HOUSE OF COMMONS

Liaison Committee

Oral evidence: Cross-government response to collapse of Carillion, HC 770

Wednesday 7 February 2018

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Watch the meeting

Members present: Dr Sarah Wollaston (Chair); Mr Clive Betts; Yvette Cooper; Frank Field; Robert Halfon; Meg Hillier; Mr Bernard Jenkin; Stephen McPartland; Nicky Morgan; Robert Neill; Rachel Reeves; Tom Tugendhat.

Questions 1-141

Witnesses

I: Sir Amyas Morse, Comptroller and Auditor General, National Audit Office.

II: Rt Hon David Lidington CBE MP, Minister for the Cabinet Office and Chancellor of the Duchy of Lancaster; John Manzoni, Chief Executive of the Civil Service and Permanent Secretary, Cabinet Office; and Gareth Rhys Williams, Government Chief Commercial Officer.

Written evidence from witnesses:

– [Add names of witnesses and hyperlink to submissions]

Examination of witnesses

Witnesses: Sir Amyas Morse, Comptroller and Auditor General, National Audit Office.

Chair: Welcome to this afternoon's session of the Liaison Committee on the collapse of Carillion. We are delighted to have you here, Sir Amyas Morse. As you will know, there are several Select Committee inquiries—both PACAC and PAC are conducting hearings, as are the BEIS and Work and Pensions Committees.

This issue has many implications for the work of several Select Committees, so we are delighted to be able to question you on some of the wider implications on behalf of the public. Without further ado, I am going to hand over to Nicky Morgan, who chairs the Treasury Committee.

Q1 **Nicky Morgan:** Good afternoon, Sir Amyas. I want to start by asking you about the Government's procurement policy, which requires the elimination of potential providers that pose an "unacceptable risk to business and/or public money". In the light of what has happened at Carillion and concerns around Capita, do you think that the policy is being applied properly?

Sir Amyas Morse: What I would say is that I think we would be having a much, much more serious debate if the Government had actually stepped in to support continued trading activity. If that had happened, I think we would be talking about serious long-term consequences for the idea of contracting. There are very serious issues contained in the current circumstances, but the fact that the Government took a view, which was a firm view at the end of the day, is probably positive.

However, I would also say that we need to recognise that the events that have happened have put us in a position where there is a real risk of private sector contracting partners that partner with the public sector falling into disrepute. There is no point in pretending that is not true. Whatever the rights and wrongs, the Government have a responsibility to take a grip of that. They have developed their approach. They need to develop it further if they do not want to find that it is more and more difficult to continue down this path. The scale is very great, so it would be a very big move to say, "We want to stop being involved in this private sector partnering." It is up to you to decide whether you think it is practical, but it would certainly be a very, very large change, and it would involve a huge commitment for the public sector.

The question is: under what terms can it happen in a way the public feels comfortable about? I think that means more insurance against things going wrong. Simply taking a sturdy view that, "Well, it's a private company; let it go down," gets difficult when they are such major contractors with such a major position in Government.

Q2 **Nicky Morgan:** I don't disagree with you that there is absolutely a role for the private sector, outsourcing and everything else, but I suppose the questions in this case—the lessons for the future—are about how early the signs of financial distress were spotted, and whether the rules that Government apply to guard the taxpayer against having to pick up large, unexpected bills, were working in this case.

Let us start with the first question: for how long was Carillion's financial distress obvious?

Sir Amyas Morse: What I know about Carillion is what I've been able to work out in a relatively short space of time; I have also had the benefit of reading the public evidence and the disclosures by Carillion. We will know more, of course, when the Financial Conduct Authority does its work, and it clearly thinks there is something to investigate.

Q3 **Frank Field:** Carillion directors did not know very much.

Sir Amyas Morse: I saw that. I am not suggesting they knew a lot; I am saying there is clearly a decision by both the Financial Conduct Authority and the Financial Reporting Council to examine all the disclosures that have been made.

I will just say that, as I have been going through the publicly available papers, I have looked at the very large write-downs that happened in early September and I know that they would have put Government on warning. I know Government were involved—started to be involved a long time before this—so they have clearly been very active. The question is, will we agree when we see all the circumstances? I am quite sure I will be looking at this from the point of view of the NAO. Will we agree that they were sufficiently robust sufficiently early?

Of course they didn't want the thing to fall over, so those are the questions we will need to understand when we look at it. It would be bit arbitrary for me to say, "I haven't actually looked at it in detail yet, but I'll just express a view anyway".

Q4 **Nicky Morgan:** This may be something else you cannot express a view on; perhaps it is again something for lessons learned for the future. Do you think that the business models of companies like Carillion and Capita, and similar companies—the issues they have been facing—now need to be reviewed? In the case of Carillion, it was very much reliance on debt finance and very little equity, combined with the largest asset in their balance sheet being goodwill. Is this sustainable if we are to continue with the private sector?

Sir Amyas Morse: I think that is a very good question and there other aspects of it as well in the business model. It is important to realise that a lot of construction companies fail each year. It may only be small ones, but the failures and insolvencies in construction run into the thousands per year. So it is probably fair to say that it is a sector that—setting aside Government—you read people talking about the sector; they say it needs to rethink itself quite deeply as to the margins it takes, the risks it seems to be prepared to take. So there is that.

The situation is also affected by the public procurement rules, which have certainly been understood by Government to mean that they can't intervene to shape the market as much as they might like. So you do tend to get over-concentration; I think that is fair to say. You also tend to get business models based on continued rapid growth. Of course, what has happened is that Government have stopped injecting more and more contracts into the system.

For a number of years, I think some of these companies were quite addicted to high growth and achieving sustained high growth by winning more and more contracts, and winning those contracts by relatively very keen margin pricing. That is the model that clearly needs to be thought about more strongly; when business is being given out, there needs to be more testing as to financial viability.

Some of the problems—I was interested to see the chief executive's own testimony; I think it was to you, Mr Field. It wasn't the most informative testimony I have ever seen, but in some of it, at least, they attributed the reasons for failure not really to dealing with Government; they were mostly to do with the middle east enterprise and long-term debt.

If you look back over the company for a number of years—I have done that—you see that they have grown by acquisition, and that very little of the growth has been by organic trading growth. They have also found themselves in a position where not much free cash flow has been generated; in fact, it has been getting less over the last few years. When you take out the product selling their capital interest in PFI undertakings, which were relatively quite profitable deals, it looks thinner even than it did before.

Q5 **Nicky Morgan:** Unfortunately, we are under very tight time constraints today, because of votes and everything. I have two final questions before I hand off to colleagues. Moving away from the specific companies, the NAO report to the Treasury Committee in October 2013 highlighted optimism bias. You talked about when business is being given out and financial viability. Do you also think that there is an optimism bias in the way that contracts are awarded?

Sir Amyas Morse: We have already had the conversation about the business model: the business model tends to be inherently aggressive. When all the drains have been pulled up on Carillion we will see some pretty aggressive accounting practices, too. This is an area where accounting and profit recognition is fuzzier than in many other parts of accounting. There can be a tendency to rob the later contracts to make the performance look better. Whether that will be true in this case, I will be very interested to see.

Q6 **Nicky Morgan:** Finally, one of the key motivations behind PFI is that the associated debt stays off the public sector balance sheet. Given what has happened in Carillion, and perhaps in other cases, do you think that in the case of vital public services—we will hear in particular about local government, schools and hospitals—the risk is really transferred in that way?

Sir Amyas Morse: If you look at where the burden of this failure lies—you may be surprised by what I am going to say—a lot of the penalty for the failure of Carillion has fallen where it ought to fall, which is on the shareholders and the banks that took the risk.

Of course, there are other penalties that have fallen on others; in particular, I want to quickly mention the subcontractors. Subcontractors have had more and more credit taken from them over the last few years. It is greatly to the Government's credit that they have encouraged bank facilities to be made available, but that is not the same as taking the debt away from these subcontractors. They really have been landed in it. They have had more and more credit taken. Now the contracts are passed over to someone else and I doubt they will want to pay all those payments that have already been invoiced by Carillion. It is very serious. These businesses subcontract a very large amount of their activity; they have a massive push-on effect on the rest of the economy.

Q7 **Frank Field:** I thought that what you just said was revolutionary. I grew up in a Parliament where we were all in favour of PFIs. The selling point was that the market would give the contracts to the person who would make the least profit. You are suggesting that there was a danger in that, aren't you?

Sir Amyas Morse: There can be danger when you have a sector that is extremely thin. You can get into a hamster wheel effect, where you are always taking on new contracts. By recognising initial profit on them you just keep going; then you get another new contract. What you don't see is whether the underlying profitability of these contracts really justifies your business. That is a real issue.

The reason why I boringly mentioned cash flow earlier is that if your cash never really comes in, that may be a sign that you need to look about how you have been accounting for these businesses. In the end, you should get cash for a business that you are successfully running.

Q8 **Frank Field:** Even if the financial directors were saying, "We should expand in this way," surely it is the job of the non-executive directors to say, "What is the profit margin?" on every one of those contracts.

Sir Amyas Morse: Yes.

Q9 **Frank Field:** If they don't do that, what else are they there for?

Sir Amyas Morse: They may ask those questions. I was interestedly reading the minutes of the last audit committee held at Carillion, as far as I know. It did seem to me that the non-executive directors asked a lot of the right questions, but they did not seem to be much the wiser at the end of it. I am not sure they were given very clear information. Non-execs can do what they are able to do if they have the right information. If they don't have the information, where do they go from there?

Q10 **Frank Field:** On local authorities, the Birkenhead constituency is within the Wirral—and like most local authorities, is really struggling to balance the books with all these cuts. Have you managed to undertake a risk register of those authorities who, like Wirral, have got all these problems and are now going to face new uncertainties because of Carillion's behaviour in going under, please?

Sir Amyas Morse: I haven't done that yet. But as I look at what we're going to do work on, that is certainly one of the list of things that we want to look at and see where the impact lies. That is one. The other thing I am worried about, frankly, which directly bears on your portfolio, is that as I was preparing for this I looked at a number of other companies and I was startled by the number of them that seemed to have substantial pension deficits. I think it might be worthwhile having a wider look.

