Dear Chairs,

I refer to your letter of 30 January 2018 regarding Santander’s “early payment facility” programme with Carillion and its suppliers. Our Chairman has asked that I respond as I am the Santander UK Chief Risk Officer and the Santander exposure to Carillion was managed within my division from July 2017. I welcome the opportunity to clarify Santander’s position in relation to this programme.

1. What was the nature of the early payment facility (EPF) between Santander and Carillion?

The EPF was an uncommitted facility constituted by a programme involving Santander, Carillion and participating Carillion suppliers for the payment or discounting of Carillion invoices. The EPF programme between Santander and Carillion had been in place since 2014. Santander was one of several banks that provided types of EPF programmes to Carillion and its suppliers.

The programme had two elements:

(a) A payment services agreement between Carillion and Santander that outlined the terms on which Santander would either:

(i) subject to Carillion providing sufficient funds for Santander to make the relevant payment, pay confirmed invoices to suppliers on the due date (the remittance service); or

(ii) at Santander’s discretion, buy confirmed invoices from suppliers at a discount (the discounting service).

Confirmed invoices were invoices notified by Carillion to Santander as eligible for payment under the programme.
Supplier agreements between Santander and each Carillion supplier participating in the programme.

Under the supplier agreement, a supplier could choose to sell all of its confirmed invoices to Santander at a discount (the auto-discounting service) or to offer to sell to Santander, at a discount, specific confirmed invoices at any point up until 3 days before the due date of the invoice (the ad hoc discounting service). If a confirmed invoice had not been discounted prior to its due date, it would be paid subject to the terms of the remittance service.

A supplier agreement could be terminated at any time with immediate effect by Santander giving written notice to the relevant supplier.

The programme principally operated through an internet based portal operated by Santander. Carillion periodically provided batches of confirmed invoices to Santander to load into the system. Once in the system, confirmed invoices subject to the auto-discounting service would be processed for payment and suppliers using the ad hoc discounting service could choose to nominate a confirmed invoice for discounting. Notwithstanding Carillion's deteriorating credit position, the discount rate that Santander applied to invoices accepted under the discounting service remained constant throughout 2017 and up to 15 January 2018.

2. If this was, in effect, a credit facility for Carillion, how much did the Company borrow from Santander in 2016?

The programme operated on an uncommitted basis. Carillion suppliers granted Carillion credit when agreeing the payment terms of their invoices with Carillion. The programme allowed suppliers to opt to receive discounted early payment from Santander of the amount due to them, with Santander assuming the Carillion credit risk for the relevant invoice until the invoice payment date.

In 2016, Santander’s exposure to Carillion under the programme averaged £109m.

3. How many of Carillion’s suppliers did Santander provide the EPF to?

During the course of 2017 c.270 Carillion suppliers were actively participating in the programme, of which 109 were using the auto-discounting service.

4. What led Santander to terminate the facility in December 2017?

Following Carillion’s profit warning on 10 July 2017 and the departure of the previous CEO, Santander worked with Carillion and the other lead banks to the Company in an attempt to restructure Carillion’s financial position. This work included the provision by Santander on 24 October 2017 of additional committed new money facilities of £28 million as part of a total new money package of £140 million. These new money facilities were part of a package designed as a bridge to Carillion completing certain
disposals. Despite the provision of these new money commitments and continued close engagement with Carillion into December, the envisaged disposals did not take place and the detailed business and restructuring plans originally expected to be received by 8 December 2017 were further delayed. This series of events, combined with updated financial analysis provided by Carillion to the banks’ advisors in the second week of December, further undermined Santander’s confidence in Carillion’s financial position. In light of the lack of progress with the restructuring plan, Santander took the decision to terminate the auto-discounting facility as a prudent risk management measure but to keep the ad hoc discounting service available to suppliers.

Santander served notice on 21 December 2017 to terminate the auto-discounting service for all suppliers. At that time 80 of these suppliers had live confirmed invoices in the system all of which were purchased on a discounted basis and paid by Santander. In the notice given to terminate the relevant supplier agreements with suppliers who had been using the auto-discounting service, suppliers were advised that, notwithstanding this notice, they could still nominate confirmed invoices for early payment using the ad hoc discounting service. This change meant that all Carillion suppliers would participate in the programme on the same terms i.e. ad hoc discounting service only.

