



FAO: Rt Hon Frank Field MP, Rachel Reeves MP

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

House of Commons

London

SW1A 0AA

10 April 2018

Dear Mr Field and Ms Reeves

Carillion inquiry

- 1 During the course of your inquiry into the collapse of Carillion plc, a number of pieces of correspondence and other documentation have been published on your website. In reading this material, there were a number of statements made which I do not consider to be correct. In particular, I would like to comment upon the points which have been made by Msheireb Properties.
- 2 Given the degree of public scrutiny which has, quite rightly, attached to the circumstances of the collapse and the fact that a number of agencies are currently involved in investigating these matters, it is critical in my view that your inquiry has access to fair and complete information.
- 3 In order to remain focussed on the key areas of concern and not to make this letter of unnecessary length, I have not taken issue with every point with which I disagree in the letters to which I refer (in particular the letter from Msheireb Properties, which calls for a more detailed response than I am able to provide here), rather I have grouped my responses to the letter from Msheireb Properties into 4 key points. I am also aware that I do not have full access to all documentation and therefore my response is limited to the documents I do have and my recollection.
- 4 Further, given that the Official Receiver may have claims against Msheireb Properties I would again respectfully ask the Committee to confirm with the Official Receiver whether they have any concerns before this letter is published.

Undated letter from Msheireb Properties, published 27 February 2018

A Failure to pay on a timely basis and administer the contract fairly

- 5 I stated before your inquiry on 6 February 2018 that the Carillion-led joint venture delivering this project ("**CQBC**") was owed approximately GBP200m by Msheireb Properties at the point I left the business in September 2017. My letter of 21 February 2018 confirmed the exact amounts which Carillion had claimed were due. In its letter, Msheireb Properties denied this and claimed

that CQBC was paid at regular monthly intervals from January 2012 through to January 2017 "without exception" (page 2 of Msheireb Properties' letter) and that amounts were released in accordance with the time period set out in the contract.

- 6 This is simply not correct. The principal reason for my frequent visits to the site was the huge volume of design change required by Msheireb Properties, which increased the cost and caused delay to the project; and the serially late monthly payments, which CQBC experienced throughout the duration of the contract. Had we been paid in a timely fashion for the contracted works and the variation works which were requested by the client, I simply would not have needed to visit Qatar as frequently as I did.
- 7 To evidence the scale of the non-payment problem with Msheireb Properties, I instructed the Carillion commercial team to run an exercise to calculate the number of days that Msheireb Properties were late in paying us. I understand that that exercise was maintained. It may assist the Joint Committee to ask for a copy of this document. From memory, as at the point when we were around 1700 days (i.e. 4.6 years) into the contract, Msheireb Properties had paid us around 1000 days late cumulatively in respect of contracted monthly payments. Following communication of this historic performance to Msheireb Properties, the timeliness of the payments from Msheireb Properties to CQBC improved until October 2016, albeit not the quantum owed.
- 8 This does not also take into account Msheireb Properties' failures to properly administer on a timely basis (in accordance with the contract) variations and EoT claims (I referred to both in my response to the Committee and in my letter). For these reasons, I do not accept Msheireb Properties' comments at page 4 of its letter concerning CQBC's alleged "poor performance". Carillion and its supply chain used their own resources to a considerable extent to attempt to plug the funding gap and move the project forward, but when a contractor is left unfunded for a considerable period of time, wrongly, combined with a high level of change there will inevitably be an impact on the progress of a project.

B Valuation and payment of costs associated with Extensions of Time ("EoT")

- 9 At the heart of the delay and non-payment issue was Msheireb Properties' failure to value and pay EoT and variations in accordance with the contract. The principal EoT 3 claims (EoT 3A, 3B and 3C (part)) were made on 31 July 2016, with a subsequent claim (EoT 3D) made on 17 May 2017, all in respect of time overruns deriving from design changes required by Msheireb Properties. As a result of Msheireb Properties' failure to value and pay this claim, CQBC and the supply chain had to fund their staff costs, plant and equipment from, I think, September 2013 to certainly until after I left. During this time, only one "on account" payment was made against EoT3 for the very significant services provided, which was made in December 2016, in an effort, I believe, by Msheireb Properties to support and achieve completion of the contract during 2017.
- 10 Msheireb Properties does not accept that it owed CQBC £200m at the point when I left the business in September 2017, stating that that figure must relate to work then remaining to be completed. This is not the case. The figure I gave and which I detailed in my letter in the main related to EoT3 and variations complete or in progress, which were properly claimed within CQBC's monthly valuation application under the contract, but which Msheireb Properties had failed properly to administer. In my letter to you of 21 February 2018, I set out the figures. In March 2017, from memory, around 90% of the works were completed. By August, when CQBC had left site, works were around 93%-96% complete (Msheireb Properties' figure was 96%, ours was 93%). Accordingly, their comments are incorrect and I remain of the view that very significant sums remained owing to CQBC in September 2017. Whilst CQBC applied for the monies I set out in my previous letter within the March 2017 payment application, not all of these

amounts were traded within the group accounts as revenue, which is possibly why Mr Meehan, KPMG, did not recognise the amounts I communicated in my previous letter.

