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The Collapse of P3 Giant Carillion and Its Implications

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The Collapse of Carillion in the UK, Causes and Consequences

Carillion, a major global player in the promotion of Public-Private Partnerships (P3s) has gone into liquidation in the UK. The collapse of this massive company is a case study of all that is wrong with P3s as an approach to building and operating public infrastructure. Carillion sponsored and financed over 60 P3s but more importantly provided the facility management services for them once construction was completed. It was the second largest builder in the UK. It also held many government outsourcing contracts and undertook project financing as well as construction.

In the UK, Carillion was responsible for school dinners and cleaning services to 230 schools, and delivered maintenance and facility management services to many hospitals, covering the needs of 200 operating theatres and 12,000 beds and catering for 19,000 meals a day. It maintained 50,000 homes on Army bases; had £200m of prison contracts and other major construction projects, including work on highways and high speed rail projects. It had annual sales of £5.2 billion (about Ca\$9.4 billion), employed 19,600 workers in the UK, 6,000 in Canada and 46,000 worldwide. It is now being wound up by the Official Receiver, assisted by the consulting/accounting firm PwC.

Carillion collapsed after it had failed to meet huge debt commitments in 2017. The debt was the result of over-expansion of P3s by Carillion, delays in implementing some of its large P3s with big up-front costs, and a slowing down of new P3 deals in the UK as government evaluates the P3 strategy and grapples with Brexit. This combination of factors caused cash flow problems for Carillion which, in the past, had probably been hidden by the continued expansion of P3 business. It also dramatically reduced profits. In July 2017 Carillion wrote down £845 million (around Ca\$1.4 billion) of debt, £375 million on account of UK P3 business and £470 million on account of P3s in the Middle East and Canada. Its share price dropped dramatically but even then, so wedded was the Tory government to supporting private business in the provision of public infrastructure and services, that it was awarded further contracts by government amounting to £1.3 billion to the end of 2017. But the cash flow and profit problems continued to mount so that by January 2018 Carillion's share price had fallen to only 7% of its May 2017 level and the company was liquidated.

What this means is that the UK government has had to step in to ensure that school children

are fed (local fire brigades are helping out here!), that patients receive food and laundry facilities, that prisons are staffed and that roads are maintained. This puts the lie to the principal advantage claimed for P3s which is that they are supposed to transfer risk from the public to the private sector.

(T)he fundamental issue raised by Carillion's failure is that vital public services cannot be outsourced to private contractors, without Government underwriting the risks of collapse...So-called risk transfer, where financial risk associated with infrastructure construction and operation was transferred to the private sector, to justify the higher interest on PFI (PPP) loans (double the interest rate on Government loans) is, and always was, a massive con (Benjamin, 2018).

But it was this so-called risk transfer that justified the value for money that P3 proponents claimed for them which was used to justify their implementation. And this was in spite of the refutation of risk transfer by academics in Europe (such as Pollock et al, 2004 and Whitfield, 2006, 2010) and in Canada (Loxley and Loxley, 2010 and Hamel, 2007) going back many years. Unions on both sides of the Atlantic also challenged this assertion, but to no avail.

The collapse of Carillion also raises issues of the oversight of P3 companies by auditors. Only ten months before liquidation, its auditor, KPMG, had given its seal of approval to Carillion's financial statement. Yet Carillion announced the deterioration of its finances in early December 2016 which was followed by huge and unsustainable increases in its debt. How could KPMG not have realized this? This is yet another example of the terrible worldwide record of KPMG, a major advisor to Manitoba's government (Silver 2017). The reality is that the large auditing and consulting companies are so bound up in all aspects P3s, from assessment of proposals and measurement of value for money, to evaluating and auditing

them, that they are unable to be objective. There seems to be, however, no mechanism for holding them accountable for their failings. There are echoes here of the delinquency of bond rating agencies and banks in the 2008 financial crisis.