Q11 **Frank Field:** Before I hand back to the Chair, you said "the losers"—but there were other losers, called workers and pensioners.

Sir Amyas Morse: That is right. I could have given you—I have a list and I am interested in following the impact on everyone. The public sector as a whole, what does it cost them, what does it cost people who were employed—there will be a significant number of Carillion people who have been made redundant, that's true.

What we will try to do is draw together what the overall cost has been. But I don't want to suggest, in the way I am talking about this, that I do not see that there has been a pretty effective effort from the Government in a number of areas, trying to be sure that they maintain services. They have actually tried pretty hard at that; they could have done a lot less. We will see how it pans out, but there has clearly been a pretty coherent effort there.

Q12 **Mr Jenkin:** In 2015-16, about £250 billion of public money was being spent on external suppliers, construction contracts and provision of services from private companies. We have just been talking about the inherent risk in the business model of about 25 strategic suppliers. How much is it the responsibility of people who are receiving bids from these companies that they understand the inherent risks in those companies?

Sir Amyas Morse: Certainly under the rules as they stand, there is an obligation to understand whether, when you award a contract, the person is a credible counterparty to carry out the contract. That is provided within the rules. But we do need to recognise that the rules mandated throughout Europe by the EU on public sector contracting are that there are certain considerations that you can't bring to bear in including or excluding a bid. You can't look at the number of other pieces of similar business.

There are a number of things that you cannot do that are designed to make it open to competitive bidding, but nonetheless they have the effect that it is possible for the sector to get too much concentration in too few hands, in my view. I think that is something that the Government need to recognise: notwithstanding that that is what the rules say, to leave it like that does lay us open to what can be quite vulnerable concentrations.

Q13 **Mr Jenkin:** We might be shot of some of those rules shortly.

Sir Amyas Morse: I sensed you might say that.

Q14 **Mr Jenkin:** I thought you were tempting me to say it. The urgent question, though, is how well are the Government as a whole assessing the aggregate risk they are holding in these contracts?

Sir Amyas Morse: I think they could do more. I think they are progressing, but they could do more.

Q15 **Mr Jenkin:** How should they do that?

Sir Amyas Morse: I think they need to understand—we need to have a frank discussion about what the real nature of the risk is. As I said earlier, not all the risk lies with Government. If you have shareholders and banks involved, they are taking their end of the risk. You need to understand what the public sector risk actually is. In this case, it is quite likely that the Government's intervention will cost—I think this is the latest estimate of what they are planning on doing—something around £300 million thereby. It is a serious number, but not a monstrous number.

Q16 **Mr Jenkin:** Do we know what the total value of the Carillion contracts was across the public sector?

Sir Amyas Morse: If I am not able to reel it off to you, it is not because it is not there. We do know that.

Q17 **Mr Jenkin:** So we know it for all 27 strategic suppliers?

Sir Amyas Morse: We could do.

Q18 **Mr Jenkin:** But is that not something the Government should have as a matter of routine?

Sir Amyas Morse: Yes, I would think so.

Q19 **Mr Jenkin:** Then how should they evaluate the risk associated with each company?

Sir Amyas Morse: Well, it has not been helpful when they evaluate associated risk with companies and they say that they are high risk. There have been one or two instances of legal action following that. They need to be able to exercise their judgment freely, in my view. I think it is important for them to be supported in doing that.

Q20 **Mr Jenkin:** Given the disruptive effect that this failure is having across the sector and the alarm that it is causing, and therefore the vulnerability of those other companies, had we not better get a handle on that pretty quickly?

Sir Amyas Morse: I agree with that.

Q21 **Meg Hillier:** Sir Amyas, in the history of the National Audit Office or in your time—whichever you can comment on—has the NAO ever leaked or inadvertently released commercially sensitive information held by Government?

Sir Amyas Morse: No, we never have. On the other hand, we have also sometimes felt that things that were being argued to be commercially sensitive actually were not quite as sensitive as they were being cracked up to be. In those circumstances, we have had an open debate on the table, so to speak. At the end of the day, I am entitled to have Government information disclosed to me and it is ultimately my decision, which I have to exercise accountably and discreetly, but none the less it is my decision.

Q22 **Meg Hillier:** Do you have any examples of information where you have had that discussion and then released it?

Sir Amyas Morse: Absolutely—and we try to be sensitive and responsive when there is real risk.

Q23 **Meg Hillier:** Can you give us an example? I have put you on the spot there a bit.

Sir Amyas Morse: It is quite difficult to give you a good example. I will give you an example of delaying. I decided not to publish a report on Southeastern railways for a period of time, because there was a sensitive negotiation going on and I thought that bringing it out would be deeply disruptive. I was convinced of the fact that I thought that was fair. I do not have any regret about that. There are things like that, which can come out. If the case is made, we are all responsive to it.

Q24 **Mr Jenkin:** I had it drawn to my attention that UK Export Finance was actually providing credit to Carillion to fund one or two of its contracts in the middle east. We might think that these are purely commercial contracts that have no consequences for public sector liability, but it turns out they do. Is that something you were aware of?

Sir Amyas Morse: I was not aware of it, but I am aware that when UK Export Finance provides cover, it does charge a premium.

Mr Jenkin: Some $110 million in 2015, another $180 million in 2017.

Sir Amyas Morse: Sure, but they actually do charge a premium for doing that across their books, so it is not provided for nothing.

Mr Jenkin: But it is still public sector money at risk.

Sir Amyas Morse: I am just being accurate.

Mr Jenkin: Kier Group got £450 million. There are plenty of other construction companies that have that exposure for putting the public sector—

Sir Amyas Morse: And they have all clearly made assumptions about a market, which is quite dependent on the oil price, and got caught out.

Q25 **Chair:** Are there any further points you would like to make before you leave today?

Sir Amyas Morse: I think that is fine. Thank you very much, Chair.

Q26 **Chair:** Thank you very much. Do any colleagues have other points?

Mr Jenkin: It is just about the urgency of getting this data and being able to make intelligent decisions about it.

Robert Halfon: They have not had the discussion with us. Do you not think that the Government need to move to a new system, in terms of small is beautiful, rather than have these giant contracts, even if many of them are subcontracted, so that when they fail, things go completely haywire? It is the same with IT contracts. You just have a few companies with the majority of IT contracts. Whatever it may be, things should be broken down much more.

Sir Amyas Morse: I have seen an example of that that did not work out all that fantastically in the digital area. I am not sure there is a particular solution. What I do believe is this. I think Government is stepping up more and more to what I believe are its responsibilities as such a huge actor in the market place. It is getting better skills, it is getting better at intervening and I do not think the record on Carillion in many ways does it credit.

I think it needs to go further and become more confident and assertive in what it does in forming the market. I have already said that. Sometimes that will be better by having smaller and less concentrated risk. I would prefer to see that but the logic will be different in different industrial areas.

I think when you are dealing with very large contracting, maybe there should be a minimum size you need to be to be a credible prime contractor. I don't feel as if I can legislate for that but I would like to see them being more self-confident in the way they press forward. If I can be allowed to repeat myself, we are actually at quite a critical juncture in terms of the reputation of this way of delivering public services and we need to make some progress pretty quickly.

Chair: Thank you very much.

Examination of Witnesses

Witnesses: Rt Hon David Lidington CBE MP, Minister for the Cabinet Office and Chancellor of the Duchy of Lancaster; John Manzoni, Chief Executive of the Civil Service and Permanent Secretary, Cabinet Office; and Gareth Rhys Williams, Government Chief Commercial Officer.

Chair: Welcome. Thank you very much for coming to this session on the collapse of Carillion and the wider implications. I am going to start with Meg and a slightly different aspect, if that is all right.

Q27 **Meg Hillier:** Minister, as you know, we have been in correspondence about the release of the papers relating to Carillion, as passed by the House two weeks ago now. Will you undertake now to release those papers to the Public Accounts Committee before recess?

Mr Lidington: As I have said to Ms Hillier previously, Chair, we will certainly comply with the terms of the resolution passed by the House. I saw Ms Hillier's latest response to me shortly before coming into this session and I have already given instructions that, as soon as we get the request from the NAO for unredacted copies of all the documents concerned, we will release those to the NAO. I am then happy to discuss further with Ms Hillier precisely how members of the Committee have access to those. Clearly, the CAG will be able to advise the Public Accounts Committee on their judgment about the confidentiality and sensitivity of some of the information contained in the documents.

Q28 **Meg Hillier:** Minister, as you know the Humble Address urged the Government to release the papers to the Public Accounts Committee. Although we will seek advice and support from the National Audit Office, we do also need to see them ourselves. From what you have said, it sounds like you are going back to some correspondence we had earlier about possibly not wanting the Committee to have full access to those papers. Can you clarify what you said?

Mr Lidington: I would like to understand, from a discussion with Ms Hillier, exactly what the process would be that the PAC would seek in terms of having the documents, how they would be inspected, where they would be inspected—

Q29 **Meg Hillier:** With respect, Minister, we went through this at a meeting. I do not want to bore the Committee with the procedures but it is quite a well-worn route now for Select Committees to receive information, for it to be held securely. Are you saying that you do not respect the will of Parliament? As you are a former Leader of the House I doubt that—I hope. Are you saying you do not trust the members of the Public Accounts Committee?

Mr Lidington: Ms Hillier knows me well enough not to think that, but the concern that I have is that some of the information that is contained within documents—not those referring to Carillion; the documents referring to Carillion we have released and I hope the Committee will have by now received them, with redactions only in respect of the names of junior officials, in accordance with normal practice. What I have to be alive to is the risk that if some of the information in these documents, which is acutely commercially sensitive, were even inadvertently released into the public domain, then there could be very serious consequences for jobs, people working for some of those companies and investors in those companies, as well as possible legal risks to whoever had been responsible for even an inadvertent leak of it outside the proceedings of the House.

I also have to bear in mind the question of the fact that we carry a risk in Government that if there is a belief that information given by suppliers to us in confidence risks being put into the public domain then those suppliers become much less willing to share that information with us subsequently.

