

## Carillion plc

### MINUTES OF A MEETING OF THE BOARD OF DIRECTORS

Held at 25 Maddox Street, London, W1S 2QN

On

Tuesday 22 August 2017 at 8.15 am

Present: Mr. P.N. Green Chairman  
Mr. K.R. Cochrane  
Mr. A.J.H. Dougal  
Mrs. A.J. Horner  
Baroness Morgan of Huyton  
Mr. Z.I. Khan

In attendance: Mr. R.F. Tapp Secretary  
Mr. S. Watson (part only)  
Mr. A Wollaston EY (part only)  
Ms. M. Bitar EY (part only)  
Mr. M. Parr EY (part only)

**Minute  
No:**

**ACTION**

**2181 Minutes**

The minutes of the meetings of 5, 6, 9, 12 and 20 July 2017 were approved, together with the minutes of the Committee meeting of 9 July. The Notes of the Board Calls of 19 and 26 July were noted.

**2182 Sustainability**

**Health and Safety.** Mr Cochrane presented the Health and Safety Report, which had been circulated. The format had been revised as he had asked; he felt that there remained too main key safety statistics and he would work to revisit them in the coming months.

There had been a worry that the management changes of July would give rise to a deterioration in safety: this did not yet appear to be the case, although the HFAFR had deteriorated in the period and by comparison, the equivalent of some 76% of last year's total of high risk accidents had occurred in the first seven months of 2017.

The position continued to be tracked closely and communications continued to focus on safety.

Mr Cochrane drew the Board's attention to the detail of the three incidents highlighted in the paper, with particular reference to the New Oakville incident, which had occurred in pipework in a new-build P3 hospital. Checks had not revealed a fundamental issue but the incident was, of course, of great concern.

Responding to Mrs Horner, Mr Cochrane noted that Mr Picton's focus was now on health and safety: the sustainability agenda needed to be further considered in the light of affordability and the group's current position. It was agreed that Mr Picton would be asked to present at the December meeting of the Board, with a particular focus on the construction HRAFR.

**KRC**

**Sustainability.** Sustainability was on the back-burner; there was now a need to think through how various initiatives could be taken down, and the affordability of the programme reconsidered. Proposed changes in the terms of reference were to be considered by the Board later in the meeting, which may be an interim step as the Board continued to consider the appropriate role and scope of the function. By way of example, it may be appropriate to think through volunteering days, the continued role of the sustainability advisers and the scale of the sustainability function.

Lady Morgan agreed that the position had to be reviewed in the present circumstances, but perhaps brought in the mainstream. Mr Cochrane agreed that it was of value at the margin as a differentiator and a factor in the recruitment of good people, but a change of emphasis was required. Mrs Horner noted that Blue Rubicon had looked at the primary drivers of reputation and found that performance, rather than sustainability, was key. Mr Khan confirmed that sustainability provided a mitigation to cost, rather than necessarily bottom line savings.

It was agreed that Lady Morgan would meet Mr Picton as part of her induction arrangements.

**RFT**

## **2183 Strategy**

Mr Watson joined the meeting. Mr Cochrane drew the Board's attention to the draft strategy presentation which had been circulated. He stressed that this was a "straw-man" – not the finished article, but the genesis of a direction of travel.

There was more work to do in a number of areas, although he was comfortable that there were good contracts performing well in a number of areas. The intention would be to continue to develop the framework in the coming weeks prior to the Interim Announcement at the end of September.

He spoke of his initial observations around performance, accountability, people, cost, non-core activities, transparency, culture and cash.

A number of issues were covered in discussion, including the role

of the group's Values; the possibility that the longevity of some staff in the business had led to "wilful blindness" as had been the case in the Tesco business; the value of adopting a "what and how" set of measures of the kind which Tesco had adopted; the inherent strengths as well as weaknesses of the business and the need to build on the strengths which were in place.