Who will pay for the collapse? Carillion shareholders will receive nothing; their shares are worthless! The large banks which advanced the unsecured debt, Barclays, Lloyds, HSBC, RBC and Santander, will also lose, though PWC lists 'securing the best outcome for creditors' alongside ensuring 'the continuity of public services' as the priority of the Official Receiver (PWC, 2018). PWC is also asking all employees, agents and subcontractors to continue to work as normal and they will be paid for the work they do during the liquidations. At the same time, however, they are also calling for expressions of interest from companies which might be interested in buying portions of Carillion's business (PWC, 2018), which must be quite unsettling to workers.

There are concerns that many workers will lose their jobs as contracts are restructured to replace Carillion and assets sold off to liquidate debts. Work has ceased on some construction sites and workers sent home. Furthermore, some 30,000 small businesses are owed money by Carillion and are unlikely to be paid, which will inevitably lead them to lay off workers. The collapse will cost Balfour Beatty, a relatively large company, between £35 and £45 million, with unknown implications for their workers. Meanwhile, the executives of Carillion relaxed the provisions on the claw back of their bonuses in 2016 and are said to have paid themselves £4 million in 2017, though under public protest, the Insolvency Service appears to have recalled bonuses and severance payments (Financial Times, January 18, 2018).

Carillion has a pension deficit of around £800 million putting the pensions of around 27,500 workers at risk. Fortunately, in the UK there is the State Pension Protection Fund which com-

pensates defined benefit schemes when the employer is insolvent. This will take over the plans but even then, workers will lose 10-20% of what they would have expected to receive. There are

serious questions to be asked, therefore, about how the pension gap was allowed to grow to be so large, especially given the auditor's clean bill of health.

Carillion in Canada

Carillion obtained about 11% of its total annual revenue or £596 million (over Ca\$1 billion) from Canadian operations (Annual Report, 2016) and employs 6,000 Canadian workers. It is heavily involved in 10 P3s in Canada with total capital assets of \$3.25 billion, eight in Ontario and one each in Saskatchewan and the Northwest Territories. Seven of these are hospitals and two are mental health centres. It was a failed attempt to withdraw from the health sector in 2017 that helped precipitate the UK crisis. Carillion had hoped to raise \$300 million by selling off some of its health assets, a move deemed by the CEO as being crucial to its global restructuring (Waldie, 2018), though we do not know precisely which ones had been targeted.

Carillion played and still plays many roles in each of the P3s, from developer, equity investor, financier, design-builder, facilities manager and re-newer of lifecycle assets. On the facilities management and maintenance side, it is committed in all but one of the P3s to at least 20 years of involvement and for most, 30 years or more.

Carillion is heavily involved in out-sourced road maintenance in Ontario and Alberta, with contracts covering 42,000 km of road and is also

engaged in electrical transmission and related fields across Canada.

Carillion does have a Manitoba connection. In 2014 it purchased Rokstad, a BC company specializing in power line construction and maintenance. In December 2016 Rokstad was awarded a \$200 million contract by Manitoba Hydro to deliver part of its Bipole III high-voltage transmission line. Work began in late 2016 and is scheduled for completion in 2018. This involves clearing rights of way, building towers and stringing cables. Rokstad's performance has been less than satisfactory, constituting a huge risk to timely completion of the Bipole project but not because of anything to do directly with the failure of its parent company. The work has been delayed, over budget and unsatisfactory, forcing Manitoba Hydro to descope its work and shift part of the contract to another contractor (Public Utilities Board, 2018). Manitoba Hydro continues to work with Rokstad but monitors it closely to reduce further risk (Public Utilities Board, 2018, p.43)

So how will the liquidation of the parent company affect Carillion Canada? The short answer is that we really don't know. The Canadian office is assuring workers, suppliers and the or-

