

Governance, Risk and Best Value Committee

10.00am, Tuesday 20 February 2018

Risks arising from Carillion PLC entering administration

Item number 7.4

Report number

Executive/routine

Wards

Council Commitments

Executive Summary

At its meeting on 16 January 2018, the Governance, Risk, and Best Value Committee (GRBV) requested a report on the implications of Carillion PLC entering administration for the Council and the City.

Risks arising from Carillion PLC entering administration

1. Recommendations

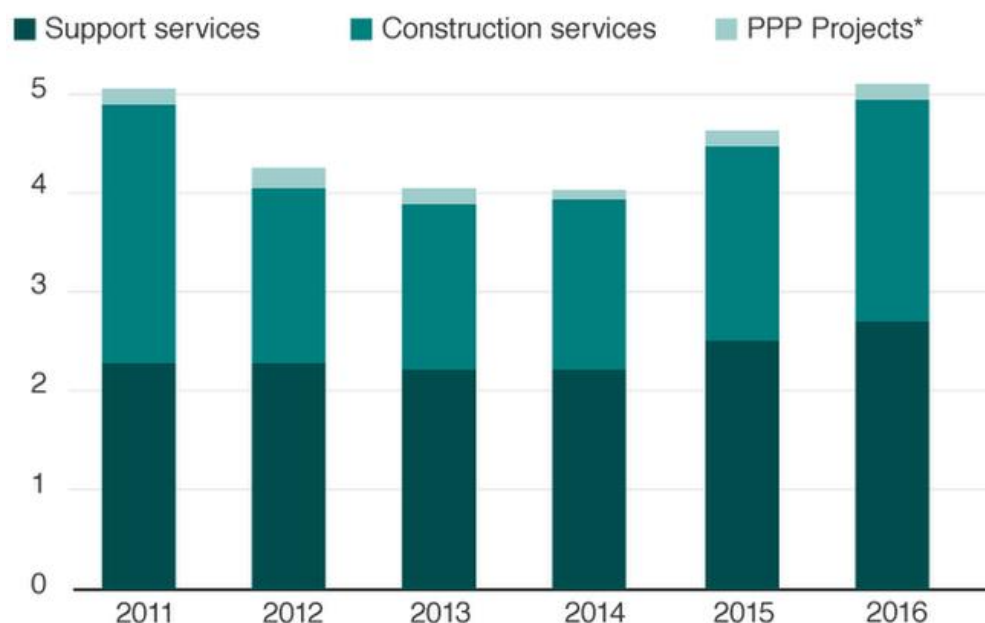
- 1.1 Members of the Governance, Risk and Best Value Committee are requested to:
- 1.1.1 note the content of the report and be assured by the Council's position in respect of the potential impacts arising from this; and
 - 1.1.2 note that the Council is also undertaking a review of other construction companies that may have issued profit warnings to assess any further potential risks.

2. Background

- 2.1 Carillion PLC employed around 43,000 people globally, with 20,000 based in the UK, with an estimated 1,000 in Scotland. Its overseas operations were primarily in Canada, the Middle East and the Caribbean and it was a major supplier of construction services to the Canadian government. Describing itself as an "integrated support services business", it held about 450 governmental contracts, spanning the UK education, justice, defence, and transport ministries. Carillion PLC managed the Smart Motorways traffic control system as well as maintaining about half of the UK's prisons and Young Offender Institutions. Its responsibilities additionally included cleaning, landscaping, and catering and it supplied school dinners and property and facilities management services to several English local authorities, e.g. Oxfordshire County Council, which has recently paid £10.65m to exit early from its arrangement with Carillion PLC.
- 2.2 Carillion PLC was also the second-biggest supplier of maintenance services to Network Rail and was responsible for delivering a range of major public-sector projects. They included the planned HS2 high speed railway line, the Royal Opera House, the Library of Birmingham, the Tate Modern, and the "doughnut" shaped building of Government Communications Headquarters (GCHQ). In 2016, Carillion had sales of £5.2bn and, until July, a market capitalisation of almost £1bn.