Mr Dougal noted that there were two themes: firstly, the apparent lack of financial transparency which the Board had become increasingly aware of over the past year, or perhaps more, with one-off items; and secondly, as working capital moved away from us, there were apparently significant operational errors on big contracts, which had not obviously been the case.

Mr Cochrane indicated that from his conversations with people in Carillion, there was a frustration that the business had not been driven in a particular direction in the last few years and had stagnated – that is seen in the financial performance. There was an issue of management capability and quality to influence the number of major projects on the go at the same time: in the UK there were three huge projects, which he did not recall previously, and problems had arisen because they were signed-up too quickly in order to get cash in – for example RLUH in 2014 to bring in advance cash.

Lady Morgan noted that the signature had been three years ago, but clearly the position had worsened. Mr Cochrane noted that MMH had been signed in four months, which meant that mobilisation had been rushed. In Aberdeen, the JV had already been established and there were recognised issues, but again we had thought they could be managed.

Lady Morgan noted that some of the pressure would undoubtedly have come from government, for example in a need to complete before government pulled funding.

Mr Cochrane reiterated that there were some very good contracts in Services – and also some in which government was not clear what it was giving us, as with the prisons contract where there was a £33m claim against the MoJ.

Work was also focusing on cash generation, on accountability and on ensuring that the right people were in place and not simply placed in roles which were not appropriate to them. Responding to Lady Morgan, he noted that he felt that those within the business who would respond to change, be willing to be led, or to resist were within the typical ranges of 25/50/25 percentages. There were positive indicators with the next generation of leadership. Inevitably there was defensiveness and blame of particular projects, whereas there should be collective ownership.

Mr Cochrane noted that the EY feedback reported layers of overhead and inefficiencies, with a need for a global redesign. There was significant resource employed in preparing for and reporting to PRM, which was generating too much information. He

had already cut down on the number and content of PRMs.

Mrs Horner noted that the review of lessons learned on projects which had been presented at the June meeting had been a collection of data, not insight. Mr Cochrane agreed, noting that that had not driven the ability of businesses to consider what they should do.

The Board discussed the consequences of failure within the business, together with the need to create respect and inspiration within the organisation, so that it was aligned to a single vision which may pleasantly surprise it – but that did require radical change.

Moving to priorities, the Board noted the focus on simplification, selectivity, efficiency, culture and capability.

Elements which distracted from the core purpose, such as giving executives non-core business responsibilities, allowing cross-charging, internal re-charging and other such arrangements which had made the identification of underlying numbers more difficult. There would be an alignment to a focus on cash throughout the year, and not simply at full- and half-year points.

Mr Watson took the Board through the draft strategy proposition, focusing on few bigger things, with better people. This would focus on selectivity in the clients we work for, fewer, larger contracts, selectivity in the support services we provide, a focus on core services, selectivity in building and infrastructure, and selectivity in geography.

He touched on issues of differentiation, comparing the strategy proposition to those of competitors, and considering the implications of the factors of sustainability, community engagement, health and safety, quality and timeliness, cost/value and people and culture. Mr Cochrane noted that he felt this required a mind-shift in the organisation, and a radical reshaping.

The “straw-man” proposition was of four sectors – Building, Infrastructure, Central Government and Regions & Corporate, being achieved through selectivity, quality, collaboration and safety. The detail of each sector was discussed, and Mr Watson and Mr Cochrane led the Board through each element.

In discussion, a number of points were noted, including the increasing difficulties in the education sector, the need for good project management as well as design, planning and mechanical and electrical competence, the opportunities in rail presented by new procurement frameworks (as Wales and Borders), and the broader strategic questions presented through joint ventures.

Mr Cochrane noted that the intention was to flesh out the proposed design, together with its leadership, over the coming weeks prior to an announcement in September.

Finally, a summary of recommendations on exits and disposals was noted, with 2017 and 2018 priorities. Significant interest had been received in a number of businesses, and the detail of each key opportunity was discussed. Clearly disposals, and the timescale in which they could be achieved, were dependent on the willingness of the counterparties to proceed but they were being pursued with vigour.

