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Treasury Committee

Fixing LIBOR: some preliminary findings

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Committee staff

The current staff of the Committee are Chris Stanton (Clerk), Lydia Menzies (Second Clerk), Jay Sheth, Adam Wales (Committee Specialists), Alison Game (Senior Committee Assistant), Steven Price and Lisa Stead (Committee Assistants) and James Abbott (Media Officer).

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Contents

1 Introduction

1. On 27 June 2012 the Financial Services Authority (FSA) issued a Final Notice fining Barclays Bank Plc (Barclays) £59.5 million for misconduct relating to the London Interbank Offered Rate (LIBOR) and the Euro Interbank Offered Rate (EURIBOR). This was the largest fine ever imposed by the FSA. It would have been £85 million had not Barclays been given the 30 per cent (stage 1) discount for its co-operation under the FSA's Decision Procedures and Penalties Manual.[1] The FSA investigation operated in co-operation with the US Commodity Futures Trading Commission (CTFC) and Department of Justice (DOJ), which imposed fines of $200 million and $160 million respectively. The misconduct to which the Notice relates lasted from 2005 to 2009.[2] The findings deeply concerned the Treasury Committee, Parliamentary colleagues and constituents.

2. This assessment of LIBOR by the Committee is necessarily a preliminary one. Enforcement proceedings continue both in the UK, where seven firms are being investigated, and in other jurisdictions. The UK Government has requested that the FSA conduct a review into the framework for the setting of LIBOR led by Martin Wheatley, its managing director and Chief Executive-designate of the future Financial Conduct Authority. Parliament has created a cross-party Commission of both Houses to examine the implications of the LIBOR findings for corporate governance and standards in banking. Commissioner Barnier is undertaking regulatory action at a European level. Both the FSA and Barclays are conducting internal reviews.

LIBOR and EURIBOR

3. The FSA has described both the significance of LIBOR and EURIBOR and the process by which it is set. On its significance:

> LIBOR and the EURIBOR are benchmark reference rates that indicate the interest rate that banks charge when lending to each other. They are fundamental to the operation of both UK and international financial markets, including markets in interest rate derivatives contracts.
>
> LIBOR and EURIBOR are used to determine payments made under both over the counter (OTC) interest rate derivatives contracts and exchange traded interest rate contracts by a wide range of counterparties including small businesses, large financial institutions and public authorities. Benchmark reference rates such as LIBOR and EURIBOR also affect payments made under a wide range of other contracts including loans and mortgages. The integrity of benchmark reference rates

1 See FSA, DEPP 6.7.3, http://fsahandbook.info/FSA/html/handbook/DEPP/6/7

2 *Barclays fined £59.5 million for significant failings in relation to LIBOR and EURIBOR*, FSA Press Notice, 27 June 2012

> such as LIBOR and EURIBOR is therefore of fundamental importance to both UK and international financial markets.[3]

Similarly, the British Bankers Association (BBA), the trade association for banks in the UK, on whose behalf LIBOR is published by Thomson Reuters, notes that "the [LIBOR] rates are also used as the basis for many types of lending, from syndicated and commercial lending, to residential mortgages", and that "it touches everyone from large international conglomerates to small borrowers".[4] LIBOR is also embedded in numerous contracts. Its influence is therefore very significant.

4. LIBOR and EURIBOR are set as follows:

> LIBOR is published on behalf of the British Bankers' Association (BBA) and EURIBOR is published on behalf of the European Banking Federation (EBF). LIBOR and EURIBOR are calculated as averages from submissions made by a number of banks selected by the BBA or EBF. There are different panels of banks that contribute submissions for each currency in which LIBOR is published, and for EURIBOR.
>
> LIBOR and EURIBOR are by far the most prevalent benchmark reference rates used in euro, US dollar and sterling OTC [over the counter] interest rate derivatives contracts and exchange traded interest rate contracts. The notional amount outstanding of OTC interest rate derivatives contracts in the first half of 2011 has been estimated at 554 trillion US dollars. The total value of volume of short term interest rate contracts traded on LIFFE in London in 2011 was 477 trillion euro including over 241 trillion euro relating to the three month EURIBOR futures contract (the fourth largest interest rate futures contract by volume in the world).
>
> Until February 2011 the US dollar LIBOR panel consisted of 16 banks and the rate calculation for each maturity excluded the highest four and lowest four submissions. An average of the remaining eight submissions was taken to produce the final published LIBOR.
>
> Throughout the Relevant Period [January 2005 to June 2010], the EURIBOR panel consisted of at least 40 banks and in each maturity the rate calculation excluded the highest 15% and lowest 15% of all the submissions collated. A rounded average of the remaining submissions was taken to produce the final published EURIBOR.[5]

The BBA told us that since 1 January 2010 LIBOR has been the responsibility of BBA LIBOR Ltd:

> BBA LIBOR Ltd undertakes the day-to-day running of the benchmark: liaising with Thomson Reuters, contributors, regulators and users as required. The company is

3 *Barclays fined £59.5 million for significant failings in relation to LIBOR and EURIBOR*, FSA Press Notice, 27 June 2012

4 BBA, LIBOR information, 2 July 2012 p 4 and p 16

5 *Barclays fined £59.5 million for significant failings in relation to LIBOR and EURIBOR*, FSA Press Notice, 27 June 2012

advised by the independent Foreign Exchange and Money Markets (FX&MM) Committee and the LIBOR Ltd. Board. The BBA LIBOR Ltd. Board is separate from that of the BBA.

BBA LIBOR became a limited company (BBA LIBOR Ltd.) with a separate board from the BBA on 1 January 2010. Prior to that BBA LIBOR was part of BBA Enterprises Ltd., a subsidiary of the BBA.

Pre-2010, all technical and rate-related issues were the responsibility of the FX&MM Committee; all contractual arrangements relating to licences were handled by BBA Enterprises Ltd; and the LIBOR Secretariat within the BBA managed relationships with contributing banks and public authorities, provided the Secretariat of the FX&MM Committee, and issued on behalf of the FX&MM Committee any statements and guidance relating to the rates as appropriate. The executive of the BBA brought regular updates on governance issues and related matters to the BBA Board.

From 1 January 2010, following the incorporation of LIBOR as BBA LIBOR Ltd, responsibilities were clarified and codified across all areas. All contractual issues were transferred to BBA LIBOR Ltd. The processes and procedures followed by contributing banks when submitting to Thomson Reuters remained the same as they were before incorporation and regular reports continued to be taken to the Board of the BBA as appropriate.[6]

FSA findings

5. The FSA found that Barclays' misconduct included:

making submissions which formed part of the LIBOR and EURIBOR setting process that took into account requests from Barclays' interest rate derivatives traders. These traders were motivated by profit and sought to benefit Barclays' trading positions;

seeking to influence the EURIBOR submissions of other banks contributing to the rate setting process; and

reducing its LIBOR submissions during the financial crisis as a result of senior management's concerns over negative media comment.

In addition, the FSA found that "Barclays failed to have adequate systems and controls in place relating to its LIBOR and EURIBOR submissions processes until June 2010 and failed to review its systems and controls at a number of appropriate points. Barclays also failed to deal with issues relating to its LIBOR submissions when these were escalated to Barclays' Investment Banking compliance function in 2007 and 2008".[7]

6 Written evidence from the BBA

7 *Barclays fined £59.5 million for significant failings in relation to LIBOR and EURIBOR*, FSA Press Notice, 27 June 2012

6. The FSA found that Barclays had “breached Principles 2, 3 and 5 of the FSA’s Principles for Businesses through misconduct relating to its submission of rates which formed part of the LIBOR and EURIBOR setting processes. There was a risk that Barclays’ misconduct would threaten the integrity of those benchmark reference rates.” Principle 2 states that “a firm must conduct its business with due skill, care and diligence”. Principle 3 states that “a firm must take reasonable care to organise and control its affairs responsibly and effectively, with adequate risk management systems”. Principle 5 states that “a firm must observe proper standards of market conduct”.[8]

7. The FSA’s acting director of enforcement and financial crime, Tracey McDermott, said at the time of the announcement of its Final Notice:

> Barclays’ misconduct was serious, widespread and extended over a number of years. The integrity of benchmark reference rates such as LIBOR and EURIBOR is of fundamental importance to both UK and international financial markets. Firms making submissions must not use those submissions as tools to promote their own interests.
>
> Making submissions to try to benefit trading positions is wholly unacceptable. This was possible because Barclays failed to ensure it had proper controls in place. Barclays’ behaviour threatened the integrity of the rates with the risk of serious harm to other market participants.[9]

The Committee concurs with the FSA’s assessment of the importance of the damage done to the benchmark rates by the attempted manipulation that the regulators discovered. Attempted manipulation of these reference rates reduces trust and confidence in markets and carries costs for end users. The Committee is concerned that the FSA was two years behind the US regulatory authorities in initiating its formal LIBOR investigations and that this delay has contributed to the perceived weakness of London in regulating financial markets.

8. The FSA identified two distinct phases of wrongdoing, with different motivations:

- Submissions from Barclays from 2005 to 2008 that took into account requests from Barclays’ interest rate derivatives traders. These submissions were motivated by profit;
- During the financial crisis, from 2007 to 2009, Barclays lowered its LIBOR submissions in response to negative media comment about the bank (often referred to in our evidence as ‘low-balling’).

These two phases are considered in detail below in sections 2 and 3 of this Report. Mr Bob Diamond, former Chief Executive of Barclays, attempted to subdivide the period of the false submissions during the financial crisis into two phases, one before 29 October 2008, the day Mr Diamond and Mr Paul Tucker, Deputy Governor of the Bank of England

8 FSA, Final Notice, 27 June 2012, paras 7, 186, 193 and 196.

9 *Barclays fined £59.5 million for significant failings in relation to LIBOR and EURIBOR*, FSA Press Notice, 27 June 2012

(Financial Stability) had a telephone conversation, and the period after that date.[10] **The Committee found Mr Diamond's attempt to subdivide the later period of wrongdoing neither relevant nor convincing. It does not appear that the conversation between Mr Tucker and Mr Diamond made a fundamental difference to Barclays' behaviour, given the repeated instances of 'low-balling' submissions to the LIBOR fixing process by Barclays set out in the FSA Final Notice covering the year running up to the phone call between Mr Tucker and Mr Diamond.**

9. Barclays may well not be alone. Nor is it likely to be a London-based phenomenon. The FSA is continuing to investigate the conduct of seven other banks in relation to LIBOR—some of them non-UK based banks. The FSA's regulatory counterparts in several other countries are also conducting their own investigations.[11] **Barclays is just one of many international banks under investigation for possible market manipulation. It is important that Barclays' serious shortcomings should not be seen in isolation from the possible actions of other banks and we await the results of ongoing investigations.**

10. In addition, the Serious Fraud Office (SFO) announced on 6 July 2012 that it had "decided formally to accept the LIBOR matter for investigation".[12] Mr Tucker told us that contingency planning was going on to examine whether "the class action suits [against banks] ... cause such financial damage to the firms that it could undermine stability ... [P]eople are starting to think about that too".[13]

Barclays' co-operation with regulators and early settlement

11. If it proves to be the case that other banks have been guilty of similar misconduct, then Barclays may well have suffered from 'first mover disadvantage'. It has taken the initial brunt of criticism because it settled first and so has been the first bank to have been found guilty of misconduct. Barclays is to be commended for co-operating fully with the regulators' inquiries. The FSA took this into account when determining the penalty:

> The FSA has also considered the nature and extent of the co-operation provided by Barclays during the course of its investigation. The FSA acknowledges that Barclays has provided extremely good co-operation, in particular in providing access to evidence and facilitating voluntary witness interviews which were conducted by the FSA together with overseas authorities. The FSA's investigation would have taken much longer to conclude without Barclays' co-operative approach.[14]

Tracey McDermott told us that Barclays had "bent over backwards to try to move this forward" and had been "extremely co-operative".[15] The US CFTC, similarly, recognised

10 Q 21

11 Qq 1167–8; HC Deb, 28 June 2012, col 463

12 *LIBOR: SFO to investigate*, SFO press release, 6 July 2012

13 Q 495

14 FSA Final Notice, 27 June 20112, para 208

15 Q 1113

Barclays' "significant co-operation during the Division of Enforcement's investigation of this matter, which included providing important information and analysis to the Division that helped the Division efficiently and effectively undertake its investigation".[16]

12. Barclays' former Chief Executive, Bob Diamond, told us:

> Clearly there was behaviour that was reprehensible; but as soon as this was recognised Barclays put all forces—if there's a mistake, if there's a problem, how do we handle it? What do we do about it? At Barclays it has been three years with three of the most important regulatory agencies in the world looking at millions of files; and all three regulatory agencies applauding Barclays for its co-operation, analysis and proactivity. We hired two external firms to work with two members of senior management, reporting to the chairman of the board and the chairman of the audit committee. The attitude of Barclays three years ago when this was recognised was, "Let's get to the bottom of it. Let's identify the problem; take the actions necessary; learn our lessons and, if any of our customers and clients got hurt, let's make them good." That attitude is recognised by the three regulatory agencies in what they wrote, but it is not coming out in the court of public opinion over the past week.[17]

Mr Agius, Barclays' Chairman, told us:

> What happened, as we all are in complete common agreement on, was abhorrent and should not have happened. Barclays, when it was first told about the inquiries, co-operated with them. As the inquiries evidently became more serious, our degree of co-operation increased. No one could have co-operated more. We spent as a bank more than £100 million in checking emails and translating Japanese, and so on and so forth. We could not have done more, and that is acknowledged in the submissions of the agencies.
>
> Once we got to the point of settlement, we also recognised that we would have first-mover disadvantage. We could have dragged our heels; that would not have been right. We feel we did the right thing.[18]

Mr Agius also made clear that Mr Diamond was not involved in any consideration by Barclays of the regulators' inquiries into LIBOR: "Because he was a potential witness, he was excluded from all considerations of these matters [...] he was simply aware that there was an inquiry into LIBOR".[19]

13. However, despite these statements from Mr Diamond and Mr Agius **it is important to state that Barclays' internal compliance department was told three times about concerns over LIBOR fixing during the period under consideration and it appears that these warnings were not passed to senior management within the bank. Statements that**

16 CFTC Order, page 4

17 Q 1

18 Q 653

19 Qq 788–9

everything possible was done after the information came to light must be considered against a background of serious failures of the compliance function within the bank. In other words, the senior management should have known earlier and acted earlier.

14. It is noteworthy that the identification of this first period of wrongdoing—the manipulation of submissions in order to benefit traders—came from Barclays' own investigation into the later period of LIBOR fixing during the crisis for Barclays' own benefit. Mr Agius told us that:

> The LIBOR inquiry was into the low-balling, to use the expression that seems to be current in this Committee. The CFTC started that inquiry into low-balling. We co-operated with that. As we searched through our records, as we searched through our emails and searched through our voice recordings, we discovered the criminality, to use your expression. Instead of sitting on that, we naturally disclosed that, and we in fact then turned up the volume, or whatever the expression is, on the low-ball activity we did to see just how much we could uncover, and we left no stone unturned.[20]

15. Asked whether Barclays had been unfairly hit by first-mover disadvantage, Lord Turner, Chairman of the FSA, responded:

> I think what has happened is entirely fair, in the sense that a process has gone through that has led to this final notice, and that has recorded the fact that it was attempting to manipulate in two different ways in the two different periods, and it accepted that and agreed to it. I do not think that is unfair. In fairness, it is important [...] to record as a balance to that that it was very co-operative with us.[21]

16. **Barclays received a reduction in its fine because of its high degree of co-operation with the FSA in its investigation. Barclays also disclosed wrongdoing that it had itself found to the regulators. Any such disclosure is likely to have carried serious risk of reputational damage. Co-operation with inquiries needs to be encouraged by regulators, who need to take into account first mover disadvantage, but it does not excuse or diminish wrongdoing. Nor does the fact that others may have been engaged in similar practices. The FSA and its successors should consider greater flexibility in fine levels, levying much heavier penalties on firms which fail fully to co-operate with them. The FSA needs to give high priority to its investigations into other banks, including those largely owned by the taxpayer.**

17. **Firms must be encouraged also to report to the regulator instances they find of their own misconduct. While such a firm should still be required to pay compensation to any other party who has been disadvantaged by the misconduct, in cases where a firm makes a complete admission of its own culpability the FSA should retain flexibility in setting the fine payable. The FSA should have regard to the desirability of encouraging other firms to confess their misdemeanours in a similar way. The FSA may also need to re-examine its treatment of whistleblowers, both corporate and individual, in order to provide the appropriate incentives for the reporting of wrongdoing.**

20 Q 786

21 Q 1115

18. The findings of the regulators have been a reputational disaster for Barclays. They have led directly to the loss of its Chief Executive and its Chief Operating Officer. These resignations were preceded by the announcement of the resignation of its Chairman, who subsequently decided to stay in post until he had overseen the appointment of a new Chief Executive. The resignations at Barclays are considered in section 6 of this Report.

19. The findings have focussed pre-existing public anger with banks. Barclays is one of many instititutions that have contributed to the state of banking's reputation. LIBOR has followed the vast public bailouts of banks during the financial crisis, the liquidity support and guarantees given to all banks and the apparent lack of penalties for those who contributed to that crisis, most of whom retained very high levels of remuneration even after 2008. More recently there has been the scandal of payment protection insurance (PPI) mis-selling, criticism of banks' perceived reluctance to lend, complaints about the sale of unsuitable and complex interest rate swap products to businesses (which are under investigation by the FSA), and serious IT failures at RBS Group. The economy needs well-functioning banks. They will have a crucial role in any economic recovery through their lending to businesses and households. An end to crude 'banker bashing' would be highly desirable, but bankers must recognise that they have brought much of this upon themselves through actions which have seriously damaged public confidence. While banks continue to provide evidence that wrongdoing persists the popular mood is likely to remain hostile.

Policy responses

20. On 2 July 2012 the Chancellor of the Exchequer announced a review ('the Wheatley review') by the FSA of LIBOR:

> I have today asked Martin Wheatley, the chief executive designate of the Financial Conduct Authority, to review what reforms are required to the current framework for setting and governing LIBOR. This will include looking at whether participation in the setting of LIBOR should become a regulated activity, at the feasibility of using actual trade data to set the benchmark, and at making initial recommendations on the transparency of the processes surrounding the setting and governance of LIBOR.
>
> The review will also look at the adequacy of the UK's current civil and criminal sanctioning powers, with respect to financial misconduct and market abuse with regard to LIBOR. It will also assess whether those considerations apply to other price-setting mechanisms in financial markets, to ensure that these kinds of abuses cannot occur elsewhere in our financial system. We need to get on with this, and not spend years navel-gazing when we know what has gone wrong. I am therefore pleased to tell the House that Mr Wheatley has agreed to report this summer so that the Financial Services Bill currently before Parliament—or, if necessary, the future legislation on banking reform—can be amended to give our regulators the powers they clearly need.
>
> The review is essential to ensuring that we mend the broken regulatory system—introduced by the last Government—that allowed these abuses to happen, but the

> manipulation of the most used benchmark interest rate reveals the broader issue of the professional standards and of the culture in some parts of the financial services industry that was allowed to grow up in the years before the crisis and which still needs to change.[22]

On 30 July 2012 the Treasury announced the detailed terms of reference of the Wheatley review:

> The Wheatley review will formulate policy recommendations with a view to:
>
> 1. Reforming the current framework for setting and governing LIBOR. This work should, inter alia, consider:
>
> whether participation in the setting of LIBOR should be brought into the regulatory perimeter under the Financial Services and Markets Act 2000 as a regulated activity;
>
> How LIBOR is constructed, including the feasibility of using of actual trade data to set the benchmark;
>
> The appropriate governance structure for LIBOR;
>
> The potential for alternative rate-setting processes;
>
> The financial stability consequences of a move to a new regime and how a transition could be appropriately managed.
>
> Determining the adequacy and scope of sanctions to appropriately tackle LIBOR abuse. This work should consider:
>
> 2. The scope of the UK authorities' civil and criminal sanctioning powers with respect to financial misconduct, particularly market abuse and abuse relating to the setting of LIBOR and equivalent rate-setting processes; and the FSA's approved persons regime and investigations into market misconduct.
>
> 3. Whether similar considerations apply with respect to other price-setting mechanisms in financial markets, and provide provisional policy recommendations in this area.