- 11 Msheireb Properties' letter tries to argue that the amounts owed to CQBC were assessed by "independent" and "reputable international cost consultants and quantity surveyors". This is misleading. There were two consultants engaged by Msheireb Properties: (1) Turner International; and (2) AECOM. Turner International are, I believe, partially owned by the Qatar foundation (namely Msheireb Properties' ultimate parent and sponsor) and so are not independent. I believe the second consultant, AECOM, was independent but their advice was often ignored or overturned by Msheireb Properties. For instance, AECOM's advice in relation to some of the variations issued by Msheireb Properties in the period up to October 2016, supported CQBC's claims which were paid by Msheireb Properties, but the advice was subsequently overturned by Msheireb Properties. This occurred even after Msheireb Properties had paid CQBC, who had then paid its supply chain, resulting in Msheireb Properties reclaiming payments made by deducting monies from subsequent monthly applications from CQBC.
- 12 To try and resolve these issues and to allow the project to move forward CQBC commissioned an independent report by FTi into the appropriateness of CQBC's EoT 3 requests. This report concluded that CQBC's EoT 3 requests were fair and that Msheireb Properties' assertions in many respects were unreasonable and flawed. FTi also reviewed Msheireb Properties/Turner's delay analysis and concluded it was severely flawed. We attempted to organise workshops in Doha with Turner and Msheireb Properties and CQBC flew FTi in from the UK so that they could discuss their conclusions with Turner and Msheireb Properties. The representative from Msheireb Properties either failed to appear for the workshops or left after a short time having been unable to offer any substantive response to FTi's points. You may wish to ask the Official Receiver for a copy of this report. I am also aware that CQBC kept a diary of missed, failed or shortened meetings throughout 2015, 2016 and 2017 whereby CQBC endeavoured to obtain the cash flows it was entitled to in order to fund progress and completion of the works.
- 13 Carillion also sought in writing the assistance of a UK Government Minister to assist it with its negotiations with Msheireb Properties given the considerable amounts owed. The Joint Committee may wish to ask the Official Receiver for a copy of that letter.
- 14 The issues I have raised above are also confirmed by a number of independent newspaper articles, which I have seen recently (copies attached) dating back over the last few years, that clearly demonstrate that Carillion's experience with Msheireb Properties (owned by the Qatar Foundation) has been and is being experienced by a large number of other contractors and sub-contractors in Qatar.

- (a) "Qatar building boom proves a challenge for foreign construction firms", Reuters, 23 June 2015: <https://www.reuters.com/article/qatar-construction/qatar-building-boom-proves-a-challenge-for-foreign-construction-firms-idUSL5N0YU1BK20150623>

The Article notes that "Construction companies and consultants are bank-rolling the projects for their clients," said the source. Getting their money back can be a lengthy process.

"Project exposure is tens of millions of dollars, which becomes untenable - they tie us up in their approvals process ad infinitum," said the source. "The money trickles out eventually, but you want a fair day's pay for a fair day's work. They (Qatar) try to shave it off at various stages."

"Contracts in the Middle East generally favour the client more than they would in the West, for example. There are a myriad of clauses that make the contractor liable," said Nick Smith, Partner at engineering consultants Arcadis in Qatar.

Clients unwilling to pay for design alterations is one obstacle, said a second construction industry source who spoke on condition of anonymity.

"Most contractors suffer major cash-flow shortages, in part because clients don't accept paying extra for essential changes due to the original design plans being late or inadequate and unworkable unless amended," he said."

- (b) "Qatar's MEP business hit by disputes and delays", ME Construction News, 19 July 2016: <http://meconstructionnews.com/15490/qatars-mep-business-hit-by-disputes-and-delays>

"Delayed payments which affect cash flow [are a major issue in Qatar]," says Murali S, managing director of Al-Futtaim Engineering, a Dubai-based MEP contractor with operations in Qatar. "Regular cash flow has been a structural problem that is affecting the whole industry."

Further, the article noted increases in Qatar for legal advice as a result of delayed payments; and that such delays were lengthy, with it taking much longer to resolve final accounts sometimes years. Variations were also seen as another critical issue along with reluctances to award EoT claims.