Meg Hillier: But Minister—

Mr Lidington: Can I just conclude? I want to emphasise that I am going to comply with the will of the House. I think the discussion that Ms Hillier and I need to have is about the precise means.

Q30 **Meg Hillier:** Minister, I would just say, though, that the Public Accounts Committee is not public. It would then be for us to discuss and consider what could be put in the public domain; and the Comptroller and Auditor General just now confirmed that the National Audit Office has never revealed commercially sensitive information, but it has had discussions with Government about whether what the Government considers is commercially sensitive is in fact commercially sensitive. So once we have received the information, which I hope will be very soon, we would, as I have said to you in letters, have that discussion. We are not a reckless Committee. We are responsible. Where people's jobs and livelihoods are concerned we have that, of course, in our minds; but it is important, as I am sure the Chair would agree, that the Government complies with the will of the House. I would remind you, Minister, humbly, that the Government did not oppose the Humble Address or seek a vote to amend it.

Mr Lidington: I too would welcome the understanding from the Comptroller and Auditor General of his view as to the degree of confidentiality that would need to be respected.

Chair: Are you happy with that conclusion?

Meg Hillier: I think we still need to have further discussions, Madam Chair. We will continue to do that, but I am heartened that the Minister has moved further forward than in his most recent letter to me, so I thank him for that.

Chair: And it is something we could return to at a later date. I will pass over to Nicky.

Q31 **Nicky Morgan:** Thank you Chair, and good evening to the panel. I know that time is tight, so although questions are probably directed at the Minister if others are better placed to answer them I am sure they will want to chip in. I want to start with looking at the total costs to the taxpayer of the Carillion collapse, realising that perhaps it is not possible to have definitive numbers—but latest estimates would be welcome. The figure of £600 million has been reported. That is separate from the pension deficit figure. Is that the right order of magnitude?

Mr Lidington: I will ask Mr Manzoni and Mr Rhys Williams to comment after I have spoken. What the Committee will see if they have not already is that a supplementary estimate has been laid before the House today, which provides £150 million to support the work of the official receiver. It is not a definite cost to the public purse as a consequence of Carillion's failure. What it is is the wherewithal, the working capital for the official receiver to go about his duties. Clearly what any net figure will be depends in significant measure on the price that the official receiver is able to obtain from some of the contracts that he will be looking to dispose of to other companies. Whereas Carillion overall has gone into liquidation, there are some elements of that business that certainly would seem to be viable, and where there would be going concerns that could be transferred for a price. John, do you have anything to add?

John Manzoni: I have very little to add. I do not recognise the £600 million. I do recognise the £150 million. As the Minister said, it is a working capital number, which is a gross number that will be offset by proceeds through the process. That is where we are. It is a little bit early to tell, because we are only a little bit into the process.

Q32 **Nicky Morgan:** On 15 January a minute was laid in the House notifying of a contingent liability. Is the supplementary estimate an update on that contingent liability?

Mr Lidington: Yes.

Q33 **Nicky Morgan:** Okay. The other point we explored with Sir Amyas was about subcontractors and people stepping in on joint ventures. How much compensation are joint venture partners getting for bearing additional risk and responsibility?

John Manzoni: From 15 January on, in the public sector, we have undertaken to maintain public sector services, and we have paid direct Carillion employees and are paying them until they can get switched through. Unfortunately, to the extent that subcontractors to Carillion were owed money on 15 January, in law they become unsecured creditors, the same as everybody else in this situation. That is not a good situation, and it is to do with how Carillion was working with its subcontractors.

Q34 **Nicky Morgan:** But there is no cost to the taxpayer of subcontractors, and there is no cost to the taxpayer, over and above this £150 million, of having to support joint venture partners, some of them smaller than Carillion, who have had to step up to the plate.

Mr Lidington: Clearly it will depend on the exact terms of the joint venture, but in general the joint venture has entered into a contract for a fixed price. For example, in the case of the HS2 contract, the remaining partners have had to step forward, as was their contractual obligation, and take it up at that price.

Gareth Rhys Williams: Just to add to what the Minister is saying, where a joint venture partner has said—and they all have done—they will take over, as they were contracted to do, the stake that was previously owned by Carillion and is now owned by the official receiver, the contracts of those joint venture agreements have formulas in them that determine the price of Carillion’s share, or of the joint venture partner’s share had they gone bust. The official receiver will actually be receiving money from the joint venture partner buying out that joint venture share. That talks to what John was saying. That defrays the cost that the official receiver is having to expend in running this process.

Q35 **Chair:** Many people I have spoken to have been concerned about the sheer complexity of Carillion and the impact of that on trying to get hold of information, because it is held by so many different sources. Are you going to publish a list of the 450-odd contractors and Government Departments that contracted with Carillion so they are all available in one place and people can fully assess the impact of Carillion’s failure by looking at one source?

Mr Lidington: Broadly speaking, at the time of the liquidation, there were about 450 UK public sector contracts with Carillion group companies. Of those, roughly 150 were from different branches of central Government and the other 300 were from local government, local NHS trusts and so on. I am perfectly happy to send this Committee as comprehensive a list of such contracts as we have available. What the official receiver is saying to us is that he is finding some difficulty in getting hold of management information in the form that he would have wanted to see.

Q36 **Chair:** That’s right. It would be useful for the public to be able to see that as well—for it all to be available in one place. It would be helpful to have not just the values but the implications in terms of public service delivery.

Mr Lidington: We can do our best on that, particularly as regards the central Government contracts. Obviously, when it comes to one placed, for example, by a local authority, it is very much that local authority that will take the decision about whether it wants to seek another contractor or to go about things in a different way.

John Manzoni: Yes, the official receiver will take a view, as is his or her right, I think. They are in commercial negotiations with some of the—where it is not central Government, it is an SPV. The SPV is the owner of the contract with Carillion, not the public sector. So, subject to limitations, we will provide—

Q37 **Chair:** Of course. I understand there would be limitations, but the criticism has been that it is very difficult for people to see the extent of this, because it is held by so many different sources, so that would be helpful. Thank you for that commitment.

Moving forward, what is going to change, or what needs to change, about the transparency of these contracts?

Mr Lidington: Of course, Government contracts above a given value are already routinely put into the public domain: they are published on the relevant Department’s website. On the lessons I think we need to draw from this, we are at the start of a process now, and our conclusions are clearly going to be informed by the various investigations now taking place, including by some of the Select Committees of the House, but particularly by the official receiver’s conclusions. I do not want to say anything that might prejudice decisions that the official receiver would take, but they will come to conclusions about how Carillion managed its business.

We in Government have started—and we certainly need—to look at lessons we might want to learn in terms of how we go about contracting with companies. We already have, for example, a system—I think the new law came in in 2011—whereby broader social considerations are taken into account alongside pure value for money. That is one aspect worth looking at again. Another is whether we want to revisit the question of seeking best value for money by getting large contractors in to manage wide-ranging, complex projects. That inevitably means that you have a limited number of potential contractors globally, as well as in this country.

The downside—the other thing that has to be weighed in the balance there—is that if a Government Department were to decide that it wanted to let a smaller number of different contracts, that would mean more in-house resource and expertise, so not just any old generalists, in the procurement and management of contracts will be needed within Government Departments to manage a larger range of contracts. You would be transferring less risk out to the private sector partner.

The experts are sitting beside me. Gareth, do you want add anything?

Gareth Rhys Williams: That is exactly right. Listening to what Sir Amyas was saying, in the IT area, which is not what Carillion was involved with, we have been disaggregating those contracts, and that has involved bringing several thousands of IT people and additional procurement people into the public sector in order to consider buying from several tier 2s instead of one tier 1. We need to really think about this; this has exposed something we need to think about. Over the last couple of years—I was brought in by John to build up a commercial capability, and if Ministers want to take that extra step, we need to go further in terms of how many people we have got who have got the skills to do that sort of work. It is something we should definitely think about.

Q38 **Tom Tugendhat:** Can I quickly come in here? My experience of prime contracting is somewhat limited in that the only places I really saw it operating were Iraq and Afghanistan. It was perfectly obvious after not very long that the prime contract may be for, say, $1 million—in fact, it was usually for something in the order of $100 million, but by the time the execution got to the ground you were talking about multiples of single-digit of millions of dollars, and often less. Effectively, the United States Government was transferring risk. There is a danger here that what we have done is somewhat different. Indeed, with Carillion, we have transferred risk from the open, public state shoulders on to unrevealed private shoulders, which has just meant that we have kept the risk anyway.

I am interested by what Mr Williams is talking about, because if indeed you can bring some of this management expertise back in-house, you are not actually transferring cost; all you are doing is managing risk in a different way. You are allowing individual failures not to be systemic failures, because you are maintaining the oversight at a public level, in-house, as it were, with the Government, and therefore allowing companies to do what they should be doing—to experiment, succeed and indeed fail and go bust—while the Government maintains the oversight it should, rather than transferring that.

Mr Lidington: I will ask Gareth and John to comment in more detail on Mr Tugendhat's question, but I just wanted to make two brief points. First, it is important to put on to the record that Carillion's failure did not come about as a result of its UK public service contracts. The public service contracts were profitable. There were concerns about one or two of the construction contracts, but it got into trouble—

Q39 **Tom Tugendhat:** Funnily enough, I was not thinking specifically about Carillion. I was actually thinking about companies like Stagecoach and Virgin. There are many examples where Her Majesty's Government, for understandable reasons, has decided that it is easier to contract one large role than many small ones, for exactly the reason that Mr Williams stated. But actually all that it is doing is agreeing either morally or legally to underwrite a private sector risk. The reality is that if major company X does not deliver prisons, rail or whatever it is, we are not going to stop doing it. We will have to do it anyway.

John Manzoni: The question of the transfer of risk, the appropriate pricing of that risk and where it sits is very important and complex. It is certainly true that in some sectors in the past decade—this sector is one of them, in fact it is probably the worst—we have seen a growth of these companies. They have spread, so they do not really have particular areas of expertise—

Q40 **Tom Tugendhat:** Or competition.