The review will report by the end of the summer to enable the Government to consider recommendations with a view to taking legislative changes forward through the Financial Services Bill, which is currently being scrutinised in the House of Lords. The review will aim to publish its conclusions by the end of September.[23]

21. Parliament has also instigated a review. On 16 July, the House of Commons created a Parliamentary Commission on Banking Standards to consider and report on:

22 HC Deb, 2 July 2012, cols 612–3

23 HM Treasury press release, *The Wheatley Review*, 30 July 2012

> Professional standards and culture of the UK banking sector, taking account of regulatory and competition investigations into the LIBOR rate-setting process;
>
> Lessons to be learned about corporate governance, transparency and conflicts of interest, and their implications for regulation and for Government policy.[24]

In response to the request from the House of Commons, the House of Lords appointed its five members to the Commission on 17 July 2012.[25]

22. On 25 July 2012 the European Commission put forward amendments to proposals for a Regulation and a Directive on insider dealing and market manipulation. The Commission intends that these will "clearly prohibit the manipulation of benchmarks, including LIBOR and EURIBOR, and make such manipulation a criminal offence". Internal Market and Services Commissioner Michel Barnier said:

> The international investigations underway into the manipulation of LIBOR have revealed yet another example of scandalous behaviour by the banks. I wanted to make sure that our legislative proposals on market abuse fully prohibit such outrages. That is why I have discussed this with the European Parliament and acted quickly to amend our proposals, to ensure that manipulation of benchmarks is clearly illegal and is subject to criminal sanctions in all countries.[26]

Committee inquiry

23. In our inquiry we have taken evidence from senior figures in Barclays: Mr Bob Diamond, former Chief Executive, Mr Marcus Agius, Chairman, and Mr Jerry del Missier, former Chief Operating Officer. We held an evidence session with FSA representatives: Lord Turner of Ecchinswell, Executive Chairman, Mr Andrew Bailey, head of the Prudential Business Unit of the FSA, and Tracey McDermott, acting director of Enforcement and Financial Crime. We also heard evidence from Sir Mervyn King, Governor of the Bank of England, and Mr Paul Tucker, Deputy Governor. We thank all the witnesses for making themselves available to give evidence at short notice. The Committee has taken extensive written evidence from many of these witnesses, and from other people and organisations. We are also very grateful for the assistance of our specialist advisers Bill Allen, Jonathan Fisher QC, John Willman and Professor Geoffrey Wood.[27]

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24 Votes and Proceedings, 16 July 2012

25 HL Deb, 17 July 2012,col 109. The membership of the Commission is: Mr Andrew Tyrie MP (Chairman; *Con*), Mark Garnier MP (*Con*), Andrew Love MP (*Lab/Co-operative),* Rt Hon Pat McFadden MP (*Lab*), John Thurso MP (*Lib Dem*), The Lord Bishop of Durham (*Non-Affiliated*), Baroness Kramer (*Lib Dem)*, Rt Hon Lord Lawson of Blaby (*Con),* Rt Hon Lord McFall of Alcluith (*Lab/Co-op*), Lord Turnbull KCB CVO (*Crossbench*)

26 European Commission press release, 25 July 2012, *Libor scandal: Commission proposes EU-wide action to fight rate-fixing*

27 William Allen declared the following interests: I am a financial and economic consultant, and also undertake academic work related to the recent financial crisis and bank regulation. I have two current consultancy contracts. One is with a company called Ad Satis Ltd (their internet site is http://www.adsatis.com/). Ad Satis itself provides consultancy services to banks, and the contract is to provide them with pieces of research on bank regulation. The other is with British Empire and General Securities Trust, is an investment trust. I also undertake occasional consultancy work for the International Monetary Fund. I do occasional lecturing and course-organising work, mainly for Cass Business School (where I am a visiting fellow), for which I get paid. I write occasional articles for publication for which I may get paid.

24. This Report draws conclusions from the evidence that we have heard and highlight issues for further consideration by Parliament, Government and regulators.

Jonathan Fisher QC declared the following interests: Practising barrister (Devereux Chambers, Temple, London) specialising in financial crime cases, Visiting Professor of Law, London School of Economics, teaching Corporate and Financial Crime, Honorary Visiting Professor, City Law School (City University London), teaching in Fraud and Financial Crime, General Editor, Lloyds Law Reports: Financial Crime, Committee member, IBA Anti-Money Laundering Forum, Honorary Steering Group Member, London Fraud Forum, Member, Commercial Fraud Lawyers Association, Member, Fraud Advisory Panel, Trustee Director, Fraud Advisory Panel, 2006–2010, Member, Criminal Bar Association, Member, Financial Services Lawyers Association, Member, Proceeds of Crime Lawyers Association.

John Willman declared the following interests: Pearson Pension Scheme beneficiary, PCS Pension Scheme beneficiary; shareholdings in: Pearson Group PLC, and Vitesse Media PLC; Editorial consultancy clients since leaving the FT in 2009: Foreign & Commonwealth Office, HM Treasury, Zurich Financial Services, The Boston Consulting Group, Financial Times Conferences, Policy Exchange, TheCityUK, CBI, PricewaterhouseCoopers, Pictet & Cie, BakerPlatt (Jersey legal and financial services firm), Rhone Trust & Fiduciary Services SA, TIMES Group, Winkreative, The Corporation of London, International Finance Corporation, Government Office for Science, London Business School; Speaking engagements since 2008: Blackrock, Bank of New York, Mellon, Experian, QAS, Cinven, Business & Politics, Trade Association Forum, Centaur Conferences, Atradius, AM Conferences, VWM, Glasgow, Man + Machine, WPA, Money Marketing Investment Alliance, North of England Education Conference, NE International Networking Club, Baker & MacKenzie; Political affiliations: Member of the Fabian Society

Professor Geoffrey Wood declared the following interests: Director, Hansa Trust, Member, Investment Advisory Panel, Strathclyde Pension Fund, Member and Adviser, PI Capital (private equity group), and Adviser, Elliot Advisers.

2 Manipulation by individuals with the intention of personal benefit

The misconduct

25. The FSA found that between January 2005 and July 2008 Barclays was in breach of the FSA's principle 5 "by making US dollar LIBOR and EURIBOR submissions which took into account requests made by its interest rate derivatives traders".[28] This phase of LIBOR manipulation differed from that discussed later in this Report, as it centred on a group of traders attempting "to benefit their own trading positions", rather than acting in the immediate financial interests of Barclays overall.[29]

26. Barclays' traders were aware of how even small movements in LIBOR or EURIBOR would be of benefit to them, with the FSA noting that "Barclays' Derivatives Traders knew on any particular day what their books' exposure to a one basis point (0.01%) movement in LIBOR or EURIBOR was".[30] Because of the central role LIBOR and EURIBOR played in how derivatives contracts were drawn up, the attempted manipulation of these reference rates "could have made the Derivatives Traders profit or reduced a loss".[31]

27. To alter the Barclays' LIBOR submission, and thus try and alter the overall LIBOR rate, the traders had to collude with those in Barclays who submitted the LIBOR figures (the submitters) to submit figures that were to the traders' benefit. In its investigation, the FSA identified that:

> between January 2005 and May 2009, at least 173 requests for US dollar LIBOR submissions were made to Barclays' Submitters (including 11 requests based on communications from traders at other banks);
>
> between September 2005 and May 2009, at least 58 requests for EURIBOR submissions were made to Barclays' Submitters (including 20 requests based on communications from traders at other banks); and
>
> between August 2006 and June 2009, at least 26 requests for yen LIBOR submissions were made to Barclays' Submitters.[32]

As we have seen, the traders knew that small changes in LIBOR could have large effects. The FSA noted that:

28 Financial Services Authority, Final Notice, 27 June 2012, para 8

29 Financial Services Authority, Final Notice, 27 June 2012, para 81

30 Financial Services Authority, Final Notice, 27 June 2012, para 48

31 Financial Services Authority, Final Notice, 27 June 2012, para 49. For a more detailed description of how Barclays' traders could have benefitted, please see Financial Services Authority, Final Notice, 27 June 2012, paras 49–51

32 Financial Services Authority, Final Notice, 27 June 2012, para 56

> For example in a telephone call on 12 September 2007, the Submitter indicated that Barclays' Derivatives Traders had an interest in high three month LIBOR submissions '*for about a couple of million dollars a basis point. Ah, but I don't know how much longer I'm gonna be able to keep it up at seventy seven*'. [33]

The Governor of the Bank of England noted that:

> I was very struck and surprised, when reading these three reports [from the regulatory authorities], to discover that changing LIBOR by one basis point was the kind of rigging that people were interested in. You would never have noticed that from market activity. We were worried about tens of basis points.[34]

The Committee was surprised and disappointed by the Governor's remarks, given the scale of the value of a single basis point, notwithstanding that the Bank of England did not have statutory regulatory powers.

28. Barclays as a whole, though, would not necessarily have benefited from the actions of its traders. Mr Diamond denied that the traders acted on behalf of Barclays. He told us that: "They [the traders] were acting on behalf of themselves. It is unclear whether it benefited Barclays but I don't think they had any interest in benefiting Barclays, they were benefiting themselves".[35] Jerry del Missier, former Chief Operating Officer of Barclays, when asked how a trader would benefit their own bonus by asking submitters to falsify the LIBOR submissions, noted the complexity of what the traders were trying to achieve, and how the outcome might not be to Barclays' benefit:

> It is very complex, and it is not entirely obvious that you are actually benefiting your own profitability, but the theory would be that if you got a certain rate submitted, the book that you were trading would benefit from that submission. It is important to understand that it is not even the whole bank—it is one particular book. On any given day, the bank does not know whether it benefits from high rates or low rates but, again, because of the complexity of the averaging process, it is extremely difficult to see how one rate would have an impact, and then how that would necessarily flow through to compensation is very convoluted.[36]

Lord Turner, Chairman of the FSA, emphasised the difficulty of proving how far the traders had benefitted individually. While he said it wasn't impossible, he noted that "That would be a very complicated thing to do, because you would have to work out what they would have put in when they did not put this in, and then you have to work out what that would have done to the average".[37] When asked whether the traders had been successful, Lord Turner told us that:

33 Financial Services Authority, Final Notice, 27 June 2012, para 164

34 HC (2012-13) 535, Q 78

35 Q 122

36 Q 1024

37 Qq 1110–1111

> The fact is that although it is very difficult to work out exactly what would have changed with the LIBOR rate if they had not been manipulating, you have to assume [...] that if someone had been induced to put in a higher figure than they otherwise would, LIBOR must have been at least some small bit higher, and you have to assume, as you say, that these traders were not entirely irrational, or that they believed that they were having an influence. Of course, the crucial issue here is that we are dealing in the derivatives market, with an environment in which minute movements in the LIBOR rate might have a very significant impact on very specific positions that they were holding at that time. That is somewhat different from, for instance, the consumer market, where single basis point movements would be unlikely to have a really material effect on, say, the cost of a mortgage.[38]

29. Other commentators believed that the actions of single submitting institutions could influence the overall rate. On 16 July 2012 Bloomberg carried a report showing how individual traders sought to do this. The Bloomberg report said, "By making a submission too high to be included in the average, a single lender can push a previously excluded rate back into the pack to send the average higher. By submitting a rate that falls too low to be included, the average can be nudged down as a previously excluded rate re-enters the pack."[39]

Collusion with traders at other banks

30. More worryingly, the FSA found that this misconduct, on occasion, was not limited to Barclays and extended to other banks. The Final Notice emphasised the benefits of such collusion with other banks. It stated that:

> Where Barclays made submissions which took into account the requests of its own Derivatives Traders, or sought to influence the submissions of other banks, there was a risk that the published LIBOR and EURIBOR rates would be manipulated. Barclays could have benefited from this misconduct to the detriment of other market participants. Where Barclays acted in concert with other banks, the risk of manipulation increased materially.[40]

31. Since the enforcement procedures on other banks continue, it is difficult to assess how far there was collusion between banks, but in its Final Notice, the FSA indicated that:

> At least 12 of the US dollar LIBOR requests made to Barclays' Submitters were made on behalf of external traders that had previously worked at Barclays and were now working at other banks (although those banks did not contribute US dollar LIBOR submissions).[41]

And that:

38 Q 1112

39 Bloomberg, *Libor flaws allowed banks to rig rates without conspiracy*, 16 July 2012

40 Financial Services Authority, Final Notice, 27 June 2012, para 11

41 Financial Services Authority, Final Notice, 27 June 2012, para 82

> At least 20 of the EURIBOR requests made by the Derivatives Traders were made on behalf of traders at other banks that contributed EURIBOR rates. Barclays' Derivatives Traders passed on the requests of these other traders to Barclays' Submitters, even blind copying in the external traders to their emails in order to demonstrate they had done so. [42]

The FSA also found that:

> Barclays' Derivatives Traders attempted to influence the EURIBOR (and to a much lesser extent, US dollar LIBOR) submissions of other banks by making requests to external traders. One of the Derivatives Traders also embarked on co-ordinated strategies to align Barclays' positions with traders at other banks and to influence the EURIBOR rates published by the EBF.
>
> Between February 2006 and October 2007, Barclays' Derivatives Traders made at least 63 requests to external traders with the aim that those traders would pass on the requests for EURIBOR and US dollar LIBOR submissions to their banks' submitters. 56 of those requests related to EURIBOR submissions. Five Derivatives Traders made the requests to external traders. [43]

32. We asked witnesses what this behaviour meant about the culture of Barclays, and of the banking industry more widely. The Final Notice by the FSA paints a picture of a close-knit group of people collude to try to manipulate LIBOR. For instance, the following conversations are noted:

> Trader C requested low one month and three month US dollar LIBOR submissions at 10:52 am on 7 April 2006 (shortly before the submissions were due to be made); "*If it's not too late low 1m and 3m would be nice, but please feel free to say "no"... Coffees will be coming your way either way, just to say thank you for your help in the past few weeks*". A Submitter responded "*Done…for you big boy*".[44]
>
> on 26 October 2006, an external trader made a request for a lower three month US dollar LIBOR submission. The external trader stated in an email to Trader G at Barclays "*If it comes in unchanged I'm a dead man*". Trader G responded that he would "*have a chat*". Barclays' submission on that day for three month US dollar LIBOR was half a basis point lower than the day before, rather than being unchanged. The external trader thanked Trader G for Barclays' LIBOR submission later that day: "*Dude. I owe you big time! Come over one day after work and I'm opening a bottle of Bollinger*". [45]

Lord Turner said that actions over this period indicated a cultural weakness within Barclays. Referring to the period in which the rogue traders operated, he noted that:

42 Financial Services Authority, Final Notice, 27 June 2012, para 84

43 Financial Services Authority, Final Notice, 27 June 2012, paras 88–89

44 Financial Services Authority, Final Notice, 27 June 2012, para 65

45 Financial Services Authority, Final Notice, 27 June 2012, para 83

> Nevertheless, there does seem to have been a culture that allowed this to occur. One of the shocking things about this is that on some occasions, the derivatives trader is not asking the submitter to change his submission on the basis of a hidden phone call or a note that he believes is hidden, but by shouting it across the trading floor. That suggests something is deeply wrong with the culture that could possibly have allowed that to occur.[46]

33. Mr Diamond though was keen to emphasise that this phase of wrong-doing was limited to a small set of Barclays' employees. He said that "It was 14 traders [...]. We have a couple of thousand traders."[47] A similar view was also expressed by Mr Agius, who when asked whether Barclays was in denial over the scale of the problem, replied:

> No, not in denial of the scale of it, because although it went on for a long period of time, it was undetected. It should have been detected and should never have happened in the first place—all of that is absolutely clear—but it was not endemic across the whole bank. It was isolated in one area that was under-monitored [...]. That does not excuse it.[48]

Lord Turner accepted that "I think it is probably the case that the total number of people identified in this investigation and others will end up as a relatively small number."[49] He did however also accept when questioned that some traders may not have been caught:

> ***Stewart Hosie:*** [...] In terms of the traders who have been caught, it was because they left an electronic trail. If they speak informally orally in the pub, outwith the recorded net, there could be many more. Is this the tip of an iceberg?
>
> ***Lord Turner:*** Almost by definition, I don't know, because I only know what we are capable of finding out. I would be amazed if it is everything, precisely for the reasons you suggest. If people are acting in a way that leaves a legally identifiable trail, it would be very surprising if there are not other activities without a legally identifiable trail. We know in general that market abuse or manipulation of any category is incredibly difficult to spot, because often people are clever enough to do it in a verbal, off-the-record, off-the-legal-trail basis.[50]

On 2 July 2012, Barclays announced that it would undertake a review of its business practices.[51] On 24 July 2012, following our hearings, Barclays announced the terms of reference of a review to be led by Anthony Salz, Executive Vice Chairman of Rothschild:[52]

46 Q 1094

47 Q 137

48 Q 668

49 Q 1094

50 Q 1095

51 Barclays PLC, Anthony Salz to lead independent business practices review, 24 July 2012

52 Barclays PLC, Anthony Salz to lead independent business practices review, 24 July 2012

> The global review will assess the bank's current values, principles and standards of operation and determine to what extent those need to change; test how well current decision-making processes incorporate the bank's values, standards and principles and outline any changes required; and determine whether or not the appropriate training, development, incentives and disciplinary processes are in place.[53]

The opening words of the terms of reference of this are: "The culture of the banking industry overall, and that of Barclays within it, needs to evolve.[54] Not only Barclays has recognised the need for a change in culture. Stephen Hester, Chief Executive of RBS, stated that "At RBS we have our share of problems to correct from the past and just as we are working hard at putting our financial weaknesses behind us, so too must we cement cultural change."[55]

34. **The actions that have so far been discovered of Barclays and other traders were disgraceful. As the FSA's Final Notice states, the attempted manipulation of LIBOR "created the risk that the integrity of LIBOR and EURIBOR would be called into question and that confidence in or the stability of the UK financial system would be threatened". This attempted manipulation of LIBOR should not be dismissed as being only the behaviour of a small group of rogue traders. There was something deeply wrong with the culture of Barclays. Such behaviour would only be possible if the management of the bank turned a blind eye to the culture of the trading floor. The incentives and control systems of Barclays were so defective that they incentivised traders to benefit their own book irrespective of the impact on shareholders and the bank's overall performance. Now exposed, their actions are to the detriment of Barclays' reputation and the reputation of the industry. The standards and culture of Barclays, and banking more widely, are in a poor state. Urgent reform, by both regulators and banks, is needed to prevent such misconduct flourishing.**

The failure of internal controls

35. We asked why this wrong-doing by traders had not been caught earlier. Although the Final Notice included references by traders to the need to keep their actions secret,[56] other, more blatant, behaviour was also detected. For instance, the FSA report noted, and Lord Turner referred in oral evidence to, the fact that "At least one Derivatives Trader at Barclays would shout across the euro Swaps Desk to confirm that other traders had no conflicting preference prior to making a request to the Submitters".[57]

36. Mr Diamond confirmed that desk supervisors would have known that this type of behaviour was wrong.[58] He also confirmed that it was their responsibility to report such