C Design changes and administration of change

- 15 There was an abnormal amount of change over a long period of time on the Msheireb contract, all driven by Msheireb Properties, which was extraordinary even taking into account the scale of that project. This was in part due to Msheireb Properties changing lead architectural designers on two occasions and subsequently not having a lead designer on the scheme.

- 16 I stated before your inquiry that Msheireb Properties issued around 40,000 new drawings. As I clarified in my letter to you of 21 February 2018, Msheireb Properties in fact issued 25,000 new or revised drawings but these drawings were inadequate and CQBC (and its suppliers) were then forced to produce approximately a further 38,000 new drawings itself to make MP's design workable. CQBC and its supply chain were obliged to provide certain specialist working drawings, but not to the extent they did, which was as a result of Msheireb Properties' inadequate and changing design. In its letter to your inquiry, Msheireb Properties took issue with that number, claiming that "there were a considerable number of variations on the project, although there were only 700 – i.e. 28% of the number that Carillion alleges". This is not an accurate summary. I have since found a 10 May 2017 Design Summary (copy attached) which provides further clarity on this issue:

- (a) Msheireb Properties has confused the number of new drawings with the number of changes on the project. As is evident from contemporaneous documents (see the 10 May 2017 Design Summary, attached), up to May 2017 there were 103,645 shop drawing submittals (from CQBC to Msheireb Properties), 41,992 shop drawings (from CQBC to Msheireb Properties), 10,860 Requests For Information from CQBC to Msheireb Properties, and 33,217 'Issued For Construction' drawings or revisions from Msheireb Properties to CQBC (this figure is the original contract drawings plus new and revised drawings);

- (b) There were 7,738 drawings contained in the contract, a further 25,479 "Issued For Construction" drawings were subsequently issued, 5,878 were new drawings entirely and 19,601 were revisions;
- (c) CQBC and its supply chain then had to produce in the region of 38,000 new drawings itself to compensate for the fact that Msheireb Properties did not have a regular architect on the project to do this work (having previously stood down two architects). Such a step was completely unprecedented.
- (d) To give you an idea of the size of the variations, the first variation, Bulletin No 1 contained over 2000 drawings.

17 The contract was not a design and build contract, meaning that Carillion was not responsible for the design. Instead, Msheireb Properties contracted to provide CQBC with a full working design from the commencement of the project. They not only failed to do this but also allowed significant and excessive change to prevail in an unmanaged and haphazard way throughout the contract, leading to significant cash flow challenges for CQBC. Had the project been "design and build", then CQBC would have taken ownership of the design aspects. What was clear to Carillion (by Q2 2017) when we looked at the amount of change as against what had originally been designed (this is recorded in the design summary attached) is that the design can only have been between 17% and 23% complete when Msheireb Properties moved into the construction stage of their project. I have never seen this amount of change on a project in my 27 years in the industry.

D. Termination of CQBC after Msheireb Properties withheld significant amounts over a long period

18 In their letter Msheireb Properties state that "When construction progress at Site reached a sufficiently-advanced state of completion, their construction supervision services (only) were removed, and a new Supervision Consultant was engaged. The new Supervision Consultant adopted a more flexible and proactive approach to the contractual review, inspection and approval processes, to the benefit of the Contractor." This is incorrect. I understood that Msheireb Properties replaced CQBC unlawfully with, CCC, with effect from July 2017, in breach of contract and despite the advanced state of the project at that time, the works have still not been completed.

19 Msheireb Properties' letter in a number of places suggests that cash was in fact being passed to CQBC to fund the project and that Msheireb Properties voluntarily released and made generous and premature payments to Carillion to assist them with their cash position on the understanding that the works would be progressed. This is simply not correct. CQBC used various measures to try and avoid making actual payments and failed to administer claims in accordance with the contract. For example, I believe what Msheireb Properties are referring to by voluntarily releasing payments is payment of retention monies to Carillion. However, as the inquiry will appreciate, it is in the nature of a retention that the funds retained have already been earned by the contractor for historic works. This was therefore for work we had already done and was not new money. Further, whilst Msheireb Properties made advance payments these were made against on demand advance payment bonds provided by CQBC and the payments themselves were therefore of limited value, with the bonds unwinding progressively to zero over either the next 6 or 12 months of the contract.

20 I am also aware from the annual Msheireb Properties CEO forum, which we attended along with the CEOs of Multiplex, Obayashi and Arabtec, that these other contractors experienced the same issues as CQBC. I would respectfully invite the inquiry to seek evidence from these

companies, which I believe would validate the points I make above in respect of Carillion's experience in Qatar.