John Manzoni: They have competition, but not expertise, other than perhaps winning the bid. We do need to re-examine that issue, but in order to re-examine it and have an intelligent conversation we have to have enough expertise in-house to be able to do so. That is something we have been building over the past two or three years under Gareth and his team, specifically so that we can get better at this.

Q41 **Chair:** Following on from that, do you think there is a risk that you lose that in-house expertise? When or if a company fails, it can have very serious consequences. In the health service, for example, some concerns have been expressed about Capita. Look at the sheer extent to which primary care has been reliant on and, by all accounts, not getting a particularly good service from it. If it were to fail, that would have consequences right across the delivery of primary care.

John Manzoni: I am passionate about rebuilding the appropriate levels of expertise back into the Government. That is what I am here for. That is what I am trying to do, with Gareth and his commercial team in this instance, but there are others—the technical, the finance, the legal, the property. We are on that journey. I am not saying that it is finished, but we beginning that in this sector. The same is true of Capita. We are actually engaging with Capita in a very different conversation about their total business across Government—where they have expertise and where they haven't—to the extent that we can begin to understand where they should be competing and where, frankly, they are just bidding for work.

Tom Tugendhat: Sometimes the expertise is in the bidding.

Meg Hillier: The Public Accounts Committee has highlighted that quite often.

Q42 **Nicky Morgan:** We have had an interesting philosophical discussion about the involvement of the private sector. There will be differing views, but it is right to look at what has happened with Carillion and to ask ourselves the questions. Assuming that we do very much believe in outsourcing and the involvement of the private sector, one of the other things that has to apply are the financial tests to the companies with which the Government are contracting.

Carillion issued profit warnings in July and September. Its debt was piling up. It was making losses on key contracts and writing off £800 million, while its annual profits were a tenth of that, and it had a pension deficit of £587 million. Yet it was still being awarded contracts. The Government's procurement policy requires Departments to "eliminate from a procurement any potential provider whose current financial capacity would pose an unacceptable risk to business and/or public money." I am not sure who is most suited, but could somebody talk us through how the financial tests were being applied in this case over the past nine months?

Gareth Rhys Williams: I apologise to the Minister and his colleagues for not having the data at my fingertips when this first came up, but of the seven or so contracts that were let or announced after the first profit warning, two had already been awarded by us. The company had chosen not to announce that—that is its call. There are two very large ones that everyone should rightly focus on—the two HS2 contracts that were awarded a week after the first profit warning.

To respond to your question, the financial tests are related to turnover, whether the company is large enough to execute a project of that sort of size and, typically, whether they have had turnover twice the size of the contract in question. In this case, the hurdle that HS2 set was three times. Carillion passed that. There is then an assets test, which is designed to probe whether the company can afford to run the contract. That was set at 0.75 times that of the peak contract value.

It is important to remember that those two HS2 contracts were let to a consortium, of which Carillion was a third part, and the tests were run both against the consortium and the individual members. When that first evaluation was done, which was several months beforehand—there was a purdah period as well—the consortium and the individual members all passed.

When the profit warning came out, colleagues at HS2 and DFT re-ran those tests in the light of the new information, and the businesses—the consortium and the individual members—still passed. DFT went further, which I think was good practice, and called in the other consortium members and asked, in the light of the new information that is now in the market, which none of us had a week before, were they still prepared to enter into a joint venture with Carillion. They all said yes, and they signed up to the joint and several liability clauses in the contract.

Rolling forward six months, Carillion unfortunately did go bust. That day is slightly imprinted on my memory. The Kier announcement was at 8.27 in the morning, saying that they were taking over their half of the Carillion work; indeed, they have taken Carillion employees on to their books.

In this case, I think the mechanism has worked, and we have got through what is an unexpected calamity with this business. The financial tests work. We are not looking at profitability or returns to shareholders. That is a matter for shareholders. We are looking at whether a potential counterparty can deliver the work that we want it to do in a way that is robust and within a margin of error.

Q43 **Nicky Morgan:** It has worked, but at a cost, so far, of £150 million to the taxpayer. I hear that could be—Mr Manzoni, you are frowning at me—less or more, depending on what new information comes to light. As Carillion's largest contractor, were you aware of dangers before the first profit warnings?

Gareth Rhys Williams: I will defer to the Minister, but when various people see some of the things on our risk register—I think the NAO has already seen them—I think you will hopefully take some comfort in the way those risk registers were moving forwards. Is it fair to wait until you see that stuff?

John Manzoni: The answer to your question is that Gareth and his team are in constant dialogue with all the strategic suppliers across Government; there is a list of 27 of them, or thereabouts. I think it is true to say that the market was clearly was very surprised by the £800 million profit warning on 10 July. We are not inside these companies or managing these companies, so we certainly—

Q44 **Nicky Morgan:** Were you as surprised as the market?

John Manzoni: I wasn't there on the day. I think the answer is yes. We had 25 meetings with the company from 10 July to 15 January, so we certainly stepped up our engagement with it. I think it is also true to say that the company was surprised and continues to be surprised.

Q45 **Nicky Morgan:** I have one final question, about subcontracting. As you said before, Mr Manzoni, some of the subcontractors, which can be very small companies, are now unsecured creditors. Of course, they can be quite financially damaged by what happens to a large company, like Carillion, that they are contracting with. What analysis has been done of the impact if some of the subcontractors cannot carry on servicing the contracts? What happens if, heaven forbid, some of them have to go out of business?

Mr Lidington: The Business Secretary convened a meeting on the day Carillion collapsed and met the various trade bodies representing those who were most likely to be in the subcontractor chain. He has now chaired four meetings of a dedicated Government taskforce designed to give some support to subcontractors.

I will be plain with the Committee: I am not talking here about the Government using taxpayers' money to bail out those subcontractors. It is partly about ensuring that advice from the various Government business advisory services is being properly targeted at subcontractors in difficulty, so that they know how they can access that. Mr Clark and his team have also persuaded the banks to put together up to about £1 billion of support in the form of loans, credit and other financial support to affected businesses, and HMRC is giving affected businesses a grace period rather than expecting them to pay immediate tax bills.

Q46 **Mr Jenkin:** The Committee I chair, the Public Administration and Constitutional Affairs Committee, working together with the Public Accounts Committee, will look at the longer-term lessons. I am rather more concerned about the here and now and about what is happening. The Government have committed £150 million to support the work of the official receiver. Does that include the money going to support the subcontractors, or is that separate money?

Mr Lidington: The up to £1 billion I mentioned is coming from the commercial sector. That is banks. What you have is the British Business Bank using its own support scheme to guarantee loans. It is loans.

Q47 **Mr Jenkin:** So this £150 million committed by the Treasury so far is to support the working capital of the public service contracts and the PFI contracts. Is that correct? Was there an approval limit to that contingent liability?

John Manzoni: It was agreed by the Chancellor before it was committed.

Q48 **Mr Jenkin:** What was the approval limit?

John Manzoni: He approved £150 million.

Q49 **Mr Jenkin:** What this means—you know what I am going to say—is that, morally speaking, the taxpayer has taken charge of those contracts. The taxpayer has, through the official receiver, basically taken ownership of the contracts, but, Minister, you have just told us that the contracts may be sold off to other companies. Why is that in the public interest?

Mr Lidington: What is in the public interest is, first of all, to maintain the service contracts. Construction contracts one can look at in a different category. We are paying for two things there. We are paying for the ongoing costs of service provision, with the money being routed via the official receiver rather than via Carillion. It is not the case that Carillion has walked away with a payment for service provision that was never actually provided. Secondly, we are supporting the administrative and legal costs of the official receiver. Our judgment was that, compared with the counter-factual, which was a liquidation proceeding in an unplanned fashion, it was not only a way of ensuring continuity of service provision but would end up being much less of a burden on the taxpayer than the sum that we are talking about potentially being liable for as far as the OR is concerned.

Q50 **Mr Jenkin:** But supposing a private company had come along to offer the receiver £150 million. What would it have got in return?

John Manzoni: I'm sorry—say that again.

Q51 **Mr Jenkin:** Supposing a private company had offered £150 million to the receiver for all the contracts. What would the receiver have done?

John Manzoni: That is exactly the process that is going on now. As of right now, the official receiver is busy trying to substitute new providers for Carillion, where Carillion was either running a construction site or not. I think our previous conversations indicate that the question is why we would not take back the PFI.

Q52 **Mr Jenkin:** Not just the PFI, but let's deal with the PFIs first.

John Manzoni: I do not think today is the place to rehearse the detail of PFI in principle, which I know there is another Committee to do, but in fact, they are structured, contractually, in order to create a number that is certain for the public sector. The contractual structure of these SPVs and PFIs effectively means that the public sector pays a fixed price for whatever it is that that PFI was doing. They are done through SPVs, so if it fails, the first people who get to have a shot at doing something else are the private lenders to that SPV. The reason they are structured that way is because the private sector takes all the risk, and there has been quite a lot of risk in this—they have lost a lot of money. The PFI structure is contractually a very complex structure, but essentially it results in the public sector being absolutely certain of the cost.

Q53 **Mr Jenkin:** Okay. How much of the £150 million is going to support PFI contracts?

John Manzoni: It isn't going to support PFI contracts.

Q54 **Mr Jenkin:** Okay, that's fine. So let us turn to the other contracts, which I think are a more obvious candidate, because a lot of these public service contracts—the school meals, the facilities management contracts—

John Manzoni: Mostly through PFIs.

Q55 **Mr Jenkin:** Are they all through PFIs? Actually, quite a lot of public contracts—

Gareth Rhys Williams: There are three parts to Carillion's businesses: the buildings business, the infrastructure business—rails and roads—and then there are the service contracts, and they are predominantly PFI. The service contracts are buried within PFI contracts. There are two salient examples that are not that, but that central Government are directly contracting: a relatively small one with the British Museum and another large one with the Ministry of Justice for the provision of facilities management services for prisons.