53 Barclays PLC, Anthony Salz to lead independent business practices review, 24 July 2012

54 Barclays PLC, The Salz Review of Barclays Business Practices – Terms of Reference, 24 July 2012

55 Daily Mirror, 'You are right to be angry with banks, but none of us can afford to give up on them': Stephen Hester's message to readers on banking crisis, 3 July 2012

56 For example, Financial Services Authority, Final Notice, 27 June 2012, Para 93

57 Q 1094; Financial Services Authority, Final Notice, 27 June 2012, Para 54

58 Q 154

behaviour to their supervisors and compliance, but that this had not happened.[59] Mr Agius provided the following detail on the compliance function at Barclays following his appearance:

> • Compliance functions in the investment bank and across Barclays have dual reporting lines, both within the business and to the Group Head of Compliance.
>
> • The Group Head of Compliance reports to our Group General Counsel, who in turn reports directly to the Chief Executive.
>
> • The Chief Executive and Finance Director are the two executive directors on the Board.
>
> • The Group Head of Compliance provides regular Compliance reports to the Group Governance and Control Committee, the Board Audit Committee and the Executive Committee.
>
> • There was a failure within the Investment Bank Compliance team to escalate information about the LIBOR-related issues either within the business or to the Group Head of Compliance.[60]

Having needed "notice" for some of our questions when he appeared before us,[61] and therefore having checked the facts, Mr Agius told us that Barclays had added a compliance presence on the trading floor during mid-2009.[62] Mr Agius provided the following explanation as to why Barclays had not thought of LIBOR as a risk prior to the investigation:

> In any bank, as well as the people who do the business, you have people who control and manage what is called the compliance function. The compliance function is there to ensure that the bank acts at all times within the regulatory constraints under which it is due to operate. It is not a practical proposition that every single individual is monitored at every single minute of his or her working day. That is simply not practical. What happens is that compliance is constructed around areas where risk is perceived to lie, and the riskier the area of the bank or the activity, the greater the levels of compliance and oversight.
>
> For many years, the activities of the LIBOR market were seen to be low-risk because the passage of the LIBOR rate was very constant, the spreads were very narrow and very little happened. Separately, because of the way the LIBOR rate is struck—with 16 banks submitting, the top four taken off, the bottom four taken off and an average taken—the chances of anybody manipulating the rate successfully were deemed to be very low. As we heard yesterday from other testimony, as the credit crisis occurred,

59 Q 158

60 Letter from Marcus Agius to the Chairman of the Treasury Committee, 20 July 2012

61 Qq 799, 801–802

62 Letter from Marcus Agius to the Chairman of the Treasury Committee, 20 July 2012

> the behaviour of LIBOR departed from its historic patterns and, evidently, that led to an opportunity for risk and for people to take advantage of that.
>
> We should have changed our compliance in recognition of that. We were behind the curve and that is most unfortunate, but it explains why these things were allowed to happen, why they were not detected and why more attention was not brought to our level at an earlier stage. It does not excuse any of it, but I seek to give an explanation as to what happened.[63]

37. However, in its Final Notice, the FSA noted that on 12 September 2007 an email from a manager raised questions with Barclays' Compliance in relation to Barclays' obligations and LIBOR setting.[64] That email specifically referred to interest rate derivative contracts, and the Barclays' manager stated that "Although there are contracts that reset everyday, Monday is particularly important as all of the 3 month futures contracts fix".[65] Despite this email, Compliance at Barclays failed to take any action. The FSA Final Notice recorded that:

> Compliance agreed to draft a policy and some procedures which would ensure that Barclays' Submitters were not aware of the firm's overall exposure to LIBOR. After considering the issue further, Compliance concluded there was no risk of the Submitters becoming aware of the firm's overall exposure to LIBOR. Compliance considered at that time whether any information barriers between Barclays' Submitters and any other area of the bank were required.
>
> Compliance concluded that no such information barriers were necessary, even though there was a potential conflict of interest between Barclays' Submitters and its Derivatives Traders. However, Compliance did not query the reference to derivatives contracts in Manager E's email on 12 September 2007. No questions were asked of Manager E or the Submitters in relation to this issue, no action was taken by Compliance and no systems and controls were put in place to deal with the potential conflict.[66]

38. **The attempted manipulation of Barclays' LIBOR submissions with the intention of personal gain continued for four years. It is shocking that it flourished for so long. Any system may fail for a short period, but compliance at Barclays was persistently ineffective. Even when Barclays' compliance had indications that something was awry, it failed to take the opportunity to strengthen the bank's controls. Nor was there any pressure from senior executives within Barclays to ensure that effective LIBOR controls were in place, as it was considered low-risk, in particular where LIBOR setters sat, with no presence of the compliance function. These are serious failures of governance within Barclays, for which the board is responsible. The compliance function within a bank is**

63 Q 648

64 Financial Services Authority, Final Notice, 27 June 2012, Para 165

65 Financial Services Authority, Final Notice, 27 June 2012, Para 165

66 Financial Services Authority, Final Notice, 27 June 2012, Paras 166–167

very important. If it is weak or ignored in the practices of the bank that is reflective of a poor culture which does not take seriously enough abiding by the rules essential to proper functioning of the bank and the wider financial system. The serious failings of the compliance function during the period under examination suggest there was this kind of culture at Barclays.

39. **During this period of extremely weak compliance at Barclays, it was nonetheless subject to extensive regulatory oversight by the FSA. Despite the numerous ARROW visits that were conducted by the FSA during this period, we have seen no evidence that this weakness in compliance elaborated in the Final Notice was identified by the FSA in a timely manner, still less, dealt with. The FSA must report to this Committee on how it will alter its supervisory efforts to counter such weak compliance in future.**

3 Manipulation during the financial crisis

Background

40. In 2007, significant strains began to appear within the inter-bank funding markets. Table 1, adapted from the March 2009 Turner Review, highlights the key issues faced by banks during this period.

Table 1: Stages of the Crisis: 2006-2009

2006 – Summer 2007 Localised credit concerns	Rising defaults in US subprime loans. Expectations of property prices fall.
Summer – Autumn 2007 Initial crack in confidence and collapse of liquidity	Failure of 2 large hedge funds. Spreads in inter-bank funding and other credit products rise sharply. Inter-bank funding for second tier banks dries up. Northern Rock faces retail run.
Autumn 2007 – early Summer 2008 Accumulation of losses and continuation of liquidity strains	Severe mark-to-market losses in trading books. Collapse of commercial paper markets. Funding strains in the secured financing market. Worries about liquidity of major institutions. Government-assisted rescue of Bear Stearns.
Summer 2008 Intensification of losses and liquidity strains	Mark-to-market losses and liquidity strains continue to escalate. Housing market problems recognised as widespread in UK, US and other countries, as house prices fall and supply of credit dries up. Funding problems of UK mortgage banks intensify.
September 2008 Massive loss of confidence	Bankruptcy of Lehmans breaks confidence that major institutions are too big to fail. Credit downgrade of AIG triggers rising collateral calls, requiring government rescue. Mix of credit problems, wholesale deposit runs and incipient retail deposit runs lead to collapse of Washington Mutual, Bradford & Bingley, and Icelandic banks. Almost total seizure of interbank money markets; major banks significantly reliant on central bank support.
October 2008 Government recapitalisation, funding guarantees and central bank support	Exceptional government measures to prevent collapse of major banks; explicit commitments that systemically important banks will not be allowed to fail.
November 2008 ➔ Feedback loops between banking system and economy. Further government measures to offset feedback loop risk.	Impaired bank ability to extend credit to real economy produces major globally synchronised economic downturn. Recession threatens further credit losses which might further impair bank capital. Asset Protection Scheme.

Source: Adapted from Financial Services Authority, The Turner Review, March 2009, Box 1B, p27

41. In the face of these pressures in the inter-bank lending markets, Mr Tucker, emphasised the importance of LIBOR to the authorities. He explained that:

> [...] what is important from quite early in the crisis, from the summer of 2007 onwards, is that LIBOR became increasingly used as a summary statistic of what was going on in the market. I think there are two reasons. First of all, LIBOR diverged

> from the safe rate of interest in a material way for the first time in living memory. Secondly, we became aware as the weeks and months passed that less money market activity was going via the brokers, more was being done bilaterally. Those are circumstances where everybody has less information about what is going on, and in those circumstances you place greater weight on the indicator that is available every day, which was LIBOR. I think everybody rather slipped into the habit of using LIBOR as a kind of portmanteau term for money market conditions, bank funding conditions, actual submissions, the actual LIBOR fix, and actually I think that is going on today.[67]

42. The individual LIBOR submissions of the banks, rather than the aggregated headline LIBOR figure, were also becoming important markers of the health of individual banks. On 3 September 2007, Bloomberg published an article entitled "Barclays Takes a Money Market Beating".[68] This article highlighted Barclays' high LIBOR fixing relative to other banks in the LIBOR panel, and posed the question "So what the hell is happening at Barclays and its Barclays Capital securities unit that is prompting its peers to charge it premium interest rates in the money market?".[69]

43. This article would mark the start of a second phase of LIBOR manipulation by Barclays. In this phase, Barclays attempted to manipulate its LIBOR submissions to prevent it being singled out when compared to other banks in the LIBOR panel. The FSA's Final Notice stated that "Senior management's concerns in turn resulted in instructions being given by less senior managers to Barclays' Submitters to reduce LIBOR submissions in order to avoid further negative media comment".[70] Mr Diamond confirmed that these senior management were from Barclays' Group Treasury.[71] The FSA's Final Notice said that:

> Concerns about the media perception of high LIBOR submissions continued at intervals for the remainder of 2007 and throughout 2008. At times of particular market stress this resulted in instructions being given to Barclays' LIBOR Submitters to reduce Barclays' submissions such that they did not stand out too far from the submissions of other contributing banks. This was expressed by Manager D (in Barclays' Group Treasury) as an instruction that Barclays should not "*stick its head above the parapet*" in terms of its LIBOR submissions.[72]

It should be noted Barclays is not alone. FSA investigations continue against seven other banks, including some non-British banks.[73]

67 Q 354

68 Bloomberg, Barclays Takes a Money-Market Beating: Mark Gilbert (Update1), 3 September 2007

69 Bloomberg, Barclays Takes a Money-Market Beating: Mark Gilbert (Update1), 3 September 2007

70 Financial Services Authority, Final Notice, 27 June 2012, Para 112

71 Qq 127, 129

72 Financial Services Authority, Final Notice, 27 June 2012, Para 115

73 Qq 1167–1168

Media and academic concern about LIBOR setting

44. Barclays' continuing manipulation of its own LIBOR setting took place against a background of media concern about the LIBOR setting process during the crisis. On 25 September 2007, an article by Gillian Tett in the *Financial Times* entitled "Libor's value called into question" noted the complaint of the Treasurer of one of the largest City banks that "The Libor rates are a bit of a fiction. The number on the screen doesn't always match what we see now".[74]

45. On 16 April 2008, the *Wall Street Journal* published an article called "Bankers cast doubt on Key Rate amid crisis" by Carrick Mollenkamp. This noted that:

> The concern: Some banks don't want to report the high rates they're paying for short-term loans because they don't want to tip off the market that they're desperate for cash. The Libor system depends on banks to tell the truth about their borrowing rates.[75]

However, the article also noted that there was no specific evidence to suggest false submissions were occurring.[76] On 29 May 2008, another Wall Street Journal article, "Study casts doubt on key rate", compared LIBOR submissions with the market for credit default swaps.[77] It provided the following analysis:

> In order to assess the borrowing rates reported by the 16 banks, the Journal crunched numbers from another market that provides a window into the financial health of banks: the default-insurance market. Until recently, the cost of insuring against banks defaulting on their debts moved largely in tandem with Libor—both rose when the market thought banks were in trouble.
>
> But beginning in late January [2008], as fears grew about possible bank failures, the two measures began to diverge, with reported Libor rates failing to reflect rising default-insurance costs, the Journal analysis shows. The gap between the two measures was wider for Citigroup, Germany's WestLB, the United Kingdom's HBOS, J.P. Morgan Chase & Co. and Switzerland's UBS than for the other 11 banks. One possible explanation for the gap is that banks understated their borrowing rates.[78]

74 Financial Times, Libor's value is called into question, by Gillian Tett, 25 September 2007

75 Wall Street Journal, Bankers Cast Doubt On Key Rate Amid Crisis by Carrick Mollenkamp, 16 April 2008

76 Wall Street Journal, Bankers Cast Doubt On Key Rate Amid Crisis by Carrick Mollenkamp, 16 April 2008

77 Wall Street Journal, Study Casts Doubt on Key Rate, By CARRICK MOLLENKAMP and MARK WHITEHOUSE, 29 May 2008

78 Wall Street Journal, Study Casts Doubt on Key Rate, By CARRICK MOLLENKAMP and MARK WHITEHOUSE, 29 May 2008

The article noted though that "The Journal's analysis doesn't prove that banks are lying or manipulating Libor".[79] On the same day, Bloomberg published an article, "Libor Banks Misstated Rates, Bond at Barclays Says", which started as follows:

> Banks routinely misstated borrowing costs to the British Bankers' Association to avoid the perception they faced difficulty raising funds as credit markets seized up, said Tim Bond, a strategist at Barclays Capital.
>
> "The rates the banks were posting to the BBA became a little bit divorced from reality," Bond, head of asset-allocation research in London, said in a Bloomberg Television interview. "We had one week in September where our treasurer, who takes his responsibilities pretty seriously, said: 'right, I've had enough of this, I'm going to quote the right rates.' All we got for our pains was a series of media articles saying that we were having difficulty financing."[80]

46. It was not only in the media where discussion of the potential for manipulation of LIBOR was occurring, as academics and international authorities also explored the weakness in the LIBOR setting process. A paper by Jacob Gyntelberg and Philip Wooldridge at the Bank for International Settlements (BIS) in the March 2008 BIS Quarterly Review noted that banks had a reason to misquote during funding crises:

> However, transparency raises questions about the information signalled by contributing banks through their quotes. There may be circumstances in which contributing banks deliberately choose to disclose biased quotes. If there is uncertainty about the liquidity position of a contributing bank, the bank will be wary of revealing any information that might add to this uncertainty for fear of increasing its borrowing costs.[81]

However, the BIS paper played down the possibility that there was fixing of the LIBOR submissions at work:

> In the US dollar market, the widening of Sibor and H.15 spreads over Libor is consistent with signalling by Libor contributor banks. However, many of the banks on the US dollar Libor panel are also on the euro Libor panel, and there are no signs that signalling distorted the latter fixing.[82]

Meanwhile, a working paper entitled "LIBOR Manipulation?" from August 2008, and referencing the Wall Street Journal articles, noted that:

79 Wall Street Journal, Study Casts Doubt on Key Rate, By CARRICK MOLLENKAMP and MARK WHITEHOUSE, 29 May 2008

80 Bloomberg, Libor Banks Misstated Rates, Bond at Barclays Says (Update2), By Gavin Finch and Elliott Gotkine ,May 29, 2008

81 Bank for International Settlements, Interbank rate fixings during the recent turmoil , Jacob Gyntelberg and Philip Wooldridge , March 2008 BIS Quarterly Review ,p 65

82 Bank for International Settlements, Interbank rate fixings during the recent turmoil , Jacob Gyntelberg and Philip Wooldridge , March 2008 BIS Quarterly Review ,p 70

> While statistical methods alone do not prove that manipulation has occurred in a particular market, some questionable patterns do exist with respect to the banks' daily Libor quotes. Our analyses of these apparent anomalies within the individual quotes suggest that the evidence is inconsistent with an effective manipulation of Libor. Nevertheless, the analyses presented in this study demonstrate that distinct non-random patterns of reported borrowing costs did exist during distinct periods of time, patterns that go beyond the findings that were originally reported by the Journal. In particular, for the period ending on August 8, 2009, the intraday variance of individual quotes is not statistically different from zero, and the banks deciding group for the Libor includes almost the entirety of the sixteen banks for a period of over seven months.[83]

In other words, the statistics did not show that manipulation of LIBOR was successful. But they did show that in several episodes LIBOR submissions were not behaving as they had when the market was functioning—they were very steady from day to day, and the quotes from different banks were very close together. This could readily be interpreted as the consequence of an attempt to make up a number that had to be available but could not be observed.

The role of the authorities

Concerns about LIBOR

47. Given the existence of the concerns over the LIBOR setting process, both in the media and academe, we asked why the regulators had not spotted the manipulation of submissions by Barclays earlier. The Governor of the Bank of England made the following observations:

> I did not say that fraud was restricted just to the rogue traders. It was also true that there was deliberate misrepresentation by Barclays in the submissions. On that, we had no evidence of wrongdoing. None was supplied to us. The evidence you cite—there were plenty of academic articles that looked in it and said that they could not see in the data any evidence of manipulation. I say again, if you go back to the inquiries that the regulators made, it took them three years to work out and find the evidence of wrongdoing. If it was so obvious and all in the newspapers and everyone was talking about it, one might ask why everybody did not say, "This is wrong." The reason was that it wasn't wrongdoing. It was a market that was dysfunctional and was not operating in any effective way.[84]

Paul Tucker noted that:

83 Abrantes-Metz, Rosa M., Kraten, Michael, Metz, Albert D. and Seow, Gim, LIBOR Manipulation? (August 4, 2008). Available at SSRN: http://ssrn.com/abstract=1201389 or http://dx.doi.org/10.2139/ssrn.1201389

84 HC (2012-13) 535, Q 112

> We didn't see it. I think there were other studies, including one by the BIS, although I think I am aware of this after the fact, that didn't conclude that it was a problem. Maybe we were just too focused on the financial crisis.[85]

The Sterling Money Markets Liaison Group

48. On 15 November 2007, the Bank of England hosted a meeting of the Sterling Money Markets Liaison Group. Present at the meeting were Paul Tucker as Chairman, several other representatives of the Bank of England, Douglas Hull from the FSA, as well as various representatives of banks, including Simon Chatterton as an alternate for Barclays. The minutes of that meeting record that:

> Several group members thought that Libor fixings had been lower than actual traded interbank rates through the period of stress. Libor indices needed to be of the highest quality given their important role as a benchmark for corporate lending and hedging, and as a reference rate for derivatives contracts.
>
> John Ewan (BBA) outlined the quality control and safeguard measures used by the BBA to ensure the quality of Libor. Dispersion between panel banks' submissions had increased during August but had since fallen back, in part reflecting clarification from the BBA on Libor definitions.[86]

49. In his evidence to us, Mr Tucker claimed that he had not taken the concerns expressed at the November 2007 Sterling Money Markets Liaison Group meeting as signs of dishonesty, but rather as a signal of dysfunction in the market. He explained that:

> [...] less [inter-bank lending] was going through the brokers, more was being done bilaterally, people did not know anything very much about each other's transactions at all, and so I heard this as, "They don't know what each other are doing." It was questioning the judgments that the different parties were making, or that they were relying on bilateral private transactions—I did not read this as cheating. And when John Ewan responded there was not then a great outcry in the room. People did not get in touch afterwards and say, "You've missed the point here."[87]

In Mr Tucker's supplementary evidence to the Committee, he provided more explanation as to why he did not believe the discussions noted in the minutes from the 15 November 2007 meeting indicated dishonesty:

> The BBA's rules do not require LIBOR submissions to be based on actual transactions, but require panel banks to answer the following question:
>
> *"At what rate could you borrow funds, were you to do so by asking for and then accepting interbank offers in a reasonable market size just prior to 11am."*

85 Q 460

86 Bank of England, BANK OF ENGLAND STERLING MONEY MARKETS LIAISON GROUP, Thursday 15 November 2007 Bank of England, MINUTES, Paras 2.1–2.2