- 21 In a similar light, as mentioned above, I have found recently various newspaper articles which corroborate the experience that Carillion has had in Qatar. In 2014 it was reported that Qatar Foundation had taken similar unlawful steps against OHL, as those taken by Msheireb Properties against Carillion, by removing OHL from their role in building the Sidra Hospital, when the project was 95% complete. The announcement to the LSE by OHL stated that the reasons given by Qatar Foundation lacked "any legitimate grounds." (OHL to sue Qatar after Sidra hospital contract terminated", Doha News, 24 July 2014: <https://dohanews.co/ohl-sue-sidra-hospital-contract-termination/>)

Letter from the inquiry to Emma Mercer dated 26 February 2018

- 22 This letter seeks information from Mrs Mercer in relation to the concerns around accounting issues which she raised with me, Mr Khan and subsequently Janet Dawson, the Group HR director. I thought it may assist the inquiry if I were to include in this letter a brief chronology of my own involvement in this matter, which I believe shows that I acted promptly and appropriately when I learned of Mrs Mercer's concerns:

- (a) **14 April 2017:** I learned from Adam Green that Mrs Mercer had found some working capital allocations in the Carillion Construction Services accounts that she was not entirely comfortable with. I asked that these concerns be detailed at the next Project Review Meeting ("PRM"). The same evening I notified Mr Khan (then the CFO) that Mrs Mercer would be presenting these issues at the next PRM and I asked him to spend time with Mrs Mercer in advance to understand the issues in more detail and report back to me.
- (b) **26 April 2017:** Mrs Mercer presented her concerns at the PRM. Following the meeting I asked Mrs Mercer and Mr Khan to meet again to thoroughly review the position together and report back to me within a few days.
- (c) **3 May 2017:** Following the AGM, Mrs Dawson asked me to meet with Mrs Mercer one-to-one, as Mrs Mercer remained concerned that she had made little progress with Mr Khan. I was due to fly to Qatar that evening so I asked my PA to arrange a meeting between Mrs Mercer and myself to take place on my first day back in the UK, which was Friday 5 May 2017. That same evening, I notified the Chairman, Philip Green, who I understand then notified the rest of the board. I also informed Mr Khan that I would be meeting Mrs Mercer and that I had notified Mr Green.
- (d) **5 May 2017:** I met with Mrs Mercer one on one in Leeds to discuss her concerns. I then immediately arranged for work to be done over the weekend of 6/7 May 2017 by senior personnel to better understand the issues and to prepare to brief the board during the following week (commencing 8 May 2017).
- (e) **7 May 2017:** I held various discussions with Mrs Mercer and the team I had tasked with examining the issue over that weekend. I also briefed Mr Green, the head of the audit committee and representatives of our brokers, Stifel and Morgan Stanley. Mr Green and I agreed that a sub-committee of the board should be formed, to be chaired by the head of the audit committee and attended by Keith Cochrane, to investigate the issues further. I wanted that committee to be independent and it was.

- (f) **9 May 2017:** A board meeting by telephone took place, where I introduced the issues. Following this board meeting, a "clean" team at KPMG was appointed to run a full investigation under the direction of, and reporting to, the board sub-committee that Mr Green and I had established for that purpose.

Letter from Zafar Khan dated 21 February 2018

- 23 Mr Khan's letter acknowledges the fact that the company's debt levels had grown over several years prior to his appointment as CFO in January 2017 (during which time, as Financial Controller, Mr Khan was the "number 2" to the then CFO, Richard Adam).
- 24 In 2013 (and subsequently at various stages) when the group debt levels had continued to rise, primarily due to the descaling of the UK construction business by 50% between 2009 and 2012 and the acquisition and subsequent de scaling of Eaga Energy Services, both as a result of the changes in government policy, the board discussed various steps to reduce debt, but Mr Adam explained to the board that such steps were not necessary given the additional facilities he had previously obtained and could be secured going forwards and the fact that the cash flow projections at that time were such that improved cash would be generated going forward.
- 25 In Q2 2016, the board, supported by our corporate brokers, held a number of discussions relating to the level of debt within the business. Mr Adam presented to the board the history of the debt evolution, the current cash projections, which included further cost reduction initiatives and contract settlements, which he explained would deliver gradual debt reduction. In addition to these actions the Chairman and I instigated a process of disposals with the ambition of raising around £100m.
- 26 Accordingly, whilst Mr Khan is correct to note that debt played a role in the company's final position, it is important that the inquiry understands that the board, led in this respect by an experienced CFO, had been closely monitoring the situation for some years previously and had taken steps to address the position before Mr Khan's appointment as CFO.

