

UK FCA censures Carillion plc for breaches of the Market Abuse Regulation and the Listing Rules

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On 28 July 2022, the Financial Conduct Authority (FCA) published decision notices for Carillion plc (Carillion) and three of its former executive directors relating to breaches of the Market Abuse Regulation (MAR) and the Listing Rules.

The FCA's decision notice in relation to Carillion provides an important reminder of the expectations for issuers with listed shares in the UK, particularly around the disclosure of credible risks to financial performance and the design and implementation of internal systems and controls for complying with issuer obligations under the Listing Rules.

Carillion was a leading international construction, project finance and support services business operating in the UK, Canada and the Middle East. It was a non-trading investment company operating through a number of subsidiaries and joint ventures. Carillion went into liquidation in January 2018. Prior to entering liquidation, Carillion's shares were listed on the premium segment of the London Stock Exchange.

Carillion entered into liquidation on 15 January 2018 following the announcement in July 2017 of a provision of £845 million, of which £375 million was in relation to projects in Carillion Construction Services (CCS), one of its divisions. The provision arose from a review following a deterioration in cash flows across several major construction projects. The announcement of the required provision was a surprise to many market analysts, with Carillion's share price falling by 39% on the day the provision was announced and by 70% within three days. These events led ultimately to Carillion's liquidation in January 2018.

The FCA's decision notice relates to three market announcements made by Carillion between December 2016 and May 2017. The FCA explains that these announcements did not accurately or fully disclose Carillion's true financial performance to the market. Specifically, the announcements made positive statements about Carillion's financial performance generally and in relation to CCS's construction business segment specifically. They did not disclose significant deteriorations in projects across the CCS portfolio and did not take account of various warning signs indicating anticipated losses and potentially reduced profitability, which were known at the time but had not been reported to the board or audit committee.

The market announcements, which included a trading update, Carillion's 2016 financial results and an AGM statement, were found by the FCA to have contained positive statements regarding the group's financial condition that were not justified and failed to reflect the true performance of CCS's construction contracts. The announcements also did not make reference to the significant risks associated with the positive statements regarding meeting financial expectations.

The announcement relating to the 2016 financial results was found to have been misleading as it did not accurately reflect the financial performance of certain major construction projects, and the costs and revenue associated with these projects was not determined in accordance with applicable accounting standards relating to the treatment of the revenue and costs associated with long-term construction contracts (i.e., IAS 11). Similarly, the May 2017 AGM statement did not, according to the FCA, give an accurate depiction of the group's trading position at that time, which had been materially affected by the deteriorating financial performance of CCS's construction projects.

As a result of the announcements, the FCA determined that Carillion breached Article 15 of MAR, which makes it a civil offence to engage in or attempt to engage in market manipulation. Article 12 of MAR defines market manipulation as behaviour which gives, or is likely to give, false or misleading signals as to the supply of, demand for, or price of, a financial instrument. The behaviour may include disseminating false or misleading information to the market. The FCA found that Carillion disseminated false or misleading information to the market in circumstances where it should have known the information was false or misleading.

The FCA found also that Carillion breached Listing Rule 1.3.3R, which requires firms to take reasonable care to ensure that market announcements are not misleading, false or deceptive and do not omit anything likely to affect the import of the information. The FCA noted that the deterioration in CCS's business combined with the pressure to meet challenging financial targets significantly increased the risk that overly aggressive accounting judgements would be applied to maintain financial performance. Carillion's procedures, systems and controls were not sufficiently robust to ensure that these judgements were made appropriately.

Moreover, due to the actions of the three executive directors, the board and audit committee were not made aware of the significant financial risks relating to CCS's construction projects. This meant they were unable to provide proper oversight of CCS's financial performance and the overly aggressive contract accounting judgements being applied to its major projects. As a consequence of Carillion's failure to take reasonable steps to establish and maintain adequate procedures, systems and controls to enable it to comply with its obligations under the Listing Rules, the FCA also found that it breached Listing Principle 1.

In addition, the FCA considers that the three former Carillion executive directors acted recklessly and were knowingly concerned in Carillion's breaches. In the FCA's view, they failed to ensure that the relevant announcements, for which they were responsible, accurately and fully reflected the deteriorating financial performance of CCS's UK construction business. The FCA decided to attribute their state of mind to Carillion. Consequently, the FCA found that Carillion failed to act with integrity towards existing and potential holders of its premium listed shares in breach of Listing Principle 2.

Due to the fact that Carillion is in liquidation, the FCA decided to impose a public censure rather than a financial penalty. However, the FCA notes that, were it not for Carillion's financial circumstances, it would have imposed a penalty of £37,910,000.

In relation to the three former executive directors, the FCA imposed fines on each ranging from £154,000 to £397,000 for their roles in the breaches described above. This is the first fine related to breaches of the Listing Rules since the second half of 2019. The Upper Tribunal will decide whether or not to uphold the FCA's decisions against the former executive directors.

If you have any questions regarding the matters covered in this publication, please reach out to any of the lawyers listed below or your usual Davis Polk contact.

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