87 Q 433

The BBA provisions go on: *"Therefore, submissions are based upon the lowest perceived rate at which it could go into the London interbank market and obtain funding in reasonable market size, for a given maturity and currency. BBA LIBOR is not necessarily based on actual transactions ...".*

Bearing in mind the definition of LIBOR and the illiquid, volatile and sometimes dysfunctional conditions generally prevailing in the money markets after August 2007, there might legitimately be a difference between actual transactions in the market and an individual bank's LIBOR submission because:

(i) There was uncertainty as to what constituted "reasonable size" and increased scope for different panel banks legitimately to make different judgements on this point;

(ii) Given the sporadic nature of market liquidity in this period, there might be a significant difference between the rate at which a bank could borrow at reasonable size at 11.00 am. and the rate at which it could borrow at other times of the day, or its average borrowing costs over the course of the day;

(iii) Banks entered into fewer, more sporadic and on average smaller interbank transactions, particularly at longer maturities. They therefore had to rely more on judgement in formulating their LIBOR submissions than pre-crisis, and market conditions made the exercise of that judgement increasingly difficult;

(iv) There was less transparency of the interbank market, in all likelihood because of reduced activity at longer maturities and more bilateral as opposed to brokered transactions.[88]

The Governor of the Bank of England also emphasised that:

If you go back to the money markets liaison group meeting, the regulator and the BBA were present at the meeting. The minutes were published on the website. No journalist interpreted those remarks as, "Gosh, we have a smoking gun of wrongdoing." The regulator did not look at it and say, "This is wrongdoing." There was enormous concern at the time about what the submissions of LIBOR actually meant in circumstances when the market was dysfunctional, and indeed I discussed it with this very Committee.[89]

Following our hearing, Lord Turner wrote to the Chairman of the Treasury Committee, and noted the preliminary findings of the FSA that:

In relation to any information which flowed to us from the Bank of England, we are aware that a member of our staff attended the Bank's Sterling Money Markets Liaison Group on November 15th 2007. We are investigating whether there was any

88 Supplementary memorandum to the Treasury Committee by Paul Tucker, 16 July 2012

89 HC (2012–2013) 535, Q 57

report of that meeting circulated within the FSA which might have raised concerns, but we are not currently aware that that is the case.[90]

The US authorities

50. On 13 July 2012, the Federal Reserve Bank of New York released copies of transcripts of calls its analysts had had with Barclays staff, as part of a release to Congress.[91] One of those transcripts, of a call between a Barclays staff member, and Fabiola Ravazzolo (FR), an analyst in the markets group of the Federal Reserve Bank of New York on 11 April 2008 contained a seeming admission of dishonesty at Barclays:

> [Unknown Barclays staff member]: We were putting in where we really thought we would be able to borrow cash in the interbank market and it was
>
> FR: Mm hmm.
>
> [Unknown Barclays staff member]: Above where everyone else was publishing rates.
>
> FR: Mm hmm.
>
> [Unknown Barclays staff member]: And the next thing we knew, there was um, an article in the Financial Times, charting our LIBOR contributions and comparing it with other banks and inferring that this meant that we had a problem raising cash in the interbank market.
>
> FR: Yeah.
>
> [Unknown Barclays staff member]: And um, our share price went down.
>
> FR: Yes.
>
> [Unknown Barclays staff member]: So it's never supposed to be the prerogative of a, a money market dealer to affect their company share value.
>
> FR: Okay.
>
> [Unknown Barclays staff member]: And so we just fit in with the rest of the crowd, if you like.
>
> FR: Okay.
>
> [Unknown Barclays staff member]: So, we know that we're not posting um, an honest LIBOR.
>
> FR: Okay.

90 Letter from Lord Turner to the Chairman of the Treasury Select Committee, 24 July 2012

91 Federal Reserve Bank of New York, New York Fed Responds to Congressional Request for Information on Barclays - LIBOR Matter, July 13, 2012

> [Unknown Barclays staff member]: And yet and yet we are doing it, because, um, if we didn't do it
>
> FR: Mm hmm.
>
> [Unknown Barclays staff member]: It draws, um, unwanted attention on ourselves.[92]

The release by the Federal Reserve Bank of New York recorded that "Immediately following this call [noted above], the analyst notified senior management in the Markets Group that a contact at Barclays had stated that underreporting of LIBOR was prevalent in the market, and had occurred at Barclays".[93] Between the 4–5 May 2008, the Governor of the Bank of England and Timothy Geithner, at the time President of the Federal Reserve Bank of New York, had a conversation at Basel about the operation of LIBOR.[94] Following discussions with the BBA, on 1 June 2008 Timothy Geithner sent an email to the Governor of the Bank of England.[95] The email contained a memorandum entitled "Recommendations for Enhancing the Credibility of LIBOR".[96] The memorandum contained the following recommendations:

> 1. Strengthen governance and establish a credible reporting procedure
>
> To improve the integrity and transparency of the rate-setting process, we recommend the BBA work with LIBOR panel banks to establish and publish best practices for calculating and reporting rates, including procedures designed to prevent accidental or deliberate misreporting. The BBA could require that a reporting bank's internal and external auditors confirm adherence to these best practices and attest to the accuracy of banks' LIBOR rates.
>
> To further enhance perceptions of the BBA as an objective intermediary in the rate-setting process, we recommend greater transparency with respect to the financial relationships between the BBA and the panel banks, and around the BBA's financial interests in LIBOR.
>
> [...]
>
> 6. Eliminate incentive to misreport
>
> If the combination of best practices and audit recommendations in (1) above seems unlikely to be sufficiently effective in ensuring accurate reporting, a complimentary approach might be to adopt the following process for collecting, calculating, and

92 Federal Reserve Bank of New York, New York Fed Responds to Congressional Request for Information on Barclays - LIBOR Matter, July 13, 2012

93 Federal Reserve Bank of New York, New York Fed Responds to Congressional Request for Information on Barclays - LIBOR Matter, July 13, 2012

94 Bank of England, Timeline of Bank/Federal Reserve/BBA communications about BBA Libor Review in 2008, 20 July 2012

95 Federal Reserve Bank of New York, New York Fed Responds to Congressional Request for Information on Barclays - LIBOR Matter, July 13, 2012

96 Federal Reserve Bank of New York, New York Fed Responds to Congressional Request for Information on Barclays - LIBOR Matter, July 13, 2012

> publishing LIBOR rates. The BBA could collect quotes from all members of the expanded panel, and then randomly select a subset of 16 banks from which the trimmed mean would be calculated. The names and quotes for the 8 banks whose rates are averaged to calculate the LIBOR fixing would be published. The banks whose reports fall above or below the midrange would not be publicly identified, nor would the level of their outlying rates. This random sampling from an expanded panel would lessen the likelihood that the market would draw a negative inference regarding a particular bank's continued absence from the list of published quotes.[97]

The Governor was keen to emphasise that:

> I solicited it [the note described above], which is the first part. I spoke to Tim Geithner in Basel a few weeks before. After that, I think it was on 19 May, his deputy, Bill Dudley, telephoned Paul Tucker and said that Tim Geithner wanted some advice on feeding views to the BBA, who are responsible for LIBOR. Should he write to the BBA, copied to me? Or should he write to me, copied to the BBA? Whatever.
>
> I sent a message back through Paul saying, "Write to me. We will look at your letter, and if we agree with it, we will endorse it and send it on to the BBA." So we solicited that e-mail, which arrived late one evening when I was in Frankfurt. I sent a message back saying that staff should give a view on it. I got that the next evening when I was back from Frankfurt, and the next day we wrote to the BBA, forwarding the e-mail memo from the New York Fed, saying that we wanted them to take account of this in their forthcoming consultation.[98]

51. We discussed this memorandum, and the Bank of England's response, with both the Governor of the Bank of England and Paul Tucker. We also requested further information on any Bank of England staff briefing about this note. The Governor of the Bank of England strongly denied that the Bank had received evidence of wrong-doing from the Federal Reserve Bank of New York via the memorandum. He noted that:

> [...] we have been through all our records. There is no evidence of wrongdoing or reporting of wrongdoing to the Bank. The memo from Mr Geithner that you referred to was, if you like, a constitution for how LIBOR should operate. It already had a set of operations. This was a self-reporting scheme. Any self-reporting scheme has to have a provision about deliberate misreporting. That is not the same as saying that they believe that there was deliberate misreporting.[99]

52. Since Mr Tucker had had conversations with the New York Federal Reserve, we questioned him about whether these contacts, and the paper from the Federal Reserve Bank of New York, had elicited any evidence of wrong-doing. He strongly denied that it had:

97 FRBNY Markets and Research and Statistics Groups, Recommendations for Enhancing the Credibility of LIBOR, May 27, 2008. Part of Federal Reserve Bank of New York, New York Fed Responds to Congressional Request for Information on Barclays - LIBOR Matter, July 13, 2012

98 HC (2012–13) 535, Q 42

99 HC (2012–13) 535, Q 55

Michael Fallon: Mr Tucker, last week when we asked you specifically about LIBOR integrity, you said, "We thought the underlying markets were dysfunctional, sporadically illiquid, much less reliable than normal, but we did not have suspicions of dishonesty". Yet the paper from the New York Fed recommends work with LIBOR banks to establish procedures designed to prevent deliberate misreporting. There is a whole section in this note on the need to "eliminate incentives to misreport". They were clearly concerned about misreporting. Did you really not have any suspicion of dishonesty?

Paul Tucker: In my discussions with Bill Dudley of the New York Fed, it was not framed in that way; it was framed as eroding confidence and credibility, particularly in dollar LIBOR, which was being set lower during London hours than it was subsequently trading in New York. We were very concerned about this piece of global infrastructure losing credibility. As the Governor said, we urged the BBA to review everything, particularly its governance, and to do so on a global basis. No, the note did not set off dishonesty alarm bells.

Michael Fallon: The penny didn't drop that the phrase "deliberate misreporting" might imply some degree of dishonesty?

Paul Tucker: No, it didn't.

Michael Fallon: Why not? What did you think "deliberate misreporting" was?

Paul Tucker: I am not sure I addressed my mind to it.

Michael Fallon: You didn't address your mind to the note from the New York Fed that we are discussing?

Paul Tucker: We were very focused on ensuring that there was a completely open-ended review of the way that LIBOR was run and constructed, and of some technical issues, as well. We were less interested in the technical issues than in the overall governance of the process. I think that we acted pretty firmly to ensure that that review occurred. The annual review that the BBA published was on which banks would be on the LIBOR panel, and we had made it clear to the BBA that that regular review of the LIBOR panel would not be enough.

Michael Fallon: This is not about credibility. Is "deliberate misreporting" dishonest?

Paul Tucker: Well, it turns out with hindsight that, yes, it was, but it did not set alarm bells ringing at the time, I am afraid.

Michael Fallon: But how could "deliberate misreporting" be honest?

Paul Tucker: I understand the question, Mr Fallon, but all I can say is that it did not set alarm bells ringing. We were very concerned about the credibility of LIBOR as a piece of global infrastructure and we acted.

> ***Michael Fallon:*** But you must have realised at the time that there were considerable incentives for banks to underreport and to protect their positions, given what was happening to Barclays.
>
> ***Paul Tucker:*** As I said last week, LIBOR seemed to move in a broadly sensible direction, given the strains in the market. The period that we are discussing now is one where sterling LIBOR and the LIBOR spread were rising. There were rumours about HBOS and about it approaching us for funds. We were very much focused on sterling LIBOR because we are the sterling lender of last resort. There was then this emerging concern in particular about dollar LIBOR. We were very concerned about the loss of credibility, but we did not seize on it in terms of dishonesty.[100]

The release of further information from the Bank of England following our oral evidence hearings contained a Bank of England staff note sent to Mr Tucker on 22 May 2008. That note contained the following passages:

> Fixing process, perception problem
>
> 5 The Libor problem has two fundamental sources: the nature of the fixing process (a survey not a traded rate), and its transformation from a measure of London money market conditions to the basis of a global derivatives market.
>
> 6 There is a long standing **perception** that Libor by virtue of the manner in which it is set is open to distortion: panel banks have no obligation to trade or to have traded at the rates that they submit, so it is at least *plausible* that these are influenced by commercial incentives. In normal times these might only have had a marginal effect, and could bias Libor different ways at different times. But this perception does mean that confidence in Libor *is fragile.* And in the extreme conditions of the last eight months banks have been subject to the more powerful incentive of avoiding **stigma** from being seen to submit high rates reflective of what they are actually paying.
>
> 7 If stigma does influence submitted rates, it would tend to bias Libor downwards and/or narrow the dispersion of individual, submissions. But it is not clear why the effect would be bigger in dollars, so this does not seem to be a good explanation for the alleged downward bias in $ Libor.

The release to this Committee by the Bank of England included an email chain between the (unknown) author of the note above, and Mr Tucker. Following further questions from Mr Tucker, the author made the following comments:

> We're saying that the fact there is a fuss is a problem, because of (a) the effect on confidence and (b) feedback from the fuss into real volatility in the fixing (after the April 16 BBA warning). But it is poor governance that allows there to be a fuss, hence governance needs fixing. We also say that the difference between Libor and other empirical measures (H15, swaps) is _not_ itself evidence that Libor is distorted. (The

100 HC (2012–13) 535 , Qq 45–51

> Fed will know this - our argument is just a small extension of that in the JPM piece.) So the empirical evidence does not as yet justify reforming the _definition_ of Libor.[101]

Lord Turner, in a letter to the Chairman of the Treasury Committee in July 2012, made the following comments about contacts between the FSA and the Federal Reserve Bank of New York:

> In addition it might be helpful to outline our current state of knowledge in relation to any information that passed from the Federal Reserve to the FSA. In his testimony to Congress on 17 July 2012, when referring to a conversation between a Barclays employee and a Federal Reserve employee on 11 April 2008, Chairman Bernanke stated: 'The Fed, after receiving this information...informed all the relevant authorities in the UK and the US. The NY Fed also communicated with the FSA and the Bank of England in the UK.'
>
> We have since been in touch with the Federal Reserve to clarify whether they did indeed send this information to us. They have now confirmed that they do not have any evidence to suggest that the communication took place. Nor do we currently have any evidence of such communication in FSA records.
>
> We have also asked the Federal Reserve to let us know whether they have any evidence to suggest that the email from Tim Geithner to Mervyn King on 1st June 2008 was copied to the FSA. They have confirmed that they have no indication that it was.
>
> It remains of course possible that our Internal Audit Review will subsequently find examples of communications between the Federal Reserve and the FSA of which both we and the Federal Reserve are currently unaware.[102]

The British Bankers Association review

53. Much of the contact between the Federal Reserve Bank of New York and the Bank of England centred on the memorandum described above, and then the British Bankers Association (BBA) review of LIBOR setting. This review provided an opportunity for the BBA, and the authorities, to reform the LIBOR setting process. The information received by the Treasury Committee after our oral evidence hearings with the Bank of England provides an insight into how the authorities acted on their concerns over LIBOR setting. The British Bankers Association has also provided the Committee with additional information. The Bank of England's correspondence contains the following short timeline of its efforts, alongside those of the Federal Reserve Bank of New York (FRBNY):

101 Bank of England, News Release, Further information and correspondence in relation to the BBA Libor Review in 2008, 20 July 2012

102 Letter from Lord Turner to the Chairman of the Treasury Select Committee, 24 July 2012

- From May 2008, the Bank of England encourages the BBA to conduct a global review of Libor and banks to engage with the review at a sufficiently senior level. It also begins to discuss these issues with the FRBNY.
- The Bank considers the points in the Geithner memorandum and ensures that those points are taken on by the BBA.
- The Bank and the Federal Reserve work closely together behind the scenes to influence the consultation paper issued by the BBA on 10 June 2008.
- The Bank also continues to work on influencing the outcomes after the consultation paper is published until the BBA publishes its final report on 18 December 2008.[103]

54. The additional evidence from the Bank of England provided a picture of an institution that took a keen interest in what the BBA review might achieve. An early BBA announcement on 30 May 2008 was met by the following comment from the Governor to Bank staff: "This seems wholly inadequate. What should we do?"[104] After the Bank had passed on Mr Geithner's memorandum to the BBA, the Bank engaged with the BBA on various drafts of the BBA consultation documents.

55. As the consultation continued, another concern developed at the authorities. They were keen to ensure that they did not appear to endorse the BBA's proposals and appeared to wish to maintain their distance. For example, on 5 June 2008, an email from Michael Cross at the Bank of England to Alex Merriman at the BBA contained the following comment:

> On the Bank's name, we have a clear line that it should not be used. I understand that the FSA and the Federal Reserve have the same position. Neither can we accept "relevant central banks...etc". That will obviously be taken as implying our endorsement of the proposals you make. Hence our suggestion that you refer to "all interested parties", as we and I am sure the far wider community with an interest in Libor would of course be happy to discuss your ideas on the basis of this paper.[105]

A paper on LIBOR by Michael Cross on 26 June 2008 noted that:

> We do not think that central banks should be formally involved in the LIBOR panels and processes, but we do think we should maintain a watching brief. We know the Federal Reserve and the Swiss National Bank wish, like us, to engage with the BBA on its review.[106]

103 Bank of England, News Release, Further information and correspondence in relation to the BBA Libor Review in 2008, 20 July 2012

104 Bank of England, News Release, Further information and correspondence in relation to the BBA Libor Review in 2008, 20 July 2012

105 Bank of England, News Release, Further information and correspondence in relation to the BBA Libor Review in 2008, 20 July 2012

106 Bank of England, News Release, Further information and correspondence in relation to the BBA Libor Review in 2008, 20 July 2012

The documents show that the Governor of the Bank of England responded on 2 July 2008 that he was "broadly content with the approach" described in the 26 June 2008 note above.[107] He also said though that he "would like Mr Tucker to meet with Angela Knight to impress on her the need for greater energy in [the] BBA's response and to make clear that [the Bank] would not stand in the way of alternative market initiatives to provide alternatives to LIBOR".[108] A letter from the Bank to the Treasury Committee, sent on 23 July 2012, summarised the position as follows:

> With regard to the Bank's involvement in the work undertaken by the BBA in 2008 on the scrutiny and governance of the Libor fixing process, the Bank's preferred approach was (and is) for there to be a gradual move away from systems based on self-reporting. And the Bank, having no regulatory authority, was not prepared to lend its imprimatur to a system that it was not able to control or enforce. As can be seen from this note and the papers disclosed on Friday, the BBA did want to use the Bank's name to bolster confidence in Libor.[109]

When asked whether he thought that the BBA had done a "good job", the Governor of the Bank of England told us that "I think they had to be nudged to get into the right direction, but, once they had been nudged in May 2008, they did work very hard to make a success of the consultation."[110]

56. In a letter to the Chairman of the Treasury Committee following our evidence hearings, Lord Turner outlined the FSA staff's knowledge at the time of the BBA review:

> We have identified, however, that some of our Markets Division staff most directly involved in inputting to the BBA LIBOR Review during May/June 2008 were sufficiently aware of market concerns of possible divergence between some LIBOR submissions and the actual cost of available funding that they identified this as a crucial issue which needed to be addressed by the Review. There is for instance, in the documents released last week by the Bank of England, an email from one of our staff to the BBA noting that the BBA should examine the 'Scrutiny of Submissions' since 'the rates submitted must represent the levels the panellists actually can fund.' This point was also made by the relevant staff in a memo to the FSA's then Managing Director, Wholesale, which described the key points we were inputting to the LIBOR review.[111]

57. It should be noted that on 25 April 2008, Angela Knight is quoted as telling a meeting of senior UK bankers, as well as representatives of the Bank of England (including the Deputy Governor at the time, Sir John Gieve) that "Longer term, [she] thought it would be

107 Bank of England, News Release, Further information and correspondence in relation to the BBA Libor Review in 2008, 20 July 2012