Letter from Mike Cherry, FSB National Chairman dated 27 February 2018

- 27 Mr Cherry's remark that "*[i]f it is simply not good enough to point to an early finance scheme as proof of good practice, when a company has admitted operating with formal payment terms of up to 120 days*", ignores the reality that Carillion's supply chain was typically paid within 30 days (for Government suppliers) or 45 days (for other suppliers). By signing the Government's Prompt Payment Code we committed to paying Government suppliers on 30 day terms. In 2012, the UK Government asked Carillion (and other major companies) to introduce a supply chain finance initiative, which Carillion did in early 2013. It was called an Early Payment Facility ("**EPF**") and it allowed suppliers to choose when they took payments on approved invoices, which they could do at no cost to themselves on 30 days on government contracts and on 45 days on non-government contracts. So whilst the contracts between Carillion and the suppliers often provided for 120 day payment terms, the reality was that suppliers were paid within 30 or 45 days, as a result of the EPF. Carillion met the cost of the interest between 30 or 45 days (as appropriate) and 120 days and suppliers could opt for even quicker payments (i.e. under 30 days) for which they would be charged interest at a lower rate than they would be able to obtain themselves. The 120 days effectively set the time period with which Carillion paid its EPF partner banks, not the time period it took to pay its suppliers.
- 28 In fact, far from "dismissing" small suppliers, on a number of very significant Government contracts Carillion ensured that its supply chain was paid even though Carillion had not been paid by its customer, the Government. This was particularly evident on a number of

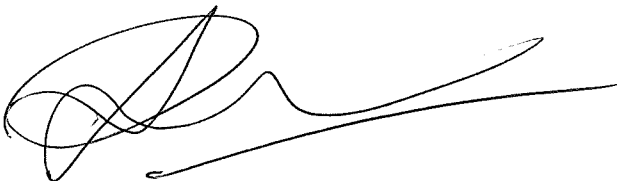
Government services contracts, where Carillion encountered very significant discrepancies between the contracted scope and the actual scope of the Government Estate. For example, we found that the size of the actual estate and assets to be maintained to be substantially larger than the Government customer had stated in the contract. In these cases, Carillion was expected to fund the extra work for months and occasionally years, before the Government paid us for the additional work and substantial sums were still outstanding when I left the business. Emma Mercer would be able to confirm what was still outstanding on UK Government and related contracts at the time of the liquidation. In the meantime, Carillion funded its suppliers on these contracts from its own funds.

29 One example of this happening in practice was the prisons maintenance contract ("**NOMS**") tendered by the Ministry of Justice ("**MoJ**"). When Carillion won the contract to maintain prisons in the South of England, we found as we began to maintain the 54 prisons that the asset registers (i.e. the registers of assets which needed to be maintained by the contractor, such as smoke alarms, lifts, etc.) which the Government had previously maintained and which had formed the basis of the tendering process, were significantly incorrect. In fact, I recall that there were approximately 60% more assets to maintain across the prisons forming our contract than had been disclosed by the MoJ in the tender and which Carillion had accordingly priced for. In monetary terms this meant that Carillion, I believe, was initially incurring approximately 35% more cost than it was being paid to maintain and service, in good faith, an estate which ultimately was not properly understood by its owners. Although the MoJ did make some on account payments, when I left in July 2017 the costs which Carillion was seeking to recover in relation to the differing scope were around £15m. In the meantime Carillion had paid its people and its supply chain, many of them SMEs, each month while trying to negotiate a fair contract adjustment to the contract scope and pricing. This was not forthcoming and in my mind was grossly unfair. This point also relates to the comments made in the select committee in relation to timely payments to suppliers. In many instances, particularly with support service contracts, Carillion paid its supply chain in advance of the customer paying Carillion for scope 'gaps', as described above, or for variable works while waiting for the contract scope change and variable works to be administered fairly for payment. The positive affect of Carillion paying its supply chain in advance of its customers paying Carillion was never recognised as a positive or even as a burden on the contractor.

30 I also do not accept Mr Cherry's suggestion that Carillion adopted a practice of using technical faults with the way invoices were presented as a means of delaying or denying payments to suppliers. It is right, and appropriate, that Carillion reviewed invoices before making payment and if the invoice did not match the delivery ticket or approved works then questions would have to be asked, which could cause delays. These requirements were not confined to Carillion; our customers rightly employed the same requirements in respect of Carillion's invoices.

31 I remain available to answer any further questions you may have.

Yours sincerely

A handwritten signature in black ink, appearing to be 'Richard Howson', written in a cursive style with a long horizontal stroke extending to the right.

Richard Howson