Q56 **Mr Jenkin:** Earlier, we were talking about the vulnerability of the sector and the thinness of this almost non-market, where there are so few bidders in some fields that there is hardly a market to bid into—it is a curious kind of negotiation. We are talking about the lack of in-house expertise in Government to assess and manage risk. Out of the ashes of Carillion, it would be possible to acquire quite a lot of these things, and it would be possible to create perhaps a new entity, perhaps an employee-owned entity, that could acquire some of these contracts and carry on managing them. I have made this proposal.

John Manzoni: You are right. The cost of that would be exactly the same as the cost of the original PFI, for the reason that I have just described. Contractually, we cannot get it cheap. Most of these activities are designed to be fixed-price for the public sector, so even if we decided to do that, we would need to pay the same price—this is a value deal. Your point about creating more diversity in the market is a good one, and there are conversations that we can have, for instance with the prison example, where we have time to organise and orchestrate that. But standing up a mutual, or an alternative thing, of course takes time: you have to have a management team, you have to find the finance for it, the management team has to be competent, and, by the way, it has to have a certain business to do. We can organise all of that for the public sector, but not instantaneously.

Gareth Rhys Williams: I think that is a very important point. In the large contract—the NOMS contract—that is coming back in, we are the customer directly.

Q57 **Mr Jenkin:** That is the prison one, is it?

Gareth Rhys Williams: Yes. Because the business—Carillion—has gone insolvent, the customers have the right to terminate these contracts. So the SPVs have the right to terminate a contract. Now, it will take them time to set—

Q58 **Mr Jenkin:** The customers have a right to terminate the contract with the SPVs?

Gareth Rhys Williams: No, the SPVs are the contract holder. The SPVs are contracted with Carillion. In Carillion's place is now the official receiver. So, to your point about mutuals—

Q59 **Mr Jenkin:** But who owns the goodwill in the SPVs—the receiver?

Gareth Rhys Williams: No, the SPVs are still free-standing entities; they are private sector businesses that have contracted with the hospital or—

Q60 **Mr Jenkin:** Yes, but who owns the SPVs?

Gareth Rhys Williams: They are banks, or private owners. The one in the Midland Met Hospital is a local enterprise in Birmingham. Setting up a mutual will take time, so there are two conflicting things here. We need to move these contracts on quickly, because the OR is not a long-term home for any business, and the ex-Carillion employees, who are doing a fantastic job of executing these services, will find other jobs with more permanent employers. The risk to public sector service provision is that over a period of time, unless we do something quickly, that will degrade, because people will inevitably leave. There is a trade-off to moving the businesses quickly from the OR to a new, permanent home—another contractor, ideally a regional one, so that service provision can continue. If we don't move it quickly, the SPV may well cancel the contract and substitute whoever they like. That is at no cost to the public purse.

On your point about setting up a mutual: that is a good idea and something that we should think about, but that is not a quick thing to do, because you need to guarantee the volume. The only place we can guarantee the volume is in that NOMS contract, because we hold the keys to that.

Q61 **Mr Jenkin:** How are we going to prevent a further consolidation in this sector, where the receiver is just selling off these SPVs and contracts to the names we know about—the usual suspects—so there is just one fewer company bidding in the sector? We would have an even bigger problem and the risk would be concentrated even further.

Mr Lidington: Don't forget that the official receiver has a legal duty to maximise the return to the creditors—

Mr Jenkin: The secured creditors.

Mr Lidington: The secured creditors. And the need to—

Mr Jenkin: One of whom is the taxpayer, by the way.

Mr Lidington: Yes, but that obligation on the part of the official receiver applies whether one is talking about a mutual or a plc.

Q62 **Mr Jenkin:** But if value is being realised, why isn't it being realised for the public good, the taxpayer and the benefit of these contracts?

John Manzoni: It is being realised because it will offset our £150 million that we have secured into the OR. They are directly offsetting those things. The complexity here is that all those SPVs, as we have just discussed, are private entities: there are a lot of them, they are all private and they all have different things.

Right now, the OR is trying to find a way of transferring that activity to a new provider where Carillion has failed. That is a conversation between the OR, the SPV, sometimes the customer to that SPV and, to some degree, the Government. We have an interest and we do not want an unsatisfactory sale by the receiver, who is legally bound to do what he or she is doing. We have quite a complex commercial structure from this point, to try to optimise the value and make sure that we do not unduly concentrate risk in some other bad provider.

Q63 **Mr Jenkin:** My final question is by what criteria should we judge the Government for where all these SPVs and contracts finish up? What does success look like?

Mr Lidington: I hate to use the word success because, with the best will in the world, we are talking about a situation in which decent workers—

Mr Jenkin: Okay, this is Dunkirk and not the D-day landings.

Mr Lidington: The Government interest—defining it in that way—is to ensure that public services continue to be provided, that public service construction projects resume as rapidly as possible after the pause to get new construction partners in place, and that that is done at the best possible value for money and the lowest net cost to the taxpayer. In summary, that is how I would look at this.

Gareth Rhys Williams: May I add one thought to what the Minister said, in terms of competition? The facilities management market is quite a competitive space—there are lots of people in that area. We have just launched a new FM framework that is designed to make it easier for us to access regional players. Although we should not try to reduce competition, it would be better if the OR sells it to someone new who does not have much business in that space.

The lack of competition that is talked about in the outsourcing market is more in what is called the business process outsourcing market, rather than in the FM market—facilities management, maintenance, cleaning and canteens—where we would love to have more competitors and we are trying hard to generate more competitors. The really thin markets are more in BPO than in FM.

Q64 **Mr Jenkin:** If individual management teams come forward and say, "We would like to bid for our bit of this, and we will put some financing together," will the Government give them some support?

John Manzoni: Of course—but they haven't yet.

Mr Jenkin: Of course we would! Put out a welcome mat, it might happen.

Q65 **Meg Hillier:** I think Mr Manzoni talked about PFI contracts being at a fixed level, so there wasn't a risk in that sense, but there is the option to vary your PFI and, once a variability clause is enacted, they invariably cost more, so I don't know if you want to think again about what you said. And is there a risk, in this situation, that there will be a demand for variation, because of throwing everything in the air, and therefore there will be an extra cost to the taxpayer when they are the client or—

John Manzoni: I don't think there is going to be a danger of extra costs to the taxpayer in this set of situations that we are working through one by one. I don't think there is going to be a danger.

Q66 **Meg Hillier:** There is no desire by Government at this point to vary contracts at all.

John Manzoni: No—partly because, as I think has been described, speed is somewhat of the essence here. People might try to open them up, but the OR will be keen to get this done quickly and cleanly.

Gareth Rhys Williams: The variations you refer to are when the requirement changes—we want an extra building to be built on the side, we need more beds, or more of this, that or the other—but that is not the issue here. The issue here is transferring it to a new provider.

Q67 **Meg Hillier:** But both could be true at the same time—we need a new provider, but you may need changes too, so there could be a cost.

Gareth Rhys Williams: Yes, but that is not related to the Carillion problem. That may be true on a local level, I don't know, but that sort of would have happened anyway, probably.

Q68 **Rachel Reeves:** I want to move on to the subject of the regulatory oversight at Carillion and who was supposed to be doing that. As you know, Minister, KPMG provided the audit for Carillion for its 19 years of existence. KPMG earned more than £13 million in audit fees over that time, and several million more pounds for non-audit work. How good a practice do you think it is, or do we need to look again at whether one company can provide audit services for such a long period?

Mr Lidington: Those are perfectly reasonable questions. I am going to be very cautious in what I say because, as Ms Reeves knows, the FRC is conducting an investigation into KPMG's performance. The FRC has various sanctions available to it and I don't want to say anything that could remotely be construed as prejudicial to the FRC's findings there. But I think those are reasonable questions, and once we have the FRC's verdict on what happened in this case, I would be wanting to take advice within Government on whether we needed to change arrangements.

Q69 **Rachel Reeves:** Would you also consider whether—a bit like the issue of whether enough firms bid for Government contracts—there are enough audit firms to bid for the audit work at these big companies? There are only four big audit firms, as you know. All of those big four earned substantial fees over the last 19 years from Carillion. The work just seemed to move between the four of them, and I am sure Carillion is not unique in that. Do you think, Minister, that there might be a case for breaking up the big four audit firms?

Mr Lidington: I would need to be persuaded by evidence on that point. It is not something that I will rush to a view on in this Committee sitting. John, did you want to—

John Manzoni: No, absolutely not.

Mr Lidington: I think even on a case as high-profile as Carillion, one would need to have compelling evidence to justify that. We have an independent Competition and Markets Authority, after all, and if it believes that the market has become a cartel in effect—there was some implication of that in Ms Reeves's question—then the CMA has powers to investigate and to take action.

Q70 **Rachel Reeves:** Let us go back to the Financial Reporting Council. After the collapse of BHS, both the FRC and the Business Select Committee pressed for tougher regulatory and enforcement powers covering the behaviour of company directors. The Government didn't take up those recommendations. Do you think it is now time to look at tougher regulation for company directors, Minister?

Mr Lidington: We should certainly be willing to have a look at it again. It will depend, I think, in large part on what the official receiver concludes about the conduct of the directors of Carillion.

Q71 **Rachel Reeves:** When we had the directors of Carillion, past and almost present, in front of our Select Committees yesterday, we questioned them about the changes in rules about the clawback of bonuses. Many of the people we had in front of us had earned big bonuses in the period leading up to the collapse of the business, but the company changed its own rules making it harder to claw back those bonuses.

One of the lessons from the global financial crisis was to have tougher rules about being able to claw back bonuses when things go wrong at a business. Do you think we need to look again at the clawback arrangements for bonuses, so that we can get some of that money back?

Mr Lidington: Again, sitting here today, I am open-minded on that, but there have been serious allegations of misconduct by the board and former board members of Carillion. Those are being independently investigated by the official receiver and it would be wrong for a Minister to make any comment that could be prejudicial of the official receiver's findings on that.

Q72 **Rachel Reeves:** The Financial Reporting Council said that, after the first profits warning in July last year, they were keeping a close eye on Carillion. When we had Steven Haddrill from the FRC in front of us it wasn't entirely clear what "keeping a close eye" meant.