108 Bank of England, News Release, Further information and correspondence in relation to the BBA Libor Review in 2008, 20 July 2012

109 Letter from the assistant private secretary to the Governor of the Bank of England to the Clerk of the Treasury Committee, 23 July 2012

110 HC (2012–13) 535 , Q 90

111 Letter from Lord Turner to the Chairman of the Treasury Select Committee, 24 July 2012

necessary to explore whether a trade association was best placed to continue to provide what represented a key piece of market infrastructure.”[112]

Barclays’ contact with the regulators

58. We have seen already that the New York Federal Reserve Bank received direct confirmation from a Barclays source that manipulation of its submissions was occurring. Barclays’ discussions with UK regulators appear to have been less clear. The FSA’s final notice concluded that:

> Barclays did raise concerns externally about the LIBOR submissions of other banks (which Barclays perceived to be understated) and on occasion referred to its own approach to submitting LIBOR. However, these comments did not fully explain Barclays’ approach and were inconsistent.[113]

Barclays provided this Committee with a timeline of contacts with the FSA, the BBA, the Bank of England and the US Federal Reserve.[114] Lord Turner defended the FSA’s response to these contacts as follows:

> Well, as I said earlier, Barclays had very usefully identified the 13 instances between September ’07 and October 2008, where they feel that in some way they contacted the regulator—the FSA. The three of those which in the judgment of enforcement and, so far, in my judgment, looking at the file, were the clearest or closest to being clearest in suggesting that something was going on are described in the [FSA’s] final notice. They are described in paragraphs 128 to 130, 131 and 172 to 174.
>
> What two of those illustrate is that Barclays were actually sort of saying some elliptic things that implied that some other people might not be playing the game, but behind that they themselves were saying, “We’d better not tell the FSA about it”, and that is set out in the final notice.
>
> However, when I looked at one of them—paragraph 131—somebody said, “We’re being clean in principle, but we’re not being clean clean.” The question is why didn’t somebody put up a red flag? Well, the answer is this occurs as a comment among lots of comments in a large conversation about liquidity conditions in the marketplace. It occurs at a relatively junior level, and at that level somebody does not say, “This is a red flag that I should put up the management chain.”
>
> So within the FSA at that time, I can find no evidence that there were concerns noted at a senior management level or, for instance, discussed at the ExCo level. Now, in a perfect world, yes, those would have been spotted. But I return to the fact that there was simply a mindset that if there were problems here, it was for the BBA to solve them. Now, maybe that is a part of the way the world then was—the assumptions

112 Bank of England, BANK / BBA MEETING, 25 April 2008

113 Financial Services Authority, Final Notice, 27 June 2012, para 145

114 Barclays, Supplementary information regarding Barclays settlement with the Authorities in respect of their investigations into the submission of various interbank offered rates (Amended), 3 July 2012

> people then had—but that was the assumption that people were making at that time.[115]

Lord Turner has informed us that the Internal Audit Department of the FSA is now undertaking a review of how the FSA dealt with the contacts about LIBOR.[116] We discuss the Bank of England's contact with Barclays over LIBOR, and particularly the conversation between Mr Diamond and Mr Tucker, in the next section of this Report.

The role of the Barclays board

59. We have seen that the crisis in 2007 led to a close examination of the LIBOR submissions by the media, markets, and regulators. We questioned Barclays as to why, given both Barclays' submissions to the authorities that LIBOR submissions were being manipulated, its own board did not question Barclays' LIBOR submissions:

> ***Mr Love:*** [...] Mr Diamond, in his evidence to us, told us that he was continuously trying to alert others in important positions to the fact that other banks were manipulating LIBOR and that was the occasion for weakness on behalf of Barclays. Did it never occur to people at Barclays, particularly the board of directors, that if that were true—that banks were manipulating LIBOR—that would apply just as much, perhaps even more, to Barclays because it was an outlier in this regard? Did that never occur to the board? Were you being naïve in not thinking that that might be the case?
>
> ***Marcus Agius***: The concern that we had was not so much about the actions of LIBOR as such, because that was indicative of the underlying situation. The concern we had was that, because our submissions were high, people might falsely or incorrectly conclude that we were having more trouble funding than we actually were. And again, to put this into context, anybody who was not on the bridge of a bank during the financial crisis—and many others besides—who says it was not terrifying was not there. These were very difficult times and we were very nervous that we may be misinterpreted by the market as to our financial strength. We monitored it—and I know I did not, because it is not my job—and I know from many conversations I had with John Varley, with Chris Lucas and other people inside the bank that we were watching the funding markets like a hawk, as we should have done.
>
> ***Mr Love:*** Let me just take those facts you have just said: you were watching the markets like a hawk, and you were terribly concerned about the level of turbulence—and we do understand that, as it was a significant part of the evidence that we received yesterday. Did it not occur to anyone that one of the ways in which you could ease the situation for Barclays in that particular context was by manipulating LIBOR submissions on—

115 Q 1129

116 Q 1087

Marcus Agius: That was not a consideration.

Mr Love: I am not suggesting for a moment that you thought this was true, but you may well have had a conversation that went, "This could be possible. Can we make sure that we are submitting accurate results to LIBOR and the BBA?"

Marcus Agius: As I said, our greater concern was what was actually happening rather than the technicalities of LIBOR submissions.[117]

Conclusions on LIBOR submissions during the financial crisis

60. **Barclays has suggested that there were numerous contacts between itself and the authorities over LIBOR during this period. The clearest message appears to have been given by Barclays to the Federal Reserve Bank of New York, rather than to the UK authorities. Lord Turner described some of Barclays' contact with the FSA as "elliptic". We have found little evidence that Barclays provided the UK authorities with a clear signal about dishonesty at other firms, or its own. We await the outcome of the other regulatory investigations to see whether other firms provided such a signal, were equally elliptical or even silent on this problem. The timeline of contacts between Barclays and regulators provided to the committee by Barclays is not, of itself, evidence of a proactive approach on trying to report irregularities in the setting of LIBOR rates.**

61. **We would have expected the FSA and the Bank of England to have made efforts to identify and provide to the Committee documents clearly and directly relevant to our inquiry, subject to statutory restraints.**

62. **The financial crisis, and the serious dysfunctionality of the interbank lending markets, meant that it was difficult during this period for firms to estimate their own funding costs. LIBOR submissions were being used by markets and regulators to assess the financial health of the institutions involved. The FSA and the Bank of England were engaged in crisis management, alert to the possibility of further bank failures, rather than LIBOR manipulation. This is understandable, given the circumstances of the financial crisis, but with the advantage of hindsight constitutes a failing by the authorities.**

63. **Given the importance of LIBOR submissions in assessing banks' health, Bank of England staff were aware of the danger that banks might improperly manipulate their submissions. They noted that "banks have been subject to the more powerful incentive of avoiding stigma from being seen to submit high rates reflective of what they are actually paying". However, they primarily saw this as a matter for the regulator rather than the Bank of England. Mr Tucker told us that possible clues to dishonesty "did not set alarm bells ringing at the time". The evidence suggests that the Bank of England was aware of the incentive for banks to behave dishonestly, yet did not think that dishonesty was occurring. Nor did it appear to have asked the FSA to check to see if such dishonesty was occurring. With hindsight this suggests a naivety on the part of the Bank of England. They were certainly relatively inactive. This confirms evidence from**

117 Qq 649–651

other Treasury Committee inquiries of the dysfunctional relationship between the Bank of England and the FSA which existed at that time to the detriment of the public interest.

64. **Unlike the Bank of England, the Financial Services Authority was the prudential regulator. Its shortcomings at this time are therefore far more serious. The Committee is concerned about the FSA's failure to appreciate the significance of market rumours relating to the artificial rigging of the LIBOR rate. We therefore look forward to the result of the FSA's internal investigation, the existence of which was disclosed in evidence to us. The Committee will want the findings of that investigation to be published.**

65. As we have noted, the US authorities had received direct notification from Barclays that their LIBOR submissions were dishonest. In response to this, evidence given to a parallel inquiry in the US congress by Timothy Geithner revealed a 2008 memorandum provided to the Bank of England by the Federal Reserve Bank of New York on LIBOR setting. We know that the Bank of England then forwarded that memorandum to the British Bankers Association by the Bank of England. The evidence we have received from the UK authorities claims that they received no direct information about the evidence the US authorities had received about Barclays' dishonesty. **The evidence we have received is that there was significant co-operation between the US and the UK authorities at the time of the 2008 BBA review. It is understandable that regulators, in response to the LIBOR crisis, may have placed information in the public domain to demonstrate their respective assiduity at the time. This release of information must complement co-operation between regulators. The Chancellor should stress to his counterparts the need for such co-operation at the next G20 meeting.**

66. **The BBA's review of LIBOR in 2008, given that it focussed on the concerns of the market over the LIBOR setting process, appears to have been an opportunity missed to stop the attempted manipulation that was occurring. The Wheatley review should now look at the role of the BBA in LIBOR setting at that time in detail and publish its findings. This is essential if its recommendations for a more reliable LIBOR setting process are to carry credibility. The review should include how such systems work during times of financial crisis, when there may be little or no interbank lending taking place, and how the authorities should respond to signs of dysfunction. It should also consider whether a trade association is the appropriate body to perform that role.**

67. **We have seen no explanation for the failure, both of Barclays' board and of senior executives, to question its own firm's LIBOR submissions, when its staff were complaining about the submissions of other firms, and media and academic reports questioned the incentives present in LIBOR setting. There appears to have been enough doubt being spread about the LIBOR setting process to suggest that a closer examination by Barclays board of its own practices should have taken place. It stretches credibility to suggest that Barclays was trying to alert regulators to inconsistencies in the LIBOR submissions of other banks yet had no idea about the repeated 'low-balling' of its own submissions during the financial crisis set out in the FSA Final Notice. We have found no evidence that the board of Barclays sought to conduct an investigation.**

This was one of a number of failings on the part of Barclays' board. Others can be found in Sections 5 and 6.

4 The Tucker-Diamond dialogue and the Diamond File Note

The conclusion of the regulatory investigations

68. Paragraph 176 of the FSA Final Notice documents “a telephone conversation between a senior individual at Barclays and the Bank of England during which the external perceptions of Barclays’ LIBOR submissions were discussed”. The FSA Final Notice went on to say that, following this telephone conversation, which took place on 29 October 2008, an “instruction to reduce [Barclays] LIBOR submissions” was “given by senior management” on the same day. The FSA Final Notice made clear that “no instruction for Barclays to lower its LIBOR submissions was given during this telephone conversation”, but went on to state that “as the substance of the telephone conversation was relayed down the chain of command at Barclays, a misunderstanding or miscommunication occurred”. This, the FSA Final Notice, concluded meant “that Barclays Submitters believed mistakenly that they were operating under an instruction from the Bank of England (as conveyed by senior management) to reduce Barclays’ LIBOR submissions”.[118]

69. The CFTC and Department of Justice investigations also examined the role of the Bank of England in the lowering of Barclays LIBOR submissions in late October 2008. The Department of Justice’s description mirrored that of the FSA Final Notice. They explained that “on October 29, 2008, a senior Bank of England official contacted a senior Barclays manager”. The Bank of England official “discussed the external perceptions of Barclays’s LIBOR submissions and questioned why Barclays’s submissions were high compared to other Contributor Panel banks”. The Department of Justice concluded that:

> As the substance of the conversation was passed to other Barclays employees, certain Barclays managers formed the understanding that they had been instructed by the Bank of England to lower Barclays’s LIBOR submissions, and instructed the Barclays Dollar and Sterling LIBOR submitters to do so – even though that was not the understanding of the senior Barclays individual who had the call with the Bank of England official. Beginning on November 6, 2008, as a result of increased liquidity in the market, Barclays no longer needed to take into account the perceived instruction from the Bank of England.

70. The CFTC outlined how in September and October 2008 “Barclays increasingly felt tremendous external pressures concerning how it was being perceived in the market and media, particularly due to its higher LIBOR submissions relative to the other panel banks. The CFTC went on to say that Barclays “continued to believe that the other panel banks LIBOR submissions were unrealistically low” and that “even though it [Barclays] maintained that its liquidity position was in fact strong, Barclays was increasingly worried about these market and media perceptions”. The CFTC report that “at this time, the Bank

118 FSA, Final Notice, 27 June 2012, p 36, para 176

of England had a conversation with a senior individual in Barclays, in which it raised questions about Barclays liquidity position and its relatively high LIBOR submissions". The outcome the CFTC concluded was that:

> In late October 2008, reacting to this pressure and the discussion with the Bank of England, Barclays believed it needed to lower its LIBOR submissions even further. As a result, a member of senior management conveyed an instruction to the LIBOR submitters, through their supervisor, that Barclays U.S. Dollar and Sterling LIBOR submissions needed to be lowered to be 'within the pack,' meaning Barclays LIBOR submissions were to be made at or around the same rate as the other panel banks.[119]

Who was the senior Bank of England official?

71. There was intense media speculation over the following days as to the identity of the "senior individual at Barclays and the Bank of England" who had participated in this 29 October 2008 telephone conversation. By the weekend of 30 June 2012 the media were reporting that the 29 October 2008 conversation had taken between Mr Bob Diamond, then President of Barclays plc and Chief Executive of Barclays Capital, and Mr Paul Tucker, then Executive Director of Markets, and now Deputy Governor of the Bank of England (financial stability).[120]

72. Subsequently, and ahead of Mr Diamond's appearance before the Treasury Committee, Barclays published a File Note of the 29 October 2008 discussion, written by Mr Diamond following his conversation with Paul Tucker. This provided details of Mr Diamond's recollection of the conversation (see Box A for the full text of the File Note).

Box A: The Diamond File note

From: Diamond, Bob: Barclays Capital
Sent: 10/30/2008 14:19:54
To: Varley, John: Barclays PLC
Cc: del Missier, Jerry: Barclays Capital (NYK)
Subject: File note: Bank of England call
Fyi
File Note: Call to RED from Paul Tucker, Bank of England

Date: 29th October 2008

Further to our last call, Mr Tucker reiterated that he had received calls from a number of senior figures within Whitehall to question why Barclays was always toward the top end of the Libor pricing. His response was "you have to pay what you have to pay". I asked if he could relay the reality, that not all banks were providing quotes at the levels that represented real transactions, his response "oh, that would be worse".

119 P 24

120 'What did Bank of England say to Barclays about Libor?', by Robert Peston, BBC Newsonline, 1 July 2012

I explained again our market rate driven policy and that it had recently meant that we appeared in the top quartile and on occasion the top decile of the pricing. Equally I noted that we continued to see others in the market posting rates at levels that were not representative of where they would actually undertake business. This latter point has on occasion pushed us higher than would otherwise appear to be the case. In fact , we are not having to 'pay up' for money at all.

Mr Tucker stated the level of calls he was received from Whitehall were 'senior' and that while he was certain we did not need advice, that it did not always need to be the case that we appeared as high as we have recently.

RED [121]

The backdrop to the 29th October 2008 Diamond-Tucker discussion

73. The 29 October 2008 discussion between Mr Diamond and Tucker took place against a rapidly deteriorating outlook for the global financial system. In the United States, Merrill Lynch had sought refuge by selling itself to Bank of America, and the insurance firm AIG had received emergency funding from the US authorities. On 15 September 2008, Lehman Brothers had filed for chapter 11 bankruptcy protection, triggering an intensification of financial instability and the interbank funding markets became even more dysfunctional.

74. The situation in the UK was also critical. On 8 October 2008, the UK Government had announced a large-scale package to stabilise the UK financial system. More specifically, the Government said it was "bringing forward specific and comprehensive measures to ensure the stability of the financial system and to protect ordinary savers, depositors, businesses and borrowers".[122] These measures were intended to address what the Government described as the three root causes of the current financial crisis: concerns about liquidity, capital and funding:[123]

- To address concerns about liquidity, at least £200 billion was to be made available to banks under the Bank of England's Special Liquidity Scheme (SLS);[124]
- To address funding concerns, the Government established a Credit Guarantee Scheme. This made available to participating institutions a government guarantee to refinance maturing debt and was designed to unblock the interbank money market, and
- To address concerns about solvency, the Government asked the UK banks to increase their 'Tier 1' capital ratios and established the Bank Recapitalisation Fund, which

121 Barclays, Supplementary information regarding Barclays settlement with the Authorities in respect of their investigations into the submission of various interbank offered rates (AMENDED), 3 July 2012

122 HM Treasury Press notice, *Financial support to the banking industry,* 8 October 2008

123 HM Treasury, *Pre-Budget Report 2008,* November 2008, pp54–55

124 The Special Liquidity Scheme was first introduced in April 2008

provided support for those banks who wished to strengthen their capital ratios through the Government rather than the private sector.[125]

75. By mid-October 2008, two banks—RBS and HBOS—had been rescued with £37 billion of taxpayer support with the result that the Government now held a 57.9% stake in RBS and a 43% stake in Lloyds Banking Group (which emerged from the merger of Lloyds TSB and HBOS). Barclays at this stage had not made use of taxpayer monies for the purpose of recapitalisation, but it did benefit from other Government support mechanisms during the crisis such as the special liquidity scheme and the credit guarantee scheme. It was looking for a private-sector solution, but rumours were rife that it would also end up having to accept Government support.[126] Both Mr Diamond and Mr Tucker stressed to us that October 2008 was a time of acute financial instability and that their discussion had taken place just weeks after the part-nationalisation of RBS and Lloyds/HBOS.[127]

76. Barclays sent us a supplementary memorandum immediately prior to Mr Diamond's appearance before this Committee. This provided us with some Barclays-specific background context as to the tightening of liquidity conditions in October 2008 and Barclays LIBOR submissions during this period. Barclays told us that "during October 2008, in the wake of the collapse of Lehman Brothers, when liquidity conditions had tightened acutely, Barclays raised its US Dollar LIBOR submissions more significantly than other panel members". Barclays went on to describe how "in the month of October 2008, in particular, Barclays US Dollar LIBOR submissions for the 3 month maturity were the highest or next highest of the panel on every single day of the month and therefore excluded from the calculation of LIBOR". Barclays ended by stating that it:

> did not understand why other banks were consistently posting lower submissions; Barclays firmly believed that the other panel members were not, in fact, funding at a lower cost than Barclays.[128]

77. The discussion between Mr Diamond and Mr Tucker, which had taken place at the instigation of Paul Tucker,[129] and the subsequent publication of Mr Diamond's File note of his recollection of their discussion, had fuelled media speculation that either the Bank of England or the "senior" Whitehall figures referred to in the Diamond File note had encouraged or instructed Barclays to lower their LIBOR submissions. This was in large part because the end of the File note stated that:

> [...] while he [Mr Tucker] was certain we [Barclays] did not need advice, that it did not always need to be the case that we [Barclays] appeared as high as we [Barclays] have recently.

125 Eight banks participated in the recapitalisation scheme: Abbey, Barclays, HBOS, HSBC, Lloyds TSB, Nationwide Building Society, Royal Bank of Scotland and Standard Chartered

126 For example *British banks set for 40 billion pound rescue: sources*, Reuters, 12 October 2008

127 Qq 36, 337

128 Supplementary memorandum from Barclays, 3 July 2012

129 Supplementary memorandum from Barclays, 3 July 2012

The way Mr Diamond worded the last sentence meant that it was capable of being interpreted as an instruction, from either Whitehall or the Bank of England, to Barclays to reduce its LIBOR submissions.

78. However, Paul Tucker, when subsequently questioned on whether Mr Diamond's File note was an accurate reflection of their 29th October 2008 conversation, replied "not completely".[130] Mr Tucker told us that "the last sentence gives the wrong impression".[131] When asked how the File note should have ended in order accurately to reflect their discussion, Mr Tucker replied that:

> It should have said something along the lines of, "Are you ensuring that you, the senior management of Barclays, are following the day-to-day operations of your money market desk, your treasury? Are you ensuring that they don't march you over the cliff inadvertently by giving signals that you need to pay up for funds?"[132]

Who were the senior figures in Whitehall and did they instruct?