TABLE 1 Carillion Canadian PPP Projects Portfolio

Project	Sector	Capital Cost (\$CAD)	Delivery Model	Carillion's Role	Financial Close	Substantial Completion/ Years of Concession	Location
Stanton Territorial Hospital Renewal	Health	\$300m	Design-Build-Finance-Maintain	Developer, Equity Investor, Financier, Facilities Management, Lifecycle Renewal	2015	2018/ 30 Years	Yellowknife, NWT
Saskatchewan Hospital North Battleford	Health	\$300m	Design-Build-Finance-Maintain	Developer, Equity Investor, Financier, Design-Builder, Facilities Management, Lifecycle Renewal	2015	2018/ 30 Years	North Battleford, SK
Oakville Trafalgar Memorial Hospital	Health	\$1.1b	Design-Build-Finance-Maintain	Developer, Equity Investor, Financier, Design-Builder, Facilities Management, Lifecycle Renewal	2011	2015/ 34 Years	Oakville, ON
Forensic Services and Coroner's Complex	Justice, Secure	\$300m	Design-Build-Finance-Maintain	Developer, Equity Investor, Financier, Design-Builder, Facilities Management, Lifecycle Renewal	2010	2013 30 Years	Toronto, ON
Centre for Addiction and Mental Health	Health	\$200m	Design-Build-Finance-Maintain	Developer, Equity Investor, Financier, Design-Builder, Facilities Management, Lifecycle Renewal	2009	2012/ 30 Years	Toronto, ON
Royal Victoria Regional Health Centre	Health	\$260m	Build-Finance	Developer, Financier, Design-Builder	2009	2013/ 25 Years	Barrie, ON
Sault Area Hospital	Health	\$276m	Design-Build-Finance-Maintain	Developer, Equity Investor, Financier, Design-Builder, Facilities Management, Lifecycle Renewal	2007	2010/ 30 Years	Toronto, ON
Sunnybrook Health Sciences Centre M-Wing Expansion	Health	\$142m	Build-Finance	Developer, Financier, Design-Builder	2007	2010/ n.a.	Toronto, ON
Royal Ottawa Mental Health Centre	Health	\$130m	Design-Build-Finance-Maintain	Developer, Equity Investor, Financier, Design-Builder, Facilities Management, Lifecycle Renewal	2004	2007/ 20 Years	Ottawa, ON
Brampton Civic Hospital	Health	\$510m	Design-Build-Finance-Maintain	Developer, Equity Investor, Financier, Design-Builder, Facilities Management, Lifecycle Renewal	2003	2007/ 25 years	Brampton, ON

SOURCE: Carillion: [http://www.carillion.ca/capabilities/public-private-partnerships-\(ppp\).aspx#.WI_De3lMFdg](http://www.carillion.ca/capabilities/public-private-partnerships-(ppp).aspx#.WI_De3lMFdg)

ganizations it is contracting with that all is well and that its operations are “not in liquidation and continue uninterrupted... Our employees, subcontractors and suppliers in Canada continue to be paid and we remain committed to delivering safe, quality services for our clients” (Waldie, 2018). It goes on, however, to state that

“Our Canadian leadership is currently assessing the situation and working with stakeholders to ensure continuity of operations” suggesting that there is some doubt about the future of the Canadian operations. If, through the process of liquidation, the stability of the Canadian operations is called into question, contingency plans

will need to be ready to ensure that the ongoing operations of the P3s in the health sector are secured. Likewise, the road maintenance and power activities will need to be provided for. In the case of Manitoba Hydro, its submissions to the PUB make it clear that it does have contingency plans in the event that Rokstad fails to deliver, for whatever reason.

Until the future of Carillion's operations in Canada is clarified, workers will worry about their jobs, incomes and pensions. On pensions, as the recently insolvency and liquidation of Sears has highlighted, Canada is way behind the UK in providing support to workers when companies become insolvent. Only one province has a pension protection fund. Fortunately, that is Ontario where many Carillion workers are located. Un-

fortunately, pension protection there is limited to \$1,000 per month and only to workers "who meet certain age and service criteria" (Ontario Securities Commission, 2018).

As unions representing health care workers have recently argued, what is needed is an end to privatizing health care delivery and the contracting out of essential services. Workers affected must receive guarantees from government that they will be paid and their pensions protected, whatever happens to Carillion Canada. P3s have added huge costs to service delivery on the basis of bogus claims about risk transfer. The Carillion collapse shows unambiguously that ultimately government is on the line for risk. It is time to cease using P3s and bring infrastructure building and maintenance back into the public sector.

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