The Pensions Regulator also said that they were keeping a close eye on Carillion because, as Nicky Morgan has already said, they had a pensions deficit of £587 million in their annual accounts published in March last year. It seems that that number is closer to £800 million or £900 million. Do you think that the Pensions Regulator need to have the power to issue higher levels of fines perhaps, if they find that companies are consistently failing to close the pensions deficit, or deferring payments that are promised into a pension scheme?

Mr Lidington: The Pensions Regulator already have significant powers if they have evidence to show that there has been a breach of legal duty by the trustees of a pension fund, or directors of a company. The Prime Minister has already said that the Government will be publishing proposals later this year—I think it will be sooner rather than later this year, this spring—to strengthen further the powers available to the Pensions Regulator.

Q73 **Rachel Reeves:** I am sure that they will be welcome.

Finally, let me ask about small businesses. This has been touched on previously but in our evidence session yesterday, the former directors at Carillion suggested that around 5% of subcontractors were being paid 120 days after work was complete, and 10% were being paid 60 days after the work was complete. Do you think that that is reasonable, Minister?

Mr Lidington: Again, I do not want to make any comment that is prejudicial of what the official receiver is investigating. The Government, in line with our manifesto, are going to publish a Green Paper, then a White Paper later this year to propose ways in which that particular problem can be addressed, and to try to give greater teeth to the prompt payment code. Ms Reeves makes an important point. We all want to see prompt payments, and the Government are doing their utmost to meet their very demanding target for prompt payments—trying to lead by example there. To some extent, we and others are dependent on the willingness of subcontractors to come forward and make a complaint.

John Manzoni: We have a prompt payment code, which is voluntary, that says, "You have got to pay within 30 days." At the moment it is a voluntary code, although each contract holder has to write into the contract that the payment to the subcontractors of the prime must be done within 30 days. Of course, it is then up to the contract holders; it is a very distributed system.

The question for us is: how do we, as a Government, step in and make sure that that—as the Minister says—has more teeth, because of course it is in everybody's interest that small companies down the chain are paid properly and promptly? There are lots of things that we are trying to do to do that. In the event that a prime contractor and its subcontractors reach some other agreement, there is of course little that can be done—unless you have some teeth—so that they sign up to our prompt payment code.

Q74 **Rachel Reeves:** The Federation of Small Businesses described Carillion as being notorious for being late payers, despite being signatories to the prompt payment code since 2013. Does the prompt payment code mean anything if a company can sign up to it but still not pay its subcontractors within the period of time that they have signed up to pay within?

John Manzoni: As I have said, first, the requirement is in the contract, so it is the contract holder that has to enforce the contract. It is a distributed system and that is oftentimes a private sector player. Secondly, I think this is an issue for which we are trying to find a way to put some more teeth into that prompt payment code.

Q75 **Rachel Reeves:** Minister, in your party's manifesto for the general election—I suspect all of us around the table support this point—it says that the Government will use their "buying power to ensure that big contractors comply with the Prompt Payment Code" on both Government and non-Government contracts. It also says: "If they do not do so, they will lose the right to bid for government contracts."

Is it your intention to ensure that companies that were not paying within that period of time, like Carillion, will in the future not be able to win Government work?

Mr Lidington: That is exactly the quote that I was alluding to a moment ago when I spoke about the Government's intentions to bring forward proposals this spring. The key issue is Mr Manzoni's point, which is how you try to deliver the outcome we all want to see down the supply chain, when you might be once or twice removed from the Government Department that let the contract to the main contractor in the first place.

Q76 **Rachel Reeves:** I guess that is the point I am really trying to get to. Did the Government take any action to ensure that Carillion were complying with the prompt payment code? The reason that is important is that, as Bernard Jenkin and others have already said, there will be some subcontractors that, through no fault of their own, will potentially miss out on four months' worth of payment because Carillion hadn't paid them for months leading up to its collapse. I wonder whether the Government were taking any action to ensure that Carillion were actually complying with the prompt payment code.

Mr Lidington: My understanding—I will ask Gareth to answer in more detail—is that Carillion wrote the code into their arrangements but then had a practice of sometimes offering to a subcontractor an enhanced payment, in return for that subcontractor being willing to defer the deadline for being paid.

Q77 **Rachel Reeves:** How can they say that they are a signatory to the prompt payment code if they weren't meeting the requirements of the prompt payment code? Does it mean anything?

John Manzoni: They were complying with the letter, not the spirit.

Mr Lidington: This is what we have to tackle in the forthcoming—

Q78 **Rachel Reeves:** Mr Manzoni, you said that the Government had 25 meetings with Carillion since July. In any of those meetings, did the Government discuss with Carillion the prompt payment code and payments to subcontractors? Did the Crown representative? I know that there wasn't one for Carillion for three months, but when there was one, were they discussing it?

John Manzoni: I will defer. I wasn't in the meetings; I was in the last few meetings.

Q79 **Rachel Reeves:** Did you discuss it in any of the meetings you were at?

John Manzoni: I was in meetings in which we discussed whether we were going to loan Carillion more money with Carillion's lenders. No, we did not discuss it in the meetings at which I was present.

Gareth Rhys Williams: Yes and yes. That was absolutely a matter that we talked about. We were acutely focused on the company's short-term cash flow and where that was going. I will just add something to the previous answer on the prompt payment code. I think John typifies it exactly: Carillion were complying with the letter. It was possible for vendors to be paid in 30 days, but they had to accept a discount to do that. That is what we have to try to tighten up, so that the spirit, not the letter, points us exactly—

Q80 **Rachel Reeves:** It seems to me that, to a subcontractor seeing that a company had signed up to the prompt payment code, it would not make a blind bit of difference.

Chair: I am very keen to bring Rob in next, because I know he has to leave.

Q81 **Robert Halfon:** Can I ask you, Minister, to give an update on what is happening in terms of the Carillion apprenticeships?

Mr Lidington: There are about 1,500 Carillion apprentices overall, mostly in England but a smaller number in Scotland. The Construction Industry Training Board has stepped forward to act as the apprenticeship provider for all those in England, and has been working with the equivalent organisation in Scotland to ensure that it can step in there. The challenge has been to find new employers to allow those apprentices to continue the completion of their course and work. So far—this information was correct as of yesterday—638 apprentices, that is 573 in England and 65 in Scotland, have been matched with new employers. The Construction Industry Training Board has a further 508 offers of vacancies from potential employers that it is trying to fill and match with individual apprentices who still need a placement. It is continuing to receive offers of further vacancies, so that work is ongoing. The CITB has told the Skills Minister that it is determined to ensure that every Carillion apprentice is able to complete his or her course.

Q82 **Robert Halfon:** Are you offering a financial incentive to the employers to take on these apprenticeships?

Mr Lidington: CITB has created a £1.5 million cash incentive programme to encourage new employers to take them on.

Q83 **Robert Halfon:** And that is paid by them, not by the taxpayer, is that right?

Mr Lidington: That is paid by the CITB. The Education and Skills Funding Agency has reallocated to CITB the funding that it was paying Carillion for training, so CITB has that stream of money available.

Q84 **Robert Halfon:** You said that there are about 500 offers.

Mr Lidington: There are about 500 offers, in addition to the 638 who have been placed so far. If those are all filled, that would take us to 1,000.

Q85 **Robert Halfon:** Is the worst-case scenario that you will have a few hundred without an apprenticeship?

Mr Lidington: I hope very much—and it is the CITB's intention—that every single one of the 1,500 will be able to complete, assuming that they wish to continue.

Q86 **Robert Halfon:** If a few hundred are left, what other options will be available for them?

Mr Lidington: That is something that the Skills Minister and her officials will be taking a lead on. At the moment, there is still very encouraging contact between the CITB and various employers who want to take people.

These are often apprentices who have been doing a course in construction work. There is a massive demand for those skills at the moment.

Q87 **Robert Halfon:** Do you expect the few hundred to be offered an apprenticeship, even if it is not by the CITB?

Mr Lidington: I would expect them to be offered an apprenticeship. Certainly, if it became clear that it was proving very difficult to get people placed, I am sure that the Department for Education would want to take appropriate action.

Q88 **Robert Halfon:** Clearly Carillion did a fair bit of subcontracting. Do we know how many apprentices there are in terms of subcontractors?

Mr Lidington: No, and I certainly don't have those figures. I am not sure if we would have those—

Q89 **Robert Halfon:** Surely you would know the number of companies that Carillion had subcontracted to, and there must be some record of how many apprentices there are.

Gareth Rhys Williams: This problem arose because Carillion had an apprenticeship business. From memory—this may not be exactly right—I think it was something in the region of a couple of hundred of Carillion's subcontractors that had apprentices who were employed by those subcontractors and were being trained by Carillion—of that order.

Q90 **Robert Halfon:** What is happening to them?

Gareth Rhys Williams: That continues, except they are training now instead—what the CITB has stood in for is the training of those apprentices.

Q91 **Robert Halfon:** The CITB is training the directly employed apprentices.

Gareth Rhys Williams: And indeed those other ones as well.

Q92 **Robert Halfon:** So of the subcontracting ones, you are saying there are roughly 200.

Gareth Rhys Williams: It might be just over 100, but that is the order of magnitude.

Q93 **Robert Halfon:** Was that included in your figure of 1,500?

Gareth Rhys Williams: No, that is the people who were employed by Carillion. Carillion was both employing people and, with a different hat, training them.

Q94 **Robert Halfon:** What I am trying to understand is: does the figure you gave me include those people or not?

Gareth Rhys Williams: No. That 200—if that is the right number—is on top.

Q95 **Robert Halfon:** So there are roughly 500 who may not have apprenticeships on offer yet, and there are another 200 that you know of. So that is 700.

Gareth Rhys Williams: No. There are 200, if that is the right number—I almost regret saying it, but it is of that nature. They are still employed by the subcontractors.

Q96 **Robert Halfon:** Yes. I am trying to find out the total. The Minister said there were roughly 500 who had not been offered apprenticeships yet, or there was not an offer on the table.

John Manzoni: It's moving every day.