79. Mr Diamond appeared uncertain as to the identity of the "senior figures within Whitehall". When asked "what you took to mean by the phrase Whitehall, he replied 'officials in the Government'".[133] Later exchanges appeared to demonstrate that Mr Diamond had no idea who these "senior figures within Whitehall" were:

> ***Michael Fallon:*** Can we, Mr Diamond, go back to the file note of your call? You said in answer to the Chairman that you thought the senior figures referred to were—you said at one point—officials in the Government, and then later on you said members of the Government. Which do you believe? Who do you think they were?
>
> ***Bob Diamond:*** I would only be speculating if I told you who I thought they were, and I don't think it's appropriate to speculate. My recollection is Paul didn't mention who he was referring to or I would have put it in the note.
>
> **Michael Fallon:** Right. But who do you think he could possibly have been referring to?
>
> ***Bob Diamond:*** I don't want to speculate.
>
> ***Michael Fallon:*** A Department or—
>
> ***Bob Diamond:*** Senior people in the Government.

130 Q 330

131 Q 332

132 Q 333

133 Q 37

80. Paul Tucker, when he appeared before us the following week, confirmed that the "senior" Whitehall figures referred to in the File note were not Government Ministers, but civil servants: Sir Jeremy Heywood, Tom Scholar, Sir Nick Macpherson and Jon Cunliffe.[134]

81. Paul Tucker was questioned about the so-called instruction. He denied categorically that any Government Minister or civil servant had asked him to get Barclays to lower their LIBOR submissions:

> ***Mr McFadden:*** Can I ask you, did Jeremy Heywood or any other Government official that you mentioned in your opening answer to the Chairman ever encourage you to lean on Barclays or any other bank to lower their LIBOR submissions?
>
> ***Paul Tucker:*** Absolutely not.
>
> ***Mr McFadden:*** Did any Government Minister from the last Government ever encourage you to lean on Barclays or any other bank to lower their LIBOR submissions?
>
> ***Paul Tucker:*** Absolutely not.
>
> ***Mr McFadden:*** Specifically, did Shriti Vadera ever ask you to lean on Barclays or any bank to lower their LIBOR submissions?
>
> ***Paul Tucker:*** Absolutely not. If I may just add one thing there, what is more I don't think that I spoke to Shriti Vadera throughout this whole period at all.
>
> ***Mr McFadden:*** Thank you. Did Ed Balls ever ask you to lean on Barclays or any other bank?
>
> ***Paul Tucker:*** No. No.
>
> ***Mr McFadden:*** Or any other Government Minister?
>
> ***Paul Tucker:*** No.

82. Paul Tucker also denied the charge that he had personally issued an instruction:

> **Chair:** [...] would you categorically refute the suggestion that this conversation might reasonably have led someone to suppose you were inviting Barclays to join the pack and under-report LIBOR?
>
> ***Paul Tucker***: Absolutely.[135]

134 Q 335

135 Qq 40, 336

The Whitehall-Tucker discussions

83. Mr Tucker went on to explain why he had received these telephone calls, referred to in the File note, from "senior" figures in Whitehall. He said that Whitehall had two key concerns:

> There were two parts to this, which come together I think. Is the package working? If it is, why isn't it working more quickly? Secondly, should we be worried about Barclays? I don't want to say that it was expressed as concretely as this, because I can't remember, to be honest, but there was a sense of, including in the Bank, was the right decision taken in allowing Barclays not to take capital support from the Government?[136]

In other words, Mr Tucker said that the concerns in Whitehall were about the effectiveness of the many emergency measures which had been announced and the strength of Barclays as an institution, not about encouraging Barclays to manipulate its LIBOR submissions. With respect to the second concern, Mr Tucker said the source of this particular concern lay in the fact that "whereas some market participants felt that money-market conditions could ease because funding was being provided by the official sector, Barclays had continued to pay higher rates in the market, as reflected in their LIBOR submissions". Mr Tucker told us that civil servants were asking whether:

> the right decision [had been] taken when Barclays didn't take capital from the Government? If you remember, ... the Government's, the authorities' three-pronged package was announced on 8 October, I believe. On the 13th, when it was announced that RBS and HBOS Lloyds were taking capital from the Government, earlier that day Barclays announced that they would not be taking capital from the Government and would be taking various other measures. There was a degree of concern about that; there was a degree of anxiety about that.[137]

Mr Tucker went on to describe how some other banks "had been taken under the explicit wing of the Government", whilst "HSBC and Abbey National Santander were seen, at that point, to be relatively safe":

> That left Barclays. During that period, in the measure of credit risk indicated by the credit default swap market, Barclays was top. The way this crisis unrolled in more or less every financial centre was, as one domino went, "Who might the next one be?" We were not in the position of thinking Barclays is doomed. Had we thought that we, the Bank, would have given very strong advice to the Government that it was not safe for Barclays not to take capital from the Government, but it was a hard call and there was anxiety.[138]

136 Q 338

137 Q 337

138 Q 346

Barclays and the perceived instruction

84. Barclays, in its supplementary memorandum to this Committee prior to Bob Diamond's appearance before us, attempted to clarify the issue of whether an instruction had been issued and, if so, by whom. It told us that, subsequent to the 29 October 2008 discussion between Messrs Diamond and Tucker:

> Bob Diamond relayed the contents of the conversation to Jerry del Missier. Bob Diamond did not believe he received an instruction from Paul Tucker or that he gave an instruction to Jerry del Missier.

We questioned Mr Diamond on this point. He was clear that he did not believe he had received an instruction, whether from the Bank of England or Whitehall:

> ***Chair:*** [...] The note from Mr Tucker says that he felt your LIBOR returns could be lower, doesn't it?
>
> ***Bob Diamond:*** He felt that our LIBOR rates relative to the other 15 posters—
>
> ***Chair:*** Could be relative[ly] lower. Yes?
>
> ***Bob Diamond:*** Yes.
>
> ***Chair:*** Why then, on page 2 of the [Barclays] note to this Committee yesterday, did you say that you don't believe you received an instruction?
>
> ***Bob Diamond:*** I did not believe it was an instruction.[139]

The Diamond-Tucker discussion

85. Paul Tucker told us that the key message he wished to convey to Mr Diamond was to make "sure that the senior management of Barclays was overseeing the day-to-day money-market operations and treasury operations and funding operations of Barclays so that Barclays' money desk did not inadvertently send distress signals". He went on to explain that:

> In actual paying up for money in terms of what you borrow, you do not need to be at the top of the market all of the time. It is very important not to come across as desperate.[140]

86. Mr Tucker was challenged about the section of the File note which stated that "I [Mr Diamond] asked if he [Paul Tucker] could relay the reality, that not all banks were providing quotes at the levels that represented real transactions". More specifically, Mr Tucker was asked by the Committee whether he had considered the possibility that Mr Diamond was alerting him to the fact that other banks were falsely lowering their LIBOR submissions. Mr Tucker rejected this interpretation of Mr Diamond's comments. Instead

139 Q 38–40

140 Q 358

he explained that market conditions over this time had worsened and that the markets "had dried up", albeit "not completely". As a result, "for months there had been periods where sometimes it [LIBOR submissions] was based on judgments as to where they [banks] would be able to borrow rather than actual transactions of where they were borrowing". He went on to tell us that the banks were:

> having to make judgments about where they could borrow in the market, if they are not actually borrowing in the market. If they were not doing real transactions, then Bob Diamond was effectively saying, "Look, when they come to do real transactions they are going to be paying the same as us."[141]

87. Mr Diamond told us that he believed Paul Tucker was trying to tell him was that there were "Ministers in Whitehall who are hearing that Barclays is always high. That could lead to the impression that you are not funding yourself." He told us that his first reaction was:

> "John [Varley], you have to get to Whitehall. You have to make sure they know that we are funding fine. It's not wonderfully, it is adequately, but we have an equity issue about to settle in two days. We're raising £6.7 billion of capital when a number of British banks had just taken capital from the Government."

A key point which Mr Diamond appeared to have had in his mind at this time was the potential threat of nationalisation:

> If Whitehall was told, "Barclays is at the highest of LIBOR", without knowing all that I just went through, they might say to themselves, "My goodness, they can't fund. We need to nationalise them," as they had nationalised other British banks.[142]

This may help explain why Mr Diamond, following the discussion with Paul Tucker, then wrote a File note to John Varley, then Barclays Chief Executive and Jerry del Missier, a senior lieutenant of Mr Diamond's. Writing File notes, Mr Diamond told us, was something he did "not [do]frequently" at that stage.[143]

88. John Varley did not give oral evidence in this inquiry. However, he wrote to us on 16 July 2012 to provide an explanation of what action he took upon receiving Mr Diamond's File note:

> On the day I received Mr Diamond's email, I spoke, or left voicemail, with Lord Myners, Sir John Gieve, and Mr Sants to inform them of the successful completion of Barclays capital raising, which alleviated concerns about our capital ratios and funding position. To the best of my recollection, those conversations did not refer to concerns about Barclays LIBOR submissions. I do not recall any subsequent discussions at that time with them or other members of the tripartite authorities specifically referring to concerns about Barclays LIBOR submissions. On 7th

141 Q 362

142 Q 47

143 Q 27

> November, I attended a meeting with the Chancellor of the Exchequer and other bank executives. There was reference to LIBOR during that meeting, but it related to growth in the economy, and what the banks could do to support that, particularly in the context of the cost of credit to small business.[144]

We subsequently wrote back to Mr Varley requesting further information about any discussions he may have had with Mr Diamond or del Missier about the conversation between Mr Diamond and Mr Tucker or the subsequent File note. He told us:

> As to whether I replied to Mr Diamond's file note or took any consequential action, I emailed Mr Diamond on 3 November 2008 in response to his file note of 30 October 2008 saying: "Bob, We should discuss." I believe this was in anticipation of a working dinner I was due to attend on 3 November with Lord Turner and Mr Sants, to which I referred in my letter to you of 16 July 2012. I do not recall receiving a reply from Mr Diamond or taking any specific action beyond what I described in that letter to you of 16 July.

He went on to tell us that "other than responding to Mr Diamond in the way I describe in paragraph numbered 4 [reproduced above] , I do not recall speaking with him about his conversation with Mr Tucker or his subsequent file note". Mr Varley ended by stating that "to the best of my recollection and belief, I did not discuss Mr Diamond's conversation with Mr Tucker or his file note with Mr del Missier". Similarly, Mr Varley stated that he "did not discuss Mr Diamond's conversation with Mr Tucker or his file note with Mr Agius, or any other senior executive or non-executive director".[145]

The role of Jerry del Missier

89. Following publication of the Diamond File note it emerged that Jerry del Missier, at that time Co-President of Barclays Capital, and copied into the File note along with Mr John Varley, had mistakenly assumed that Mr Diamond had instructed him to lower Barclays LIBOR submissions.

90. When questioned as to how Mr del Missier could have misconstrued the File note and concluded that it was an instruction to lower Barclays LIBOR submissions, Mr Diamond simply replied "Michael, with apologies, I can't put myself in Jerry's shoes".[146] We therefore asked Jerry del Missier how he had misconstrued Mr Diamond's File note:

> Well, Mr Fallon, I know only what I clearly recall from my conversation with Mr Diamond. The investigators that have looked at this thoroughly have concluded that there was a miscommunication and misunderstanding, but I can only recall my recollection—I can only state what my recollection of the conversation is.[147]

144 Letter from Mr John Varley to the Chairman of the Treasury Committee, 16 July 2012

145 Letter from Mr John Varley to the Chairman of the Treasury Committee, 2 August 2012

146 Q 87

147 Q 890

91. Mr del Missier revealed that he had acted on the basis of a telephone conversation with Mr Diamond on the 29 October 2008, following Mr Diamond's conversation with Mr Tucker, and not on the basis of the File note.[148] When questioned about his conversation with Mr Diamond, Mr del Missier told us that Mr Diamond told him that:

> he had a conversation with Mr Tucker of the Bank of England, that the Bank of England was getting pressure from Whitehall around Barclays—the health of Barclays—as a result of LIBOR rates, that we should get our LIBOR rates down, and that we should not be outliers.[149]

When questioned further on this topic, Mr del Missier said that:

> What was communicated to me by Mr Diamond was ... about political pressure on the bank, regarding Barclays's health and, as indicated by our LIBOR rates, that we should get our LIBOR rates down, and not be outliers; and there's nothing in the note which is in conflict with that [Diamond-Tucker] conversation.[150]

92. We asked whether Mr Diamond had told Mr del Missier "effectively to invent a submission", but Mr del Missier replied categorically "No, Sir; that is not what Mr Diamond said".[151] When asked whether he believed he was "acting on an instruction from the Bank of England or from other Whitehall sources", Mr del Missier replied "yes".[152] He went on to say that he believed the so-called instruction to have come from Paul Tucker, adding that "Mr Diamond told me that Mr Tucker had given it[the instruction]".[153] He confirmed in response to repeated questioning that he viewed the instruction as coming from the Bank of England rather than the "public authorities" more generally.[154] Mr del Missier was finally asked whether he would have issued the instruction in the absence of "cover from the tripartite". He replied "no".[155]

93. Jerry del Missier told us that he was in "regular communication" with Mr Diamond, albeit "not always daily", and would communicate with him several times a week.[156] However, he went on to tell us that he never discussed the 29 October instruction again with Mr Diamond.[157] When questioned as to why this was the case, Mr del Missier told us that:

> there were many, many big events going on in this period, Mr Chairman. The entire financial system was hanging in the balance, and in the grand scheme of everything

148 Qq 823, 878

149 Q 825

150 Q 891

151 Q 829

152 Q 878

153 Q 882

154 Q 888

155 Qq 880–881

156 Qq 903–906

157 Q 839

> that was going on, it didn't seem a significant event, given the number of significant events that were transpiring at that time.[158]

Passing on the perceived instruction

94. Mr del Missier said that he then "passed the instruction ... on to the head of the money markets desk" who he identified as Mr Mark Dearlove.[159] Mr del Missier told us that he "relayed the contents of the conversation that I had with Mr Diamond, and fully expected that the Bank of England's views would be incorporated in the LIBOR submissions".[160] In subsequent questioning Mr del Missier told us that, more specifically:

> I said, "I've spoken to Mr Diamond. He's had a call from Mr Tucker." I alluded to the pressure—the political pressure—around Barclays's health, as demonstrated by our LIBOR rates, and that we should get our rates down and not be an outlier.[161]

When challenged on what exactly he expected to happen, Mr del Missier replied that "given that Barclays was high rates, I would have expected that taking that into account would have resulted in lower submissions".[162] When asked how Mr Dearlove reacted to the instruction, Mr del Missier told us he was unable to "recall the full specific of the conversation".[163] We pressed Mr del Missier further on what Mr Dearlove said in response to the instruction request.

> ***Andrea Leadsom:*** But would you expect Mr Dearlove to say, "Then I asked Mr del Missier, 'Are you sure about this? This is not in the rules, at the very least, and this is breaking the law, at the very worst.'"? Would he tell us that that is what he said to you or not?
>
> ***Jerry del Missier:*** I don't think that is what he would say.

95. Mr Dearlove then passed on the instruction to the submitter. Mr del Missier said that he then had "a follow-up conversation with the head of the desk, and several of the desk members, and gave them the context of the conversation that I had had with Mr Diamond about the conversation that he had had with Mr Tucker".[164] However, Mr del Missier then told us that he did not check to see what effect his instructions had on Barclay's LIBOR submissions.[165]

96. Mr del Missier was unable to remember Mr Dearlove's reaction to being issued with the instruction, but told us that through the course of the investigation, he learnt that

158 Q 839

159 Q 999

160 Qq 831–832

161 Q 1000

162 Q 834

163 Q 1003

164 Q 863

165 Q 864–868

"compliance was alerted of the nature of the request that had come in", adding "but there was no follow-up from compliance"[166] Mr del Missier confirmed that a Mr Stephen Morse, Head of Compliance was the person who was informed by the money market desk of the instruction.[167]

97. The FSA Final Notice noted that a submitter "emailed Manager F and others on 29 October 2008 in relation to this instruction, copying in compliance". The email was sent to Mark Dearlove and Stephen Morse, the head of compliance was copied in. The email, which was subsequently supplied to the Committee by Barclays, shows that the submitter was uncomfortable with what he was being asked to do. The email stated:

> As per the telephonic communication today with Mark Dearlove. I have been requested to reduce the Sterling Libor rates to be more in line with the "Pack".
>
> As I understand it this is an instruction by either senior management and/or the Bank of England.
>
> I voiced my views as below but as such will comply with the request and that it will take me a week to comply.
>
> But it should be noted that this will be breaking the BBA rules with regard to the setting of Sterling Libor rates IE (a reasonably [sic] amount offered in the market in the period concerned.) and as such the breaking of such rules will happen until the instruction demanded by senior management will be rescinded or the BBA rules are changed.[168]

The FSA Final Notice stated that "compliance did not consider appropriate for Barclays' submitters to comply with the instruction". On 3 November, Mr Morse wrote an email in response to the submitters 29 October email, and which he sent to, amongst others, Mr Dearlove. The email stated:

> Thanks for your note. In my view we should continue to quote Sterling Libor rates where we see it – we obviously need to make sure we follow the BBA's rules and avoid potential action by the FX and MM Committee [of the BBA]. I've not been made aware of any suggestion by external sources that we should reduce rates to join the "pack", but I'll take that up with senior management this week [...].[169]

98. Notwithstanding the concerns expressed by Mr Morse in his 3 November 2008 email it is clear that no further action was taken by Group Compliance. The FSA Final Notice concluded:

> Compliance did not speak to Barclays' Submitters. Compliance did not ensure that the Submitters did not follow the instruction. The relevant individual in Compliance

166 Qq 1005–1006

167 Q 1019

168 Barclays, email from money market desk to Compliance, 29 October 2008, received by Committee 23 July 2012

169 Barclays, email from Compliance to money market desk, 3 November 2008, received by Committee 23 July 2012

thought his email would suffice to "nip it in the bud". In addition, Compliance did not discuss the issue with senior management. An individual in senior management went on to reiterate the instruction at a meeting with Barclays' Submitters on 6 November 2008.[170]

99. The FSA investigation has left a number of important questions unanswered. The first of these is whether "senior" Whitehall figures issued an instruction to Paul Tucker to get Barclays to lower their LIBOR submissions or, as Mr Tucker insists, Whitehall were simply trying to garner information about the health of Barclays, and the success or otherwise of the Government's rescue package, at a time of acute financial instability. Paul Tucker told us that he did not receive an instruction from Whitehall (whether from Government Ministers or officials) to tell Barclays to lower their LIBOR submissions and we have not received any evidence to the contrary. **The evidence we received suggests that Whitehall was prompted to contact the Bank of England because of its concerns about whether the October 2008 rescue package for the UK financial system was working, as well as concerns about the financial health of Barclays. This was understandable given the fragility of the UK and international financial system in October 2008.**

100. Mr Tucker relayed Whitehall concerns about Barclays to Mr Diamond in a telephone discussion on 29 October 2008. There is no transcript or recording of the conversation between the two men. Nor did Mr Tucker, or his officials, make a contemporaneous note of the discussion. The only record of the discussion is therefore a File note written the following day by Mr Diamond.