There were three remaining action areas under the strategic review – of strategy, disposals and the business plan, and progress on each was noted.

## **2184 Ernst & Young Update – Project Ray**

Mr Wollaston, Mr Parr and Ms Bitar joined the meeting. Mr Cochrane introduced their report, noting the scope of their work. It remained to be fleshed out but he explained the purpose of the work and its intended audiences.

Responding to Mr Dougal, Ms Bitar explained that the process which had been undertaken was “outside-in”, which was then grounded in information. There had been individual data requests on contracts and a few interviews, together with a sample activity list of around 150 people in terms of how they spent their time.

The report was very judgement-led – “this is what we would do”, based to some extent on data, and on what was seen in other sectors in which EY had worked. The paper presented was an extract of a 150 page report, some parts more in-depth than others; it was observational rather than a comprehensive analysis of data.

It was noted that the report covered the overall opportunity; the operating model, proposed headcount reduction, third party spend opportunity, immediate cost-saving opportunities, indicative phasing and implementation costs, and early views in relation to the Middle East and Canada.

There were five key performance observations, around short-term prioritisation, level of complexity, transparency, data, and the value of the Group. These were rationalised into the key themes of focus on where we make money, simplification and delayering, and upgrading of systems, processes and skills.

The paper focused further on the value chain, the organisational pillars which should underpin it, the creation of centres of excellence, and a possible preferred option of a central operating model with shared centres of excellence and back office services.

Ms Bitar took the Board through the paper; the following points were noted in discussion:

- There was a reference to a culture of non-compliance. Ms Bitar clarified that she meant that this was the case in

relation to ignoring central procurement requirements. Mr Dougal noted it was important to identify areas where that was the case;

- There was a reference to a lack of accountability. Ms Bitar noted that she had observed a bias toward delivery – and that a lot of what EY had observed had not come as a surprise to people;
- There were some pockets of key strengths, but a culture of making the numbers. There were good people on contracts, doing what clients wanted and doing a good job;
- There were pockets of the business where work was done well;
- The Sheffield CEC was clearly an effective organisation and had become more so in the past 18 months – that would fit with the proposed model. The Manchester engineering function was loss-making and less clear-cut;
- The EY approach was to have dual solid line reporting and to remove functions from businesses, so that for example the sectors would not each have a Finance Director, but a business partner who also had a solid line to the CFO. That situation would apply equally to HR.
- The appointment of a Chief Transformation Officer was contemplated, together with a number of other changes to senior roles;
- The paper recommended very significant headcount reductions, and that the appointment of the right sector leads was very important – people who would be passionate advocates of the strategy and structure which was finally adopted;
- A core narrative which would engage the organisation would be important, together with a refreshed corporate vocabulary – for example new meeting names. It was proposed to introduce a new communication agency to support the change; as part of this process it was important that the strengths of the business were highlighted as well as the critical need for change;
- The business had been focused on cost-cutting for many years: there had been a criticism that that had not hit the bottom line, and it was important that in this process, savings were retained;
- Governance of the process would be important, and Ms Bitar outlined the issues and the need to ensure that relevant stakeholders worked closely together;
- There was still validation to be done and choices to be made: things would change as the process of design began;
- The business would need help to work through the timetable and process.

The Chairman thanked the EY team, who left the meeting together with Mr Watson.

The Board reflected on the report and the next steps, considering the position in detail in relation to the proposals, possible next steps, messaging, choices, and on the EY process.

The Chairman noted that the Board was supportive of the work which had been done to date and on the continued work now envisaged to develop a structure and strategy. Mr Cochrane noted that the possibility of an announcement around certain elements in early September was under review, and the Board would be kept apprised of the need for further authorisation in due course.

**2185      Trading Update and Material Developments in Relation to Contracts**

Mr Cochrane noted the contract review in hand, as previously advised to the Board at the previous calls. He would brief the brokers and advisers on strategy on Thursday.