Gareth Rhys Williams: They haven't been offered employment. CITB will be training all of them, as I understand it, so what we need to find is the employment that dovetails with the training.

Q97 **Robert Halfon:** Carillion was the training provider, and they have obviously gone, so who is the training provider—CITB?

Gareth Rhys Williams: CITB.

Q98 **Robert Halfon:** They are doing the training as well as finding other apprenticeships for employment.

Mr Lidington: I can give a bit of additional information. Our latest information—for Scotland as well as England—as I have it is that there are 796 apprentices remaining to be placed. That is more than our initial estimate, because as the official receiver has started to disentangle Carillion's affairs we found that some apprentices were employed by other Carillion group entities; we must not forget that the majority of Carillion's work was for private sector customers rather than public sector customers. CITB has received offers from four of the big house builders to absorb any apprentices that remain at the end of the process.

Q99 **Robert Halfon:** But you still don't know how many apprentices were employed by subcontractor companies in general, apart from those who were training with Carillion.

Gareth Rhys Williams: Perhaps could I get you that number, when I dig it out?

Q100 **Robert Halfon:** What I am trying to say—this is quite complicated. So you know about the ones who were trained by Carillion—that is roughly 200—but what I am trying to find out is: how many companies that Carillion had that were not necessarily trained by Carillion but nevertheless—

John Manzoni: Maybe it is quite hard to get.

Q101 **Robert Halfon:** But you would be able to ask those companies how many apprentices they had.

Gareth Rhys Williams: But their arrangements would continue regardless.

Q102 **Robert Halfon:** Not if the companies are in financial trouble because of Carillion.

Gareth Rhys Williams: That is a very fair point.

Chair: I am conscious that a number of Chairs want to come in before we lose the quorum.

Q103 **Stephen McPartland:** Are you confident that the Insolvency Service has the resources it needs to deal with a large corporate failure such as Carillion as well as providing assistance, potentially to some of Carillion's suppliers?

Mr Lidington: Yes. So far, from the evidence I have seen and from talking to the head of the Insolvency Service and to the special managers they have appointed—PwC—they seem to me to be doing a very good job. They are working their way through the various contracts that Carillion had, disentangling what have sometimes proved to be quite complex systems of management information. I know, having talked to them, that they are wanting to move forward as rapidly as possible. Clearly, if they come to us and say, "We need some extra help," that is something we would give to them.

Q104 **Stephen McPartland:** Thank you. The Government said they had no choice but to support the liquidation of Carillion. Were any other choices potentially missed at an earlier stage where it could have had an orderly administration?

Mr Lidington: I can only speak about the week between my appointment to my current role and Carillion going into liquidation. *[Laughter.]* What I do remember is that I was appointed between 1.30 and 2 on Monday 8th, and at some time that evening Mr Manzoni put his head around the door of my office and said, "I need to have a word about Carillion." Now, I had known from my previous ministerial role that there had been difficulties, but I had certainly not been expecting that there would be this complete failure.

Yes, we were basically faced with, broadly speaking, three options. The one we took was to be willing to support the official receiver for a managed and orderly liquidation that would allow the service to continue. The second was to stand aside and allow a disorderly liquidation to take place, which would have meant the termination of all the contracts, including the public service contracts and redundancy for all the workers engaged on those contracts. So, at the very minimum, there would have been a severe disruption to the provision of key public services.

The third option would have been to use taxpayers' money to provide a bail-out of some kind to Carillion. Carillion came to us. John, I think I am right in saying that it produced an outline business plan on new year's eve— something like that.

John Manzoni: Their first request to Government was on 31 December. From 31 December to 15 January, there was a series of meetings. The reasons—I think I have rehearsed this with some—why the Government decided not to step in were various, but predominantly we were not confident in the future it was painting and that it would be able to manage that. It was asking for both the future and a bridge to the future. We did not want to provide the short-term bridge, because we were not confident in the future—and, it turned out, neither were its members, because otherwise it would have—

Q105 **Robert Halfon:** I have a very quick question. In terms of what has happened with the apprentices, you were lucky that the CITB was able to step in. With future Government contracts at big organisations, do you think there are lessons to be learned, given the importance that the Government place on apprenticeships, that there are guarantees that we do not get into this situation in the future?

Mr Lidington: Clearly, the first thing to say is that we will need to be alert to learn whatever lessons need to be learned from this episode, but actually it was not a question of the CITB happening to turn up as a piece of good fortune. That was part of contingency planning that had taken place in the relevant Department.

In that week, between being alerted to the perilous and almost certainly terminal state of Carillion's business and the liquidation, I chaired meetings of Ministers from across Whitehall. Before we took a final decision about which option to go for, we stress-tested as best as we could the contingency plans that various Departments had put in place, to make a judgment as to whether we were confident that public services could continue to be provided, if we did not do what Carillion was asking of us and come forward with a bail-out.

In this respect, I think that the civil service was shown to have done a very good job in terms of the way in which those contingency plans had been drawn up in different Departments over previous months.

Q106 **Robert Neill:** Can we come back to the two prison contracts that were mentioned already. They are large facilities management contracts. Carillion actually had 50% of the share of the four contracts that were let out. Was that wise?

Gareth Rhys Williams: I was not in the business when those were let. It has the southern region and Amey won local contracts for the northern region. I think it won them fair and square at the time, as those were competitive—

Q107 **Robert Neill:** They were supposed to save £115 million over the five years. It is clearly not going to save anything like that now. How much do you assess it will now save, if anything?

Mr Lidington: Can I give a response to Mr Neill's question? While this would properly be a matter for my successor as Justice Secretary, I will respond to you now. I recall in the summer of last year—it must have been after the first profits warning—my then permanent secretary coming to me and saying that we do not think there is a crisis. The company at that stage was very confident that it would put a restructuring and refinancing plan in place. I discussed the potential risk with him and gave instructions that we needed to make certain that we had an emergency plan in place, just in case the worst happened.

The permanent secretary went away and did that. As a result, there is a Government company that is formed and ready in the wings, and is in the process of taking control. My view on the point that Mr Neill was making is that as those very large contracts expire over time, they need to be replaced by more devolution to individual governors or perhaps groups of governors in a geographical area.

Obviously, with all these things, there is a judgment, a tension, between value for money through economies of scale, and local provision, but I think we need to trust governors more to decide who does the repairs and maintenance.

Q108 **Robert Neill:** That is a fair point. One of the concerns raised with us very often when we speak to governors is that when they attempted to get work done, there was a long history of backlogs. Virtually every independent monitoring board report said there was a problem with the way these contracts were delivered, but when the governor, the person on the ground, tried to get anywhere, in effect the response from Carillion and the other outsourcers was, "Well, actually, our contract is not with you. Our contract is with the centre; our contract is with the Government's commercial operations."

John Manzoni: Rules of debate.

Q109 **Robert Neill:** There are lessons to be learned, perhaps, from that.

John Manzoni: Absolutely.

Q110 **Robert Neill:** The other thing I wanted to press you on is this. Those contracts, even before Carillion went under, were never going to make the savings of £115 million, because they had to be reset because the cost base was flawed. That was particularly around the balance between reactive and preventative maintenance.

The reality of that, in the English language, is that reactive maintenance includes repairing broken windows, and you get charged more for repairing broken windows because that is not in the basic contract. Wouldn't it have seemed pretty obvious to whoever was writing those contracts that in prisons you have quite a lot of people who might be inclined to break windows from time to time and that the cost of repairing them ought to be in the base contract? What are we going to do about getting the skills to write those contracts properly?

John Manzoni: Could I come back to what I said to the Committee before? We have spent the last two or three years building the sorts of skills that would allow us to more sensibly structure the contract—

Q111 **Robert Neill:** Lessons learned.

John Manzoni: Absolutely. Otherwise, you're on a transaction, price-based relationship, which doesn't work.

Q112 **Robert Neill:** Are there plans at the moment to keep—there are only two and a half years to run on this contract, and it was running on a very, very tight margin, perhaps an optimistically tight margin. You're not going to be able to pass this off to anyone else, really, are you?

Mr Lidington: It is for the current Secretary of State to take forward, but my understanding is that the plan is for the Government company to take over this contract for the remainder of its term. Then the Secretary of State will have to decide whether, on expiry, those powers are devolved to governors.

Gareth Rhys Williams: There is a fixed cost for the cleaning, and then for breakages and repairs, I think there is a fixed schedule per item. We talked a little bit earlier about passing risk. If—terrible instance—there is a riot in a prison, that generates more breakages. I don't think that is a fair risk that we should push on to the contractor.

Q113 **Robert Neill:** Anyone who has ever worked in a prison or even been in a prison would know that breakages of windows don't happen just during riots. They are a commonplace—a daily occurrence. That gives me the sense that whoever wrote the contracts didn't know anything about the service that was being written for.

Mr Lidington: I think there are plenty of lessons to be learned.

Q114 **Robert Neill:** I understand that, and I get the point, Mr Manzoni, and others have got that on board.

My final question, a very short one, is this. There is a different set of contracts, with different outsourcers. You have had profit warnings around Interserve and Capita. Of course, they are providers of criminal justice services, and the sensitive area is around some of the community rehabilitation companies, where again there have been concerns about contracts having to be reset with others because of the cost base. I gather the *Financial Times* said the Cabinet Office—this is to Mr Manzoni—had set up a team of officials to monitor Interserve. Is that correct, and can you help us on what the Government's plans are, lest there be a risk? Perhaps those reports were wrong, but I'm just interested to know what you are doing to monitor that.

John Manzoni: We are in discussion with all our strategic suppliers. Both the companies that you have mentioned are on the strategic supplier list. And of course when things happen to those companies, we intensify those conversations. That is the state that we're in now. We are having those normal dialogues with those companies, so that we can be alert—just as we were, by the way, with Carillion. So that's where we are.

Q115 **Robert Neill:** I understand, and you are conscious of particular issues around the CRC sector?

John Manzoni: Absolutely.

Q116 **Meg Hillier:** Minister, you talked earlier about the contingency plans in place, and every permanent secretary who has appeared before the PAC in recent weeks has talked about that. Do you have any contingency plans in place for other large Government contractors at this moment in time?