101. Mr Tucker contests the accuracy of the final sentence of the 28 October 2008 File note. The final critical sentence reads—"while he [Mr Tucker] was certain we [Barclays] did not need advice, that it did not always need to be the case that we [Barclays] appeared as high as we [Barclays] have recently". It is by no means clear that the final sentence of Mr Diamond's record of the call was an instruction to lower Barclays LIBOR submissions, although it was interpreted in that way by Barclays. Mr Tucker disputes Mr Diamond's recollection of their 29 October 2008 discussion as recorded in the File note and, in particular, objects to the final sentence. Mr Tucker told us that the last sentence "gives the wrong impression" and believes it should have said "Are you ensuring that you, the senior management of Barclays, are following the day-to-day operations of your money market desk, your treasury? Are you ensuring that they don't march you over the cliff inadvertently by giving signals that you need to pay up for funds?" **We will never know the details of the discussion between the Mr Tucker and Mr Diamond. What we do know is that Mr Tucker denied ever having issued an instruction to Barclays whilst Mr Diamond denied having received an instruction from Mr Tucker.**

102. **The File note is of secondary importance as far as the subsequent transmission of the instruction is concerned. This is because Mr del Missier told us that he acted, not on the basis of the File note, but on the basis of the 29 October 2008 discussion he had with Mr Diamond, following the conversation between Mr Diamond and Mr Tucker. Mr del Missier informed us that the File note correctly records the substance of the Tucker-Diamond discussion as relayed to him by Mr Diamond, but not the exact words. There**

170 FSA Final Notice, 27 June 2012, p 37, Para 179

is no File note of the conversation between Mr Diamond and Mr del Missier and no recording was taken of their discussion.

103. **It remains possible that the entire Tucker-Diamond dialogue may have been a smokescreen put up to distract our attention and that of outside commentators from the most serious issues underlying this scandal.**

104. Mr Diamond denied that he himself issued an instruction to Mr del Missier. Mr del Missier, on the other hand, believed that he did receive an instruction, but one which emanated from the Bank of England. The FSA Final Notice concluded that Mr del Missier misunderstood what Mr Diamond was communicating to him. However, Mr del Missier in evidence to us was clear that he believed he was implementing an instruction from the Bank of England.

105. **From Mr del Missier's evidence it appeared that Mr Dearlove was comfortable with the instruction that was passed to him following his 29 October 2008 conversation with Mr Diamond. There was some resistance from the submitter, who emailed compliance with his concerns. However, he or she ultimately acted on the instruction. There appears to have been, once again, no real 'push-back' from the compliance function when they were informed by Group treasury of the instruction. This lack of 'push back' demonstrates the weakness of the compliance function in Barclays at that time. It may also reflect the fact that Group treasury had been submitting false rates since September 2007 and that, to this end, Mr del Missier's instruction was not a departure from prevailing practice. It is unclear to the Committee why Barclays has attempted to place such weight on the Tucker-Diamond phone call given the pattern of repeated dishonesty in LIBOR submissions in the months running up to this phone call set out in the FSA Final Notice. Barclays did not need a nod, a wink or any signal from the Bank of England to lower artificially their LIBOR submissions. The bank was already well practised in doing this. Mr del Missier appears to have stressed the fact that what he saw as an instruction came from the Bank of England and that this may have muted resistance to it. Mr del Missier's evidence, that he received such an extraordinary instruction from the Bank of England, yet subsequently queried it neither with Mr Diamond nor with those to whom he passed the instruction, is not convincing. He would have known that falsifying LIBOR submissions was not permitted.**

106. Mr del Missier has sought to play down the significance of the 29 October 2008 instruction. He stressed that it was of relatively minor significance, which would fit with the pattern of behaviour from Barclays in the months running up to the phone call. Certainly, it appeared sufficiently unimportant to him that he never discussed the matter again with Mr Diamond. Indeed Mr Del Missier apparently did not even check whether his instruction had been acted on. However, Mr Diamond felt that the discussion with Mr Tucker was of sufficient importance to merit the writing of a File note, something Mr Diamond did not ordinarily do.

107. **The Committee remains sceptical about the importance of the Tucker-Diamond phone call given the already established pattern of dishonest LIBOR submissions from Barclays set out in the FSA Final Notice. The lack of a record by the Bank of England of the conversation between Mr Tucker and Mr Diamond is of great concern. The fact that Mr Tucker failed to make a contemporaneous note of the conversation is explicable**

given that the UK was in the midst of the most serious financial crisis in modern times: there was unprecedented pressure on senior Bank of England staff at this time. Nonetheless, the Bank of England should have had adequate procedures in place for at least the making of a File note of such conversations. We recommend that the Bank undertake a review of its note keeping systems, especially those involving senior executives, and publicly report its conclusions.

108. **If Mr Tucker, Mr Diamond and Mr del Missier are to be believed, an extraordinary, but conceivably plausible, series of misunderstandings and miscommunications occurred. The evidence that they separately gave describes a combination of circumstances which would excuse all the participants from the charge of deliberate wrongdoing.**

5 Barclays and the FSA

Introduction

109. Barclays is subject to prudential and conduct regulation by the FSA. Under the terms of the Financial Services Bill it will in future be regulated by the new microprudential regulator, the Prudential Regulation Authority (PRA), which will be part of the Bank of England, and the new conduct regulator, the Financial Conduct Authority (FCA).

110. Barclays' own guidance on corporate governance states that its directors must act in accordance with the principles issued by the FSA under the terms of the Financial Services and Markets Act 2000 and, in particular, must:

> 1. act with integrity;
>
> 2. act with due skill, care and attention;
>
> 3. observe proper standards of market conduct;
>
> 4. deal with the FSA and with other regulators in an open and co-operative way and must disclose appropriately any information of which the FSA would reasonably expect notice;
>
> 5. take reasonable steps to ensure that the business of the firm for which they are responsible is organised so that it can be controlled effectively;
>
> 6. exercise due skill, care and diligence in managing the business of the firm for which they are responsible, and
>
> 7. take reasonable steps to ensure that the business of the firm for which they are responsible complies with the relevant requirements and standards of the regulatory system.[171]

The fourth of these principles is particularly important in relation to the evidence we have heard about the relationship between the FSA and Barclays.

111. Mr Diamond raised the bar for the conduct of Barclays as a whole even higher in the Today Business Lecture he delivered in 2011. He said:

> [...] the single most important thing for banks and for businesses now is to focus on helping to create jobs and economic growth; and being able to do that requires us—banks in particular—to rebuild the trust that has been decimated by events of the past three years; and that rebuilding trust requires banks to be better citizens.
>
> I believe in this passionately.

171 *Corporate Governance in Barclays*, Barclays Corporate Secretariat, February 2012

That is why since I became chief executive of Barclays, at the beginning of this year, the management team has focused on four strategic priorities—one of which is citizenship.

[...]

For me becoming a better citizen means three things:

First, it's about how we behave, especially with our customers and clients; second, it's about what we do, and in particular how we help those customers and clients create jobs and economic growth; and third, it's about how we contribute to the communities we serve in many other ways.

I know how angry customers are about issues such as Payment Protection Insurance. That's why we are working hard to clear claims as quickly as possible.

We want to put things right. But we know it's not enough just to apologise. We have to try to make sure that things like that don't happen again.

In part that comes down to culture.

It's a very personal thing, but throughout my career—from my time as a teacher, to my time as a banker—I have seen just how important culture is to successful organisations.

Culture is difficult to define, I think it's even more difficult to mandate—but for me the evidence of culture is how people behave when no-one is watching.

Our culture must be one where the interests of customers and clients are at the very heart of every decision we make; where we all act with trust and integrity.

But it's not just about how we behave towards our customers and clients. It's also about how we work together with our colleagues, because if you have to deliver for customers with 150,000 colleagues around the world, as we do, you better be able to work as a team.

As far as I'm concerned, if you can't work well with your colleagues, with trust and integrity, you can't be on the team.

Culture truly helps define an organisation.

[...]

To the question "can banks be good citizens?" the answer must be "yes". But I'm mindful of what was said to me three years ago: "Bob, think about the fact that no-one will believe you."

We're in the early stages of working to restore trust.

I'd like to be able to say we're achieving that, but I know that for you, seeing is believing.

> You may not be able to see what's different today, but over time I very much hope you will see that and more.[172]

Mr Diamond's comments about culture echo the Group of Thirty report on corporate governance, which said that "Values and culture drive people to do the right thing even when no one is looking."[173]

112. **We endorse Mr Diamond's view, which echoes that of the Group of Thirty, that the culture of an organisation is demonstrated by how people behave when no-one is watching. In this case, however, the culture of the Barclays allowed people to do the wrong thing quite openly over a long period, with the attempted manipulation being shouted about across the dealing room floor. Barclays was found to have fallen lamentably below the standards that the former Chief Executive suggested should be set for his own firm.**

Appointment of Bob Diamond as Barclays chief executive

113. In September 2010 the board of Barclays appointed Bob Diamond as chief executive of the company to succeed John Varley. The FSA is required to review such appointments under its Significant Influence Function (SIF) procedures. The purpose of the SIF regime is to assess the suitability of an individual's competence to undertake a role, and to ensure that a robust and rigorous appointment process is undertaken by the firm concerned. The FSA approved the application from Barclays for Bob Diamond to become chief executive, and he took up the post in January 2011.

114. When informing the Chairman of Barclays of this approval in a letter of 15 September 2010, Hector Sants, then Chief Executive of the FSA, said that "an integral part of our approval process is to set out any appropriate issues that we expect the Board to address in its ongoing governance and oversight of Bob Diamond in his role as Group CEO". These were as follows:

> 1. The FSA expects Bob Diamond to continue to develop a close, open and transparent relationship with his regulators both here in the UK and globally. It has already been identified that this will require an increased level of engagement from Bob Diamond and we have made our expectation known to him. As discussed, we would also expect Bob to be based in the UK.
>
> 2. The succession plan announced in respect of Barclays Capital has Jerry del Missier and Rich Ricci as Co-Chief Executives. We will want to seek ongoing assurance that this managerial structure remains effective. We will also require that there is appropriate clarity in oversight and responsibilities and that independent challenge is provided by Bob Diamond in his role as Group CEO.

172 Bob Diamond, Today Business Lecture, 3 November 2011

173 *Toward effective governance of financial institutions*, Group of Thirty, 2012

> 3. As you would expect, we place considerable emphasis on the CEO setting the right culture, risk appetite and control framework across the entire organisation. It is essential that a prudent balance is struck, in delivering the group's financial and strategic objectives and desirable consumer outcomes; alongside consideration of broader reputational risks for the group.
>
> 4. You have identified Bob Diamond's relative lack of direct retail banking experience notwithstanding his role on both the Group Executive and Board. We appreciate the depth of other Executive Committee members' relevant experience but will look to be satisfied that the required focus on the retail banking business and consumer outcomes is maintained by him.[174]

115. The Committee asked Bob Diamond about the contents of this letter:

> ***Chair:*** But it is true, isn't it—at least I have been told—that the FSA were concerned about your appointment as chief executive? They sought assurances from the board at the time of your appointment that there would be a change of culture at Barclays. Is that not correct?
>
> ***Bob Diamond:*** That's the first I've ever heard that there was any question about my appointment as chief executive. I certainly went through, as a chief executive appointment would, interviews with the Financial Services Authority, and I got very strong support for my appointment to chief executive.
>
> ***Chair:*** And you know nothing of any written submission by the FSA to the board at that time, setting out the need for an improvement in the corporate governance of Barclays, an improvement in the culture, a need to look better at how you were assessing the risk appetite, and to improve the control framework? You know nothing about this whatsoever?
>
> ***Bob Diamond:*** I knew nothing about it at the time that I was appointed. Correct. I don't know anything about it.
>
> ***Chair:*** We're talking about September 2010 here.
>
> ***Bob Diamond:*** Correct.
>
> ***Chair:*** And you know nothing at all about the suggestion that you were asked to provide assurances that you would challenge your long-term colleagues at BarCap not to take excessive risks?
>
> ***Bob Diamond:*** I don't remember any specific comments, but I am sure there were discussions with the regulators during the process of my succession. My memory is more around whether, having been associated with the investment bank for a number of years, I would be able to disassociate myself so, as a group chief executive,

174 Letter from Hector Sants to Marcus Agius, 15 September 2010

> I would be able to leave the running of the investment bank to—at the time—Rich [Ricci] and Jerry [del Missier].[175]

116. Before his appearance, we took the unusual step of requesting that Mr Agius send us the correspondence between the FSA and Barclays which related to the points that we had raised with Mr Diamond. On the subject of the September 2010 letter, he wrote to the Chairman of the Committee as follows:

> As you will see from the enclosed letter from the FSA, dated 15 September 2010, the FSA approved the bank's application for Mr Diamond to be Barclays Group CEO. The FSA made it clear that they wanted an increased level of engagement from Mr Diamond with regulators in the UK and globally and that they would want him to be based in the UK. (This reflects the fact that he was, at that time, based in New York and that, until then, he had naturally not had as much engagement with the FSA as would be expected on his assuming the role of CEO). They also wanted to ensure that independent challenge to those reporting to him was provided by Mr. Diamond in his role as Group CEO. Neither of these desires can fairly be interpreted as expressions of concern about his appointment.
>
> Furthermore, as at 10 September 2010 the FSA investigation into Barclays LIBOR submissions was ongoing. The FSA had been informed by the bank of the trader requests, the actions of the bank during the financial crisis and the instructions to submitters after Mr Diamond's conversation with the Bank of England. These matters were not raised by the FSA at that time as casting doubt on his suitability as CEO.
>
> There is a paragraph in the letter detailing the FSA's emphasis on the CEO setting the right culture, risk appetite and control framework across the organisation. These are areas of focus that you would expect the FSA to require any CEO to have in mind—there was no suggestion that these expectations were particular to Mr Diamond either in the letter or in any discussions that were had between the Board and the FSA at the time. Most significantly, there was no request for assurances from the Board that there should be a change of culture at Barclays.[176]

117. When he gave evidence we asked Marcus Agius, to whom the letter was addressed, for his views about it and for his recollections of his exchanges with Mr Diamond on the subject:

> ***Chair:*** Why don't we take the 2010 letter first? What did you take from the FSA's description of what they expected from Bob Diamond as Chief Executive, that they wanted a "close, open and transparent relationship", and their specific expression of concern that there be appropriate oversight of his immediate subordinates, especially del Missier?

175 Qq 10–13

176 Letter from Marcus Agius to Andrew Tyrie MP, 9 July 2012

Marcus Agius: There are two points together in that. The first point I believe is a statement they would have made in respect of any Chief Executive.

Chair: Do you think that is the sort of thing they put in every letter and they just lift that as some kind of cut and paste?

Marcus Agius: It would be surprising if they did not make that statement to any Chief Executive coming in.

Chair: It is worth reading: "The FSA expects Bob Diamond to continue to develop"—not keep—"a close, open and transparent relationship with his regulators." Do they come out with that line to every Chief Executive?

Marcus Agius: Bob Diamond prior to being appointed as Chief Executive of Barclays was the President; he was not the leading executive in the bank. That was John Varley. John Varley did have a close relationship with the FSA; Bob Diamond was at one remove, so for them to expect him to develop a close relationship coming into the job is exactly what I would have expected them to have said.

Chair: And on Del Messier and his team? "We will also require that there is appropriate clarity in oversight and responsibilities and that independent challenge is provided by Bob Diamond in his role as Group CEO" to them.

Marcus Agius: Yes, and that was a point that we made separately to Bob, self-evidently because he had grown up—if that is the right expression—in the investment bank. Jerry Del Messier and Rich Ricci were his lieutenants. When any person makes the move from one division into the centre, it is vital that he dissociates himself or becomes more objective in his treatment of that division than he would otherwise have been hitherto.[177]

118. Mr Agius also told us that he had approached the FSA shortly before the end of the appointment process to ensure that the regulator would have no difficulty with the appointment. He told us that Mr Sants of the FSA had said that it would not cause difficulty:

Marcus Agius: [...] As I said before, conducting the search for a Chief Executive is one of the most important things a Chairman can do. You need to get it right and you need to get it right in every respect. As the process was nearing its conclusion I thought it prudent to go and have a conversation face to face with Hector Sants just to make sure that there was going to be no difficulty with the FSA. I called on Hector Sants and I said, in effect, "It's looking as if we are going to conclude that Bob Diamond is the person we should appoint as Chief Executive. I assume that's not going to cause you any difficulty." His response was, "Not only is that not going to cause me any difficulty, I can tell you now that, if it were, I wouldn't be happy with him where he is now in his present role."

177 Qq 511–4

Mr McFadden: So you never, as Chairman of the company, relayed any of these three or four specific points in the Hector Sants letter to the Chief Executive?

Marcus Agius: As I said in earlier exchanges, I believe that at least two of the comments are generic and would be made of any Chief Executive, and two of them are specific to Bob, namely: "You need to distance yourself from your former colleagues," which is an absolutely right thing to say; and secondly, "You need to improve your knowledge of the side of the bank that you don't know so much about"—absolutely right. I would have relayed those to him.

Mr McFadden: It is quite simple: did you relay these concerns to him?

Marcus Agius: I would have relayed those things to him.

Mr McFadden: So why does he tell us: "I knew nothing about it at the time that I was appointed. I don't know anything about it."

Marcus Agius: I can't speak to his testimony.

Mr McFadden: Do you accept that what he told us and what you have just told us are hard to reconcile?

Marcus Agius: I can't speak to his testimony.

Chair: Well, you could offer a view on that.

Marcus Agius: I could offer a view on that, but the challenge was that the FSA had problems with his appointment and, as I said, from my earlier exchange with Hector Sants they had anything but.

Mr McFadden: But it is your job as Chairman to reflect the concerns of the FSA to the prospective appointee, is it not?

Marcus Agius: Yes. I would challenge the word "concerns". That letter raises four issues and they are called "issues". The word "concerns" I do not believe appears. I am not being pedantic but there is a difference between "these are issues which I would like to raise with you" and "concerns", which means "I'm worried".

Mr McFadden: Did you reflect any of this to him or not?

Marcus Agius: Yes, I did.

Mr McFadden: You did?

Marcus Agius: Yes, I did.[178]

Mr Agius wrote to the Chairman of the Committee on 25 July 2012, after his appearance before the Committee. In this letter he stated that "the FSA were not concerned about Mr

178 Qq 577–85

Diamond's appointment as chief executive". He also said that his own answers to the Committee had been able to provide more clarity and detail than Mr Diamond because he—unlike Mr Diamond—had had the chance to refresh his memory of correspondence between the FSA and Barclays, including the September 2010 letter from Mr Sants.[179]

119. We asked the Chairman of the FSA, Lord Turner, and the Head of the FSA's Prudential Business Unit, Andrew Bailey, for their perspective on their exchanges with Barclays on the subject of Mr Diamond's appointment:

> ***Chair:*** [...] May I take you straight away, Lord Turner, to the letter of appointment that was sent to Barclays? What were you signalling in that letter, and was it of a generic type—the type you normally send out?
>
> ***Lord Turner:*** I think it is a relatively generic type, in that a letter of about that length would be sent—
>
> ***Chair:*** I am not talking about length; I am talking about substance. Come on, let's go straight to the point. Do you normally give these sorts of sets of instructions that are set out in that letter?
>
> ***Lord Turner:*** Yes, there is a list of comments that are specific and issues that have been identified in the interview process. Obviously, the particular ones here were of particular importance, and I know that Hector Sants, in conversation with Marcus Agius, drew attention in addition to particular issues that he was concerned about.
>
> ***Chair:*** Okay; and those concerns were?
>
> ***Lord Turner:*** I know that he explained the FSA's historical concerns regarding Barclays' risk appetite and control framework, and that he drew attention to the fact that Bob Diamond was managing the area of the group where those concerns were foremost, and that it was therefore particularly important, in his new role as CEO, that he ensured continued progress in addressing those concerns.
>
> ***Chair:*** So you were expressing concerns about the way Bob Diamond would approach the job?
>
> ***Lord Turner:*** I don't think it was necessarily specifically about Bob Diamond; it was more that we had a set of concerns about an attitude to risk and a tendency—as we subsequently spelt out in the board meeting and in my letter—to push the limits of approaches to particular issues, and those had tended to come in particular in the areas where Bob Diamond was directly involved.[180]

179 Letter from Marcus Agius to Andrew Tyrie MP, 25 July 2012

180 Qq 1037–40

Conclusions on Mr Diamond's appointment

120. Mr Diamond told the Committee that the occasion of his giving evidence was "the first I've ever heard that there was any question about my appointment as chief executive", and that he did not know about the FSA informing the Barclays Chairman in writing at the time of his appointment. Yet Marcus Agius told the Committee that he raised with Bob Diamond the issues referred to in the letter to him from Hector Sants of the FSA.