Carillion's revenue

Revenue by division (£bn)



Source: Carillion. *PPP: Public-private partnerships

BBC

- 2.3 However, Carillion PLC ran into trouble after losing money on major contracts and running up large debts. Some commentators suggest that the company overreached itself, taking on too many risky contracts that proved unprofitable. It also faced payment delays in the Middle East that hit its accounts.
- 2.4 Last year, it issued 3 profit warnings in 5 months and wrote off more than £1bn from the value of contracts. This action made it much harder for the company to manage its debts and pension deficit. Carillion PLC's share price dropped, following the first profit warning in January 2017, then dropped further as more warnings were made.
- 2.5 Ultimately, the company finally collapsed in January 2018, under the weight of £1.5bn in debts. Despite discussions between Carillion PLC, its lenders and the UK government, no deal could be reached to save the company.
- 2.6 Its biggest problems arose from cost overruns on three UK public sector construction projects:
- the £350m Midland Metropolitan Hospital in Sandwell: opening delayed to 2019 due to construction problems;
 - the £335m Royal Liverpool Hospital: completion date repeatedly pushed back amid reports of cracks in the building; and
 - the £745m Aberdeen bypass: delayed because of slow progress in completing initial earthworks.

- 2.7 Within Scotland, the company's list of existing clients includes: Registers of Scotland, the Scottish Children's Reporter Administration, West of Scotland Housing Association, and NHS Greater Glasgow and Clyde. Carillion also has two UK-wide facilities management contracts with the Ministry of Defence worth £158 million, which includes 83 military sites in Scotland.

3. Main report

- 3.1 Following the news about Carillion PLC entering liquidation, initial checks were instituted by the Council's Finance, Commercial and Procurement Services and Legal Services teams to assess any risk to the authority. These checks were completed by 17 January 2018.
- 3.2 The Council's checking and assurance processes confirmed that no direct contracts with Carillion PLC either current or planned were in place. In addition, checks against subsidiaries, joint ventures and sub-contractors were also undertaken and no records of contracts or other arrangements being in place with Carillion PLC were identified.
- 3.3 Carillion PLC was the contractor for the Niddrie Burn Restoration Project, which is now complete. The only payment made to Carillion by the Council related to this project during the last year.
- 3.4 Carillion PLC was also the Multi Utilities Diversion Framework Agreement (MUDFA) contractor for the original Edinburgh Tram project, with the contract having been awarded by Transport Initiatives Edinburgh (TIE).
- 3.5 The Council has some residual exposure on these projects in terms of not being able to enforce warranties and guarantees from Carillion PLC should the need arise. There is provision in the construction contracts for both the MUDFA and Niddrie Burn projects for Carillion PLC sub-contractors to provide collateral warranties to TIE and the Council respectively. Collateral warranties would allow TIE (now CEC Recovery Ltd) and the Council to directly enforce the warranties against the sub-contractors. Legal Services is reviewing the position in relation to such collateral warranties.
- 3.6 In terms of the broader potential impact upon the City, GRBV is advised that Carillion PLC was contracted to deliver the £23m extension to platforms in Edinburgh Waverley station in early 2017. Network Rail has indicated that they do not expect the station work, due for completion by the end of 2018, to be affected in the short-term and alternative arrangements to ensure delivery were being developed.
- 3.7 No other major contracts for Carillion PLC delivery have been identified in Edinburgh, at present.

4. Measures of success

- 4.1 The primary measure of success is that the Council has no significant exposure or liabilities arising from Carillion PLC entering liquidation.

5. Financial impact

5.1 There are no direct financial impacts arising from this report.

6. Risk, policy, compliance and governance impact

6.1 The Council has some residual exposure arising from two identified projects in terms of not being able to enforce warranties and guarantees from Carillion PLC should the need arise. There is provision in the construction contracts for both the MUDFA and Niddrie Burn projects for Carillion PLC sub-contractors to provide collateral warranties to TIE and the Council respectively. Collateral warranties would allow TIE (now CEC Recovery Ltd) and the Council to directly enforce the warranties against the sub-contractors. Legal Services is reviewing the position in relation to such collateral warranties.

6.2 To protect the Council's position as much as possible from any other such risk within the construction industry, we are also undertaking a review of other construction companies that may have issued profit warnings to assess any further potential risks.

7. Equalities impact

7.1 There are no specific equality impacts arising from the report.

8. Sustainability impact

8.1 There are no specific impacts arising from the report.

9. Consultation and engagement

9.1 There are no specific consultation or engagement issues arising from this report.

10. Background reading/external references

10.1 None.

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