Mr Lidington: Each Department that is responsible for a contract needs to have contingency plans in place.

Q117 **Meg Hillier:** To the same level as the ones that were put in place for Carillion?

Mr Lidington: That depends on the information or intelligence that we have about a particular key supplier. The purpose of the monitoring of the strategic suppliers that Mr Manzoni was talking about is in part to ensure that Departments are informed and can do appropriate contingency planning.

Q118 **Meg Hillier:** The same question to you, then, Mr Manzoni: are there any current contingency plans in place in relation to other contractors that you are worried about?

John Manzoni: The answer to your question is yes. Are they at the same level of detail and definition? We have contingency plans. Wherever we believe those to be necessary, we are in action putting those in place. They are not—

Q119 **Meg Hillier:** Can you give us any examples?

John Manzoni: I would prefer not to, on the basis that we are in public and of course these things are—

Q120 **Meg Hillier:** Can you give us the scale? How many contingency plans are being worked up right now?

John Manzoni: An appropriate number.

Q121 **Meg Hillier:** Double figures? Double figures is quite a range, Mr Manzoni—it is 10 to 99.

John Manzoni: Yes.

Meg Hillier: Between 10 and 99. Thank you very much.

Q122 **Mr Betts:** I apologise for being late. I was in the local government finance debate. Local councils clearly had quite a lot of contracts with Carillion. Minister, do you know the scale of the contracts that are with local councils and how many there are?

Mr Lidington: About 300, but some of those will be with NHS trusts. If you look at the 450 contracts that Carillion had with the UK public sector, roughly 150 were with central Government and the other 300 were with local authorities and, to some extent, with NHS trusts as well.

Q123 **Mr Betts:** When you gave the House assurances that the services that those contracts delivered and the employees engaged in those contracts would be supported by the Government, and that the Government would stand behind them to make sure the services continued, did that apply to local government contracts as well?

Mr Lidington: As far as I am aware, the contracts—for example, for school meals, cleaning and so on—have continued to be delivered. Obviously, at the same time, as with central Government contracts, the official receiver has taken charge of Carillion's businesses and is working through, with the customers—local authorities are entitled to take their own decisions on this—how particular services should be provided in the future, or whether a local authority wishes to continue with a particular service. There will be myriad decisions for individual local authorities to take about the particular contracts that fall to them.

Q124 **Mr Betts:** In terms of any financial costs to local councils, they have to bear them themselves. Is that right?

Mr Lidington: For the moment, yes, in the same way that any other customer will have to.

John Manzoni: But it is for the provision of the service that they are receiving.

Mr Lidington: Yes, they are paying for the service.

Q125 **Mr Betts:** But if another provider has to come in and that has an extra cost, councils have to cover that themselves.

John Manzoni: Yes, there is a whole process of transference that the official receiver is working through, but as I have said before, the basic principle is that these contracts get transferred quickly and like for like. That is the whole point. The official receiver has to move very quickly.

Q126 **Mr Betts:** But if there is an extra cost, councils have to cover it themselves?

John Manzoni: I think that we will have to wait—for the moment, there is no decision otherwise.

Gareth Rhys Williams: If a council owns a contract and chooses to cancel it, they are probably doing that because they think they can get it cheaper than they can by transferring—

Q127 **Mr Betts:** It is not about choosing to cancel, is it? Carillion is not there anymore to deliver the contract.

Gareth Rhys Williams: The official receiver is busy selling those contracts to other providers, who will take on the ex-Carillion employees—

John Manzoni: On the same terms.

Gareth Rhys Williams: On the same terms. If the council chooses to cancel that contract, it is presumably because they—

Q128 **Mr Betts:** But otherwise, councils should not have to bear any extra cost. Right. There may be quite a number of complications in that transfer—perhaps legal complications but also TUPE and other transfer arrangements around employment. Are councils going to get support and assistance from the Government in doing that? It could be quite complicated and quite a challenge for some authorities, which may not have been through that sort of experience before. Some of these contracts are very complicated indeed.

Mr Lidington: In the first place, the responsibility does lie with local authorities. They should talk to—*[Interruption.]* The official receiver will be navigating them through the Carillion maze.

Gareth Rhys Williams: If the contracts are moving, say, from Carillion to another facilities management vendor, it is that new vendor who will be taking on the Carillion employees. So TUPE does not strictly apply for insolvent businesses—some Carillion businesses are solvent and some are insolvent. This is quite a maze, but the challenge that you rightly point to needs to be dealt with by the new vendor, not so much by the customer, which is the council. I think the council is relatively insulated from that problem.

Q129 **Mr Betts:** You "think"?

Gareth Rhys Williams: Well, if they choose to bring those Carillion employees on to their own books and self-deliver, they are moving Carillion employees to themselves—that is something they would need to deal with. If they are moving the contract to a different third party, then the different third party has to do all that.

Q130 **Mr Betts:** But if councils want advice and assistance, are the Government ready to help them?

Gareth Rhys Williams: Yes—exactly.

Chair: I had a number of questions on the health service, but as we are pretty much out of time, would you mind, Minister, if I wrote to you about those? That would be super.

Q131 **Mr Jenkin:** I am so grateful, Chair, because I am still very vexed, having listened to everything, about the answers I was being given earlier. You have just confirmed again, Mr Rhys Williams, that the receiver is going to be selling off assets out of Carillion's balance sheets—and those assets are contracts and those contracts are worth money. Yet the Treasury is putting in money that preserves the value of those contracts. These contracts will be sold to other companies that will be buying them in a distressed sale, because that is the nature of a liquidation sale. Why is the Treasury not getting at least first refusal on those contracts? Why is the public sector going to give up yet more value to the private sector, when the public sector could actually recover some value by putting in offers for these contracts?

Mr Lidington: Some are. That is applying, for example, in the case of the prisons.

Q132 **Mr Jenkin:** That contract has failed. That is why it is automatically not buying that contract—that contract has collapsed. The other contracts, which are in the SPVs—have I missed something?

John Manzoni: Yes, I think you have. The trouble is that it is horribly complicated. I appreciate principles—I am trying to get to the principal point. Whenever this is a service provided through an SPV, it is cost-certain to the public sector. Whatever we choose to do for that SPV, we are going to pay the same for it.

Q133 **Mr Jenkin:** But what is not cost-certain is the money that is going into the receiver, to support the continuing operation.

John Manzoni: It is being offset by all of the value that the receiver is then receiving.

Q134 **Mr Jenkin:** Yes, but how do you know? What is likely is that these contracts will be sold off at a knock-down price.

Chair: That is not the point. It may not be entirely—

John Manzoni: It may not be, but the receiver is legally obliged to receive the maximum value that he can achieve through the sale. If we chose to step in, we will have to pay the full value of that—

Q135 **Mr Jenkin:** Can we nationalise these contracts? It is not the first time the public sector will have bought businesses out of receivership in order to maximise and preserve their value. It might be much better value for the taxpayer to consider that option, and it might be possible to create a new business out of the ashes of this mess.

John Manzoni: The implications of stepping into private sector SPVs is hugely complex, because of course nobody will lend to the private sector ever again, because they just step in. That is one issue.

Q136 **Mr Jenkin:** I don’t seem to be explaining myself very well. Other people attach value to these contracts that are going to be sold by the receiver. Why does the Treasury not attach value to these contracts, and then we can create something new out of this mess instead of just selling them off to the usual suspects?

Chair: Certainly there are the opportunities—I know we have explored with you previously—of getting out of very expensive PFI contracts.

Q137 **Mr Jenkin:** They think they’re going to make a profit out of it, because otherwise they wouldn’t be buying them.

John Manzoni: Look, Bernard, contractually we have to provide the lenders the opportunity first to do it. That is why these PFIs are like they are. So we cannot step in, because contractually the first people who have the opportunity are the lenders. They will say, “This is a PFI worth something.”

Q138 **Mr Jenkin:** Yes, but the receiver is offering them for sale. We have heard that again from Mr Rhys Williams. The receiver is going to offer these assets for sale. Why can’t the Treasury be a potential buyer?

Gareth Rhys Williams: There are several layers to this. The customer has a right, in an insolvency, to cancel these contracts. In the example that Mr Betts was using, if a local authority is happy that the official receiver sells the contract to Mr X, the council has to say that it is okay with that being novated over. X pays the official receiver whatever they see as a fair value, and that defrays the £150 million.

Q139 **Mr Jenkin:** You are even explaining how, if they were in default, that these contracts could be brought back in-house. How are we going to explain to the public that the same kind of companies are buying these contracts when we could have brought them back in-house?

Gareth Rhys Williams: To bring them back in-house—this comes back to the earlier discussion, which is a good one to have—we must ask whether we have the infrastructure to run those contracts ourselves. In the NOMS case that Mr Neill talked about—I would dispute whether that is a failed contract—we are the contract owners, so we can decide that because we are the customer. In the cases where the SPV is the customer, if we brought that in there is no purchase price, so there is nothing to defray against the £150 million. Then the risk is would the SPV do that or would they cancel the contract and re-compete it with Mr X or Mr Y out in the marketplace? That is the complication that John is trying to point to.

Q140 **Mr Jenkin:** There is obviously 450 customers to deal with, but I cannot imagine what the public's reaction will be if they see a lot of contracts being sold off cheap to a whole lot big companies, which then make big profits out of the demise of Carillion after the taxpayer has put money in to keep the whole thing going. How will you explain that?

Gareth Rhys Williams: The alternative was not to put money in at all, for service levels to collapse, and then these contracts would have no value and there would be no money at all. I accept your point about the fire sale, but the alternative was not to have anything to sell.

Q141 **Mr Jenkin:** No, I am not advocating letting the whole thing collapse, but usually the person who rescues the company owns the company.

John Manzoni: This is worth a longer, detailed conversation. The complexity is the contractual structure of the SPV. That is the issue.

Chair: Perhaps this is something we can explore through correspondence, because I agree that it is of huge public interest.

Nicky Morgan: It is the general principle, isn't it?

Chair: Yes. Thank you all for coming this afternoon.