5. What was the nature of the urgent discussions with Carillon and why did Santander then decide to continue the facility, albeit on revised terms?

As noted above, Santander and Carillion’s other lenders had been in discussions since July 2017. Further discussions involving Santander, Carillion, advisers and other leading banks took place over the period from 22 December 2017 to 27 December 2017. These discussions were not limited to Santander’s actions in relation to the EPF programme, but also included discussions on Carillion’s cash position and funding needs and restructuring proposals.

Santander confirmed to Carillion on 23 December 2017 that it was prepared to continue to discount invoices under the ad hoc discounting service up to an aggregate amount of its then exposure to Carillion under the programme of c.£101m. Santander was requested by Carillion to increase this exposure to Carillion’s forecast maximum utilisation by suppliers during January of £117m in order to give Carillion and its advisers more time to develop its revised business plan and financial restructuring proposals for consideration by all stakeholders. After consultation with Carillion and the other leading banks, and as part of continuing to work constructively on the restructuring plans, Santander agreed on 24 December 2017 that it would continue to offer the ad hoc discounting service on an uncommitted basis and increase its exposure in line with Carillion’s request up to an aggregate amount of £117m. The terms of the discount rate Santander applied to the ad hoc discounting service were not revised and remained constant through to 15 January 2018.

A further communication was sent to Carillion suppliers on 27 December 2017 re-confirming that the ad hoc discounting service remained in place. In the period following this communication to 15 January 2018, suppliers received from Santander a total of £14m of payments in relation to discounted invoices and a total of £0.6m in payments of invoices on their due date under the remittance service.
6. **Does Carillion currently owe any money to Santander as a result of the EPF?**

Santander’s outstanding exposure to Carillion in relation to the invoices purchased from suppliers under the programme is £91 million (including the £14m referred to in the answer to question 5 above). In light of Carillion’s liquidation Santander has taken a bad debt provision for substantially all of this amount. The EPF exposure is separate from Santander’s committed exposures to Carillion (including the new money facilities referenced at 4. above) for which we have taken significant additional bad debt provisions.

7. **Can you send us a copy of the email to suppliers referred to in the statement above?**

We append the text of the notice of termination sent on 21 December 2018 to the 109 suppliers using the auto-discounting service.

Of the suppliers who responded to the notice terminating the auto-discounting service of 21 December 2017, we are only aware of one supplier who subsequently received an inaccurate response from our customer service centre. The response from Santander customer service centre was sent on 22 December 2017 stating that “In this moment all the payments with Carillion are stopped”. This was a mistake and was corrected on 27 December 2017. All of the invoices presented by this supplier prior to 15 January 2018 were accepted and paid by Santander. The substance of the email is contained above, but as this was an email communication between Santander and a single supplier, we do not feel it is appropriate to share this correspondence without express approval from the supplier in question.

I hope that the information provided in this letter is useful, but please do not hesitate to get in touch should you need any further detail.

Yours sincerely,

Patricia Halliday
Chief Risk Officer, Santander UK plc
Appendix

Auto-Discounting Termination Notice Text

Dear Sirs,

Termination Letter in respect of the supplier agreement between Santander Factoring y Confirming S.A. EFC and [insert the name of the supplier] dated [insert date of the agreement] (the “Agreement”)

We refer to the Agreement. Terms defined in the Agreement have, where the context permits and unless otherwise defined herein, the same meaning when used in this Letter.

We would like to notify you that Santander’s operational model has changed and we are no longer able to offer the automatic payment solution in relation to all present and future invoices.

This Letter therefore serves as formal written notice of termination of the Agreement pursuant to condition 9 of the Agreement, effective as of the date of this Letter.

We may continue to offer you early payment of your invoices, at our discretion, which can be requested via our online portal or by sending us a new signed copy of the supplier agreement which we will send to you separately by email. In clause 5 of the supplier agreement please select the option entitled “Invoices specified at Clause 4”.

This Letter (including any non-contractual obligations or liabilities arising out of it or in connection with it) is governed by, and shall be construed in accordance with, English law.

Yours faithfully,