31 May 2016

Dear Sirs

BHS – Oral Evidence Session on 23 May 2016

1. I refer to the joint oral evidence session on Monday 23 May 2016 before the Business, Innovation and Skills Committee and the Work and Pensions Committee (the 23 May Session). At the 23 May Session, I agreed to follow up in writing on two specific points raised by the Committees. I have set out explanations of those points below, along with two additional points of clarification, using the references to the question numbers in the published transcript of the 23 May Session.

Questions 566 to 569: What was the reason for the share capital reduction in Taveta Investments (No.2) Limited?

2. In response to questions 566 to 569, I agreed to come back to the Committees in writing in relation to the historic share capital reduction at the Taveta Investments (No.2) Ltd (TIL2) level. It was suggested at the 23 May Session that this took place in 2002; however, I have since confirmed that it took place in 2004. I became a director of TIL2 on 21 September 2004, but I was not on the board of its parent, Taveta Investments Limited (TIL), at the time. I have made enquiries into the share capital reduction and my understanding is as follows:

(a) The share capital of TIL2 was 2,300,000,100 ordinary £1 shares. 2,300,000,000 of those shares were allotted to TIL in consideration for the transfer by TIL to TIL2 of its shares in Arcadia Group Limited (AGL), which represented the approximate market value of AGL. On 23 September 2004, it was resolved to reduce the share capital to
10,000,100 ordinary £1 shares, subject to court approval and the agreement of the creditors of TIL2.

(b) The share capital reduction, once approved and effected, created distributable reserves of £2,290,000,100. The purpose of the share capital reduction was to create such distributable reserves in order to enable the payment of interim dividends. Interim dividends of £1,300,000,000 were paid by TIL2 to TIL, the 100% shareholder in TIL2, in the financial year ended 27 August 2005.

3. Taveta took accounting and tax professional advice in relation to the above steps and Inland Revenue (now HMRC) clearance was obtained in advance.

4. It is important to note that BHS was not part of the Taveta group at this time and the interim dividends were not in any way connected to the trading of the BHS group. TIL2 acquired BHS Group Limited in July 2009. Given some of the recent comments made in the press and the written evidence from Professor Prem Sikka published on the Work and Pensions Committee website, this seems to be an important point to clarify.

Questions 599 to 601: going concern statement in BHS Limited 2014 accounts

5. In response to questions 599 to 601, I agreed to come back to the Committees in writing to confirm whether the auditors of BHS Limited were aware of the minutes of the AGL board meeting on 4 March 2015. I have looked into this and the position is as follows:

(a) The auditors of BHS Limited did not receive a copy of the minutes of the AGL board meeting on 4 March 2015. However, the going concern statement by the directors in the accounts of BHS Limited in respect of the financial year ended 30 August 2014 (the BHS 2014 Accounts) was made based on support from TIL2, not AGL. The relevant wording in the BHS 2014 Accounts is as follows: “The directors believe that preparing the financial statements on the going concern basis is appropriate due to the continued financial support of the Company’s ultimate parent undertaking, Taveta Investments (No.2) Limited.”

(b) This statement was made following receipt of a letter from TIL2 to BHS Limited, and other BHS companies, on 6 March 2015. The letter stated: “We confirm that it is our intention to finance the above companies so as to enable them to meet their liabilities as they fall due and carry on their business without a significant curtailment of operations during the course of the next twelve months, whilst it continues to be under the control of Taveta Investments (No.2) Limited.” Consequently, the BHS 2014 Accounts were signed off on the basis of support from TIL2.

Additional points of clarification

6. Having reviewed the published transcript of the 23 May Session, I would like to clarify some of the statements made.
Questions 545 and 556: guarantees provided by AGL in connection with the sale

7. First, I note some inconsistency in my references to the guarantees provided by AGL to support new financing obtained from HSBC in connection with the sale to Retail Acquisitions Limited (RAL).

(a) In my response to question 545, I said "In fact, overall, Arcadia was going to give £110 million worth of guarantees to various financial mortgages and loans that RAL had." (extract from full response)

(b) In my response to question 556, I said "The majority of those guarantees were still in place when it went into administration. I believe the figure is that £85 million of the initial £120 million of guarantees were still in place at the time of sale."

(c) I would like to clarify that:

(i) AGL provided guarantees in respect of facilities worth £110 million in total;

(ii) those guarantees were in respect of facilities provided by HSBC to entities within the BHS group, rather than RAL directly;

(iii) I intended to refer to the outstanding guarantees in place at the time that BHS went into administration in my response to question 556, rather than "the time of the sale"; and

(iv) at the time BHS went into administration, the outstanding drawn amount of such facilities was £54.5 million. This had reduced from £110 million at the time of the sale, as BHS subsequently: (I) ceased to use the £25 million working capital facility from HSBC; (II) disposed of certain of the properties in respect of which the facilities had been provided and guaranteed; and (III) made mortgage repayments which reduced the amount outstanding.

Question 495: reference to due diligence by solicitors

8. Secondly, Lord Grabiner has asked me to correct his response to question 495. The transcript accurately records his words. However, he inadvertently referred to the "solicitor acting for the buyer" when he intended to refer to the "solicitor acting for the seller". I have set out below the relevant passage from the transcript (emphasis added).

"Lord Grabiner: Well, I sat in on your earlier hearing and heard the evidence that was given by the Linklaters partner. It seemed to me that he was being assured by his opposite number at Olswang that they had done some suitable due diligence on their client, and that the Linklaters lawyer was actually going beyond what one would normally do in that sort of situation. As I think he rightly pointed out, ordinarily the solicitor acting for the buyer would not be concerned with such an exercise, as it would always be a responsibility of the solicitor on the other side. He was satisfied by what he was told and left it at
that. As to what happened at the Olswang end of the story, it is, as was pointed out, a highly reputable law firm. One assumes that it did their job properly.”

Questions 536, 537 and 545: references to EBITDAR

9. Thirdly, in response to questions 536 and 545, the transcript includes references to “EBITDAR”. These should instead refer to “EBITDA”.

10. Fourthly, in relation to question 537, I would like to clarify that my reference to “losing £35 million a year” was again on an EBITDA cash basis, as explained in my response to question 536.

Question 593: reference to Taveta

11. Fifthly, in relation to the response to question 593, I would like to clarify that Lord Grabiner’s reference to “Taveta” was intended to refer to “Arcadia Group Limited”.

12. I hope that the above information will assist the Committees in their ongoing inquiries.

Yours sincerely

Paul Budge

Arcadia Group Finance Director