scope

1 We conducted an investigation into:

- Carillion's role in the market for government services;
- the Cabinet Office's monitoring of Carillion as a strategic supplier;
- the government's contingency planning for Carillion's possible failure;
- the government's response to Carillion's request for support; and
- Carillion in liquidation.

2 The investigation is non-evaluative. In particular, we have not assessed the total cost to society or the exchequer of Carillion's liquidation against other possible outcomes. The full costs will not be known for years. We have set out the Cabinet Office's analysis.

3 We have also not assessed the actions of Carillion, its directors, or its advisers. Investigations into the conduct of the company and its board members are being carried out by: the Financial Conduct Authority; the Official Receiver; the Pensions Regulator; and the Financial Reporting Council.

4 We shared copies of our draft findings with the Cabinet Office, Insolvency Service and former Carillion directors in post at the time of the company's insolvency: Finance Director Emma Mercer and Chief Executive Keith Cochrane.

Post publication this page was found to contain an error which has been corrected (Please find Published Correction Slip)

Methods

5 In examining these issues, we drew on several evidence sources:

- **We interviewed key individuals from the Cabinet Office and the Insolvency Service.** The people we interviewed included: the government Chief Commercial Officer, the Cabinet Office's Director of Markets and Suppliers, and the Insolvency Service's chief executive. We also interviewed PwC.
- **We interviewed former Carillion directors** in post at the time of the company's insolvency, Finance Director Emma Mercer and Chief Executive Keith Cochrane.
- **We also interviewed wider government and other stakeholders** to understand contingency planning, communications from the centre of government and actions taken since the insolvency. These interviews included the Ministry of Defence, the Department for Transport, the Department of Health & Social Care, the Department for Business, Energy & Industrial Strategy, the Ministry of Housing, Communities & Local Government, the Department for Education, NHS Improvement, the Local Government Association, Lloyds Bank and Oxfordshire County Council.
- **We reviewed documents**, including evidence published by the Select Committee inquiries, and unpublished Cabinet Office documents. One document, an independent business review of Carillion by FTI Consulting, was a draft, subject to management confirmation of its factual accuracy.
- We **analysed published and unpublished data**. This included data we extracted from Carillion's annual reports and announcements, data provided by Carillion to the Cabinet Office, data from Bloomberg, data on suppliers to central government from the Cabinet Office's Bravo system, and data and information produced by the Official Receiver's special managers as part of their management of the liquidation. We did not audit any of these data. The accuracy of Carillion's accounting practices has been criticised by the advisers to Carillion's creditors and is subject to investigation by the Financial Reporting Council.

6 At points we have combined data from different sources in order to give the best understanding of the scope and scale of Carillion's work. This has involved combining data from different accounting periods or prepared on different bases, which we have assumed are broadly comparable. We set out our assumptions in notes to Figures. In particular, we have had to construct an estimate of the number of UK public sector Carillion contracts at the time of the liquidation from several different sources. This number differs substantially from the number of contracts which entered the insolvency regime, as reported by the Official Receiver. None of the parties were able to reconcile the differences. Some possible reasons for the differences are set out in the footnote to paragraph 5.3.

7 We did not have access to Carillion's internal papers, except where they were published by the Work and Pensions and Business, Energy and Industrial Strategy Select Committees, or held by the Cabinet Office.

Report by the Comptroller and Auditor General

Investigation into the government's handling of the collapse of Carillion

HC 1002   Session 2017–2019

ISBN 9781786041968

Ordered by the House of Commons to be printed on 5 June 2018

CORRECTION

Paragraph 6, in the Summary, page 7 and Paragraph 4, in Appendix One, page 51, of the report were produced in error.

Paragraph 6, on page 7 currently reads:

6 **Carillion announced £1.9 billion of new government work after the 10 July profit warning.** Two joint venture defence contracts had been signed before the profit warning. HS2 Ltd approved two contracts worth £1.3 billion before 10 July but signed them afterwards. Network Rail confirmed the next phase of one contract worth £63 million after the second profit warning in September. In total eight contracts and variations were announced. None of the contracting authorities believed they had grounds for disqualifying the bids under procurement rules and in all but one case joint venture partners were obliged to finish the contracts if Carillion failed (paragraphs 3.10 and 3.11 and Figure 16).

It should read:

6 **Carillion announced £1.9 billion of new government work after the 10 July profit warning.** Two joint venture defence contracts had been signed before the profit warning. HS2 Ltd approved two joint venture contracts worth £1.3 billion before 10 July but signed them afterwards. Network Rail confirmed the next phase of one contract worth £63 million after the second profit warning in September. In total eight contracts and variations were announced. None of the contracting authorities believed they had grounds for disqualifying the bids under procurement rules and in all but one case joint venture partners were obliged to finish the contracts if Carillion failed (paragraphs 3.10 and 3.11 and Figure 16).

Paragraph 4, on page 51 currently reads:

4 We shared copies of our draft findings with the Cabinet Office, Insolvency Service and former Carillion directors for comment.

It should read:

4 We shared copies of our draft findings with the Cabinet Office, Insolvency Service and former Carillion directors in post at the time of the company's insolvency: Finance Director Emma Mercer and Chief Executive Keith Cochrane.

BACK TO PAGE 7

BACK TO PAGE 51

National Audit Office

£10.00

ISBN 978-1-78604-196-8

9 781786 041968

Design and Production by NAO External Relations
DP Ref: 006378-001