**2186      Market Update and Feedback from Shareholders**

A detailed update had been received from HSBC, which had been prepared in consultation with the other brokers.

The update was discussed and noted. The Board reviewed the possible equity process considerations which were outlined in the paper, together with the likely timing and resource implications and their relationship to the prospective disposals which had been discussed earlier in the meeting.

The Board also noted the position concerning possible funding streams from HSBC and Royal Bank of Canada, and Mr Khan noted the steps which they sought to be concluded before such funding might be made available. The Chairman asked that the position should be pinned-down with the banks as a matter of urgency.

In response to a question from Mr Dougal, Mr Cochrane considered the position as to whether an equity issue would, or would not, be required, and considering also the relationship with any possible strategic investor.

**2187      Chief Executive's Report**

The Report had been circulated and was taken as read.

Mr Cochrane spoke to his report, noting the current position with the banking groups, and discussions with the pensions trustees and the regulator.

Contract wins included a £40m contract with Abellio, although the DoT FM bid had been lost and the DWP result was awaited. The conclusion of the Carilliontelent Gigaclear and Virgin Media bids was awaited.

Challenges remained with elements of the supplier base, most

notably with Booker in relation to Hestia.

He reported further on the likely changes consequent on the strategy and structure discussions considered earlier in the meeting, the complexity of execution, and the position with regard to strategic disposals.

He briefed the board on key contracts, including Hestia, Aberdeen, Liverpool and MMH, and on the Canadian Maritime Link and TTC discussions as well as on the Mshereib and Al Dara contracts.

In Oman, the position remained challenging and the group had had to fund the business in order that it could pay wages in the month. Three bonds had been called in the Botanic Gardens contract, and lawyers were in court earlier in the day to seek an order that payment should not be made under the bonds.

**2188 Project Hestia**

Mr Cochrane spoke to the presentation, which had been circulated. After discussion, the presentation was noted.

**2189 Finance Director's Report**

Mr Khan noted that the June and July reports had both been circulated with the papers, and he drew the Board's attention to the highlights of each month's trading, noting the areas which remained under review and the further involvement of KPMG.

There were reduced volumes in Building in the period, with operating profit down on forecast and on the same period in 2016; there were also shortfalls in services with D3 savings not having materialised to the extent anticipated in consequence of a number of factors, including the highly ambitious programme of savings, timing and the like. Mr Cochrane noted that this reflected the undue complexity of the business.

Mr Khan reported on the liquidity/net debt position covered in his paper, detailing specific impacts as a result of the treatment of joint venture funds. Overall, the level of receipts which might have been expected following the Trading Update had not been seen, although there were a number of positive discussions in hand.

Mr Khan noted the lender position, noting that a 13 week forecast had been submitted to the banks earlier in the week, and that discussions continued with the four key banks who were acting as a lead for the RCF banks.

He noted that the current pinch point was in mid-November, where there was committed headroom of £103m, and he noted the key assumptions in that forecast.

With regard to the banking position, Mr Khan noted the continuing

position on the National Bank of Abu Dhabi, Bayern LB and Svenska facilities. He noted also that discussions continued with credit insurers.

The pension deficit stood at £581m at the month-end on an accounting basis.

The Work Winning Reports and Summary of MPC Approvals were noted.

**2190 Top 10 Risks**

Mr Cochrane would review the paper and revert. The matter would be brought back to the Board in September.

**KRC /  
RFT**

**2191 Sustainability Committee – Terms of Reference**

The revised terms of reference, which had been circulated, were approved.

**2192 Any Other Business**

Mr Cochrane noted that he would shortly be appointed as a director of Third Energy Limited. The business was a private company and no obligation arose for the appointment to be announced by Carillion.

**2193 Next Meeting**

The next meeting would take place on 27 September 2017 at 8.30am.

**2194 Chairman and Non-Executive's Review**

The executives left the meeting and the Chairman and non-executive directors held a short review meeting.

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**CHAIRMAN**