121. Mr Diamond was also unable to remember "specific comments" about the need for him to offer challenge to his former long-term colleagues at Barclays Capital, although he was "sure that there were discussions with the regulators during the process of my succession". He said that his memory was "whether, having been associated with the investment bank for a number of years, I would be able to disassociate myself so, as a group chief executive, I would be able to leave the running of the investment bank" to Mr Ricci and Mr del Missier.

122. **We appreciate that Mr Diamond may not have recently read the letter of September 2010 from Mr Sants to Mr Agius in connection with his appointment as Chief Executive when he appeared before us, or have had the discussions about his appointment as chief executive at the front of his mind. However, we find it difficult to accept Mr Diamond's evidence with respect to his apparent unawareness of the matters raised by the FSA with the Chairman of Barclays in connection with his appointment as chief executive in September 2010. The evidence of the Chairman of Barclays is that he did raise them with Mr Diamond, as one would expect. It seems unlikely that they were not raised with him. If they were appropriately raised, it seems unlikely that they would be quickly forgotten.**

123. Mr Agius said that the matters raised in Mr Sants's letter were described by the FSA as "issues", rather than "concerns".[181] He also believed that "at least two" of the four matters raised were "generic and would be made of any Chief Executive".[182] The FSA says, however, that the issues in the letter constituted "a list of comments that are specific and issues that were identified in the interview process. Obviously, the particular ones here were of particular importance". The FSA told us that the Mr Sants also raised with Mr Agius in conversation "the particular issues that he was concerned about".[183] Mr Agius went to see Mr Sants about the appointment "to make sure that there was going to be no difficulty with the FSA", but went away reassured.[184] Lord Turner told us that he did not think that the FSA's concern "was necessarily specifically about Bob Diamond: it was more that we had a set of concerns about an attitude to risk and a tendency—as we subsequently spelt out in the board meeting and in my letter—to push the limits of approaches to

181 Q 583

182 Q 578

183 Q 1038

184 Q 577

particular issues, and those had tended to come in particular in the areas where Bob Diamond was directly involved".[185]

124. **The FSA expressed concerns in connection with the appointment of Bob Diamond as chief executive to Barclays. The concerns were about an attitude to risk and a tendency to "push the limits" in areas where Mr Diamond was directly involved. The concerns were not, however, serious enough to prevent the regulator from approving his appointment. Barclays appears to have regarded the points raised by Mr Sants as "issues" rather than "concerns". On the basis of the evidence it is unclear whether Barclays 'got the message'. To avoid the scope for misunderstanding in future, we recommend that the regulator set out clearly for firms any concerns it has about a senior appointment, listing any actions that it requires. It should ensure that a response is obtained in writing from the firm, undertaking to meet each of the requirements. Failure by the firm to show evidence that the regulatory messages have been seen and acted upon should be considered a serious matter.**

125. The FSA's concerns about Barclays did not go away. On the contrary, they were to be raised by the regulator more forcefully with the Barclays board within eighteen months, little more than a year after Mr Diamond became chief executive.

Mr Diamond's evidence on the FSA letter of February 2012 and subsequent communications between Lord Turner and Marcus Agius

126. On 9 February 2012 Andrew Bailey, head of the FSA's Prudential Business Unit, attended a Barclays board meeting. Such visits to boards are customary annual events for firms such as Barclays.[186] Lord Turner subsequently met Marcus Agius and in April followed that meeting with a letter to the Barclays Chairman, to which Mr Agius responded.[187] Our witnesses had different recollections of these exchanges between the regulator and Barclays. While they were not concerned specifically with the LIBOR issue, they reflected both the culture within Barclays and the state of the relationship the FSA had with Barclays at the time. They also had implications for the subsequent resignation of Barclays chief executive Bob Diamond.

127. The Committee questioned Mr Diamond about the February 2012 board meeting, which he attended, and the subsequent letter from the FSA to Marcus Agius. This was before the Committee had seen either the minutes of the board meeting or the exchange of correspondence in question:

> ***Chair:*** Is it true that, in February this year, the FSA came to the board and expressed their concerns?
>
> ***Bob Diamond:*** I think it's every year, Chairman, in that February meeting that the FSA comes, so—

185 Q 1040

186 Q 1041

187 Q1052. For the text of the letters, see Appendix

Chair: What was said?

Bob Diamond: The context of the discussion when it got to controls, which I think is what you are asking about—I should call it the control environment—was that the focus and the tone at the top was something that they were specifically happy with. In particular, they talked to the board about Chris and I and our relations with the regulators, how we dealt with any situation that came up. I am thinking of PPI—

Chair: Isn't it a bit more specific than that, Mr Diamond? Didn't they tell you that trust had broken down between the FSA and Barclays?

Bob Diamond: I don't recall that in the February meeting.

Chair: Didn't they tell you that they no longer have confidence in your senior executive management team?

Bob Diamond: No, sir.

Chair: And wasn't all this followed up with a letter?

Bob Diamond: There was a discussion that, as it got down into the organisation, they felt that there were some cultural issues—that people sometimes push back; that some of the push-back wasn't always filtered up to the top—so there was an overall discussion on culture. We took some of this as, "This is the annual review from the FSA", and—

Chair: This is the sort of thing they say every year?

Bob Diamond: No, I didn't mean it that way at all, sir—apologies—but it was part of an annual review, so it is always going to have some things that they are going to be critical of and that we can do better. But they were specifically pleased, and said so to the board, with the tone at the top, referring in particular to Chris Lucas and myself and our colleagues on the executive committee.

Chair: Isn't it true that there were challenges from them about your stress tests, your accounting practices, the handling of the Protium deal? Of course, we have subsequently had the debt buy-back scheme, the interest rates swaps problems and of course now LIBOR. Isn't this all part of a pattern?

Bob Diamond: I don't remember anything—I didn't brief before this on the February meeting, so I don't mean to skip over anything, if I am. There was a conversation, I think. There had been a series of things, such as Protium, which became quite an issue between the FSA and ourselves. Without going into the versions of that transaction, because it was a transaction that was approved by the FSA, I think, to be fair—I wasn't the chief executive at the time, so I'm probably speculating a little bit—it was a transaction that created more debate between the FSA and Barclays than probably anyone anticipated when the transaction was done.

> I remember Protium coming up during that meeting in the context of, "Let's not have these types of situations."[188]

Barclays board meeting, 9 February 2012

128. The minutes of the 9 February 2012 Barclays board meeting say the following about what was discussed with Andrew Bailey and subsequently:

> [...]
>
> 5. External Perceptions
>
> There was a perception in the market and amongst some regulators that Barclays was not all that it should be. Barclays is seen as relatively aggressive sometimes and Protium would be an example of being on the wrong side of the line. Mr Bailey emphasised that the relationship with senior management was good. However, at lower levels in the organisation there was a desire to engineer solutions rather than find real answers to regulatory issues. An improvement in attitudes at lower levels would help the relationship with the FSA. Mr Bailey also noted that it was important that external attitudes to Barclays improved.
>
> The Chairman thanked Mr Bailey and his team for presenting these issues to the board and noted that all the issues raised had occupied a lot of the board's time. Significant effort has been directed at improving the relationship with the FSA. There was a debate on the board's approach to Protium [redaction]. It was noted that the FSA received significant pressure from the Financial Policy Committee (FPC) in relation to Barclays. Barclays was continuing to improve disclosures but seems to receive little credit for that.
>
> The board discussed the results of the EBA stress test. Mr Bailey noted that traction on the issues raised by the initial results was only obtained when Bob Diamond and Chris Lucas became involved. [Redaction]

After Mr Bailey and FSA colleagues left the meeting, the board minutes record:

> Barclays was generally perceived as being too aggressive for a number of historical reasons. The senior leadership team took responsibility for the interactions with the FSA at a more junior level and the frustration that that was causing for the FSA.
>
> The board discussed the need to get the tone from the top right so that all interactions with regulators are appropriate at all levels. The issue could and would be addressed. The Group needed to be consistently on the right side of the line to rid itself of the perception of being too aggressive. Resolving this was critical to the future of the Group. [189]

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188 Qq 14–20

189 Extract from Barclays board meeting held on 9 February 2012

In a letter to the Chairman of the Committee of 25 July, after our evidence sessions, Mr Agius said that he had "taken the opportunity to revisit recollections of that February board meeting with fellow Non Executive Directors, and all, to whom I have spoken, recall it precisely as the minutes record it".[190]

Lord Turner's subsequent meeting with, and letter to, Marcus Agius

129. Lord Turner subsequently met Marcus Agius to reinforce the message to the board that Andrew Bailey had delivered. That meeting was followed up by a letter from Lord Turner to which Mr Agius responded. Lord Turner told us:

> Well, after Andrew had been to the board, and before it, in the regular briefing sessions that I would have with Andrew and Hector, we had, on a number of occasions, discussed this pattern of behaviour from Barclays, and we had discussed the fact that it would be good for Andrew to talk about it at the board; but subsequently we decided we should reinforce that by a meeting and a letter from myself.[191]

130. The letter from Lord Turner and the reply from Marcus Agius are set out in full in the Annex to this Report. Lord Turner's letter included the following messages to Barclays:

> As promised, this letter follows up our recent meeting and sets out FSA concerns relating to aspects of Barclays' approach to regulatory and other issues.
>
> Obviously where we have specific areas of concern which merit it, our Supervisory Team will directly make those concerns known at the appropriate level, and require any appropriate action in response. The purpose of my meeting with you was therefore not to focus on any one specific issue which requires remedial action. Rather I wished to bring to your attention our concerns about the cumulative impression created by a pattern of behaviour over the last few years, in which Barclays often seems to be seeking to gain advantage through the use of complex structures, or through arguing for regulatory approaches which are at the aggressive end of interpretation of the relevant rules and regulations. Andrew Bailey also expressed these concerns at your Board meeting on 9th February.
>
> [...]
>
> Clearly these examples vary in both currency and importance. And it is of course acceptable for a bank to argue for a favourable approach on any one specific issue, even if the regulator does not immediately agree. But the cumulative effect of the examples set out above has been to leave us with an impression that Barclays has a tendency continually to seek advantage from complex structures or favourable regulatory interpretations. These concerns are sufficiently great that I felt it was appropriate to communicate them directly to you, and to urge you and the Board to

190 Letter from Marcus Agius to Andrew Tyrie MP, 25 July 2012

191 Qq1052

> encourage a tone of full co-operation and transparency between all levels of your Executive and the FSA.
>
> I know from our conversation that you take these issues seriously.[192]

131. When Mr Agius wrote back to Lord Turner he said:

> It is a matter of regret for us that you have the concerns outlined in your letter. Barclays has invested significant effort and time in building and improving its relationship with the FSA. It is very important to us to have a strong, open, cooperative and transparent relationship with the FSA and with all of our regulators globally. The Board and I took note of Andrew Bailey's comments in our February meeting and, while he specifically excluded Bob Diamond and Chris Lucas from his comments, it was clear that "tone from the top" is one of the FSA's concerns. Our objective is and has always been to have a strong and mutually beneficial relationship with the FSA and you have my commitment that we will work harder in the future to procure this outcome.[193]

Assessment of Bob Diamond's evidence to the Committee

"Tone from the top"

132. We asked Mr Diamond what was said when the FSA came to the February board meeting. He said:

> The context of the discussion when it got to controls, which I think is what you are asking about—I should call it the control environment—was that the focus and the tone at the top was something that they were specifically happy with. In particular, they talked to the board about Chris [Lucas] and I and our relations with the regulators, how we dealt with any situation that came up.[194]

The minutes of the board meeting record that "The board discussed the results of the EBA stress test. Mr Bailey noted that traction on the issues raised by the initial results was only obtained when Bob Diamond and Chris Lucas became involved." Mr Agius, referring to his own letter to Lord Turner which said that the "it was clear that 'tone from the top' is one of the FSA's concerns, told us that by this "I meant, in the context of what we were told by the FSA at the Board meeting, that those at the top, including Mr Diamond, needed to ensure that those at lower levels were not acting in the way noted by the FSA".[195]

133. Lord Turner and Mr Bailey of the FSA responded to the Committee's questions on these points as follows:

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192 Letter from Lord Turner to Marcus Agius, 10 April 2012

193 Letter from Marcus Agius to Lord Turner, 18 April 2012

194 Q 15

195 Letter from Marcus Agius to Andrew Tyrie MP, 25 July 2012

> ***Chair:*** Did you say to them that the tone at the top was of concern?
>
> ***Andrew Bailey:*** Yes, and I think they have now provided you with a summary of the board meeting. I've only seen that in the last few days, and the interesting thing for me was to see the summary of the discussion after I left. I gave, as I tend to do, a reasonably short presentation in which I highlight usually only three or four things that are material to us, and members of the board then ask me questions; and then I left. You will have seen it but to recap, it says that the board discussed "the need to get the tone from the top right".
>
> ***Chair:*** And you don't distinguish between tone at the top and from the top—they mean the same thing, do they, Lord Turner?
>
> ***Lord Turner:*** I would have thought they are pretty much the same. I don't know whether Andrew intended any distinction, but I can't see a particular distinction there.
>
> ***Andrew Bailey:*** It finishes by saying that resolving this was "critical to the future of the group." Let me make one point that I think has come up in a number of your hearings. I did make the very clear point in my presentation that while we had a whole series of issues with the firm, I did not have evidence that Bob Diamond personally was involved. This was about the behaviour of the firm, of which he was obviously the chief executive.
>
> ***Chair:*** And therefore responsible.
>
> ***Andrew Bailey:*** Yes. And I was very careful about this, because had I gone into the board and levelled an allegation about Bob Diamond personally, then I think the board would have reacted very negatively. They would have challenged me on the evidence, and I did not have the evidence. So I was very careful to make that distinction.[196]

Mr Bailey added later in our evidence session with him in response to questioning:

> ***Chair:*** Perhaps we could turn to the evidence that Mr Diamond gave to us. He said that the "context of the discussion when it got to controls … I should call it the control environment—was that the focus and the tone at the top was something that they"—you, that is—"were specifically happy with." This is in answer to question 15.
>
> ***Andrew Bailey:*** Yes. I think this comes back to the point I made a few minutes ago, which is, I was very careful—I didn't use the term "tone from the top"; that's the term that Barclays have used—to make this distinction between the behaviour that I could observe, the direct behaviour that I could observe of Bob Diamond, and the behaviour of the firm.[197]

196 Qq 1042–4

197 Q1056. It is interesting to note that the Group of Thirty report *Toward effective governance of financial institutions* refers to "the tone set at the top" or "tone at the top" on pp 21, 49, 65 and 66

> [...]
>
> ***Jesse Norman:*** Okay. What were your specific concerns, Mr Bailey, about Mr Diamond?
>
> ***Andrew Bailey:*** My specific concern was exactly this point about the tone from the top. Although I could not find the evidence that he personally had his hands on these things, you really could not escape the fact that the culture of this institution was coming from the top. Frankly although, interestingly, the relationship with Bob Diamond was not antagonistic, this was not something where he would come in and shout at me—or indeed, I think Hector Sants—and he would often say, "I hear what you are saying", I could not see a pattern where that was leading to the action that we needed.[198]

134. **Mr Bailey does not recall saying that he was "specifically happy" about the tone at the top—in fact he says that the phrase "tone at the top" is Barclays' own. Mr Diamond, however, told us that the regulator was specifically pleased with his relationship with the FSA. The FSA told us that it had concerns about its relationship with the firm, but was not able to point to evidence directly linking those concerns to the behaviour of Mr Diamond. However, as Chief Executive he was responsible for the state of his firm's relationship with the regulator, and for demonstrating to the regulator that the necessary action was being taken to remedy shortcomings. The fact that the Barclays board discussed the need to get the "tone from the top" right, and how important this was to Barclays, after Mr Bailey left the board meeting, suggests that the Barclays board did appreciate his message. This appreciation was lacking in Mr Diamond's evidence. We do not accept Mr Diamond's evidence on this point. It stands in contrast to the evidence of Mr Bailey and the minutes of the discussion at the board meeting. It seems certain that Mr Bailey did express concern to the board. It is possible that Mr Diamond did not appreciate the significance of what was said. If so, this lack of appreciation could be considered part of the problem which the FSA was seeking to address.**

Trust or distrust between the FSA and Barclays?

135. Mr Diamond told us that he did not recall the FSA saying to the Barclays board that trust had broken down between the FSA and the company.[199] Mr Agius told us that the statement that "trust had broken down between the FSA and Barclays" was not made by FSA officials at the board meeting.[200] Mr Bailey, however, when asked whether he had said at that meeting whether that he felt that trust had broken down between the regulator and Barclays, told us that:

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198 Q 1078

199 Q 16

200 Letter from Marcus Agius to Andrew Tyrie MP, 9 July 2012

I did, certainly in respect of at least one of the issues that I used to illustrate it, to say that it had led to—I think I used the word "distrust".[201]

The severity of the issues discussed

136. Mr Diamond told the Committee that at the board meeting with the FSA:

> ***Bob Diamond:*** [...]We took some of this as, "This is the annual review from the FSA", and—
>
> ***Chair:*** This is the sort of thing they say every year?
>
> ***Bob Diamond:*** No, I didn't mean it that way at all, sir—apologies—but it was part of an annual review, so it is always going to have some things that they are going to be critical of and that we can do better.[202]

137. We asked Mr Bailey for his views on this part of Mr Diamond's evidence:

> ***Chair:*** Could they have mistaken all these exchanges to be what goes on in any annual review?
>
> ***Andrew Bailey:*** I don't think so, for two reasons. First of all, I can say that in all the ones I've done in the last about 15 months, this is the only time that we've followed it up with a letter from Adair, and a meeting with the chairman. Secondly, when I saw, as I quoted earlier, the minute of the board meeting, it left me, I think, convinced that there was no question that they understood the point.
>
> ***Chair:*** So when Mr Diamond said to us "it was part of an annual review, so it is always going to have some things that they are going to be critical of and that we can do better"—that was his reply to me on this point—would that have struck you as somewhat misleading?
>
> ***Andrew Bailey:*** I don't think that in any sense conveys the severity of the issue, and I think that's reflected in the board minutes. I don't think that captures the severity of the point we were making.[203]

138. **The impression that Mr Diamond gave to the Committee as to the significance of the FSA's message to the 9 February 2012 board meeting sits uneasily with Barclays' own board minutes. Mr Bailey of the FSA has also told us that in his view the evidence from Mr Diamond to the Committee failed to convey the severity of the matters under discussion.**

201 Q 1045

202 Qq 18–19

203 Q 1057–8

The April 2012 letter from Lord Turner

139. Lord Turner expressed surprise that Mr Diamond had not mentioned Lord Turner's letter of 10 April 2012 to the Committee when giving evidence:

> ***Chair:*** You've read the evidence overall. Do both of you consider it to be a reasonable and fair assessment of their relationship with you at this time, or one that left gaps which could have led Parliament to be misled?
>
> ***Lord Turner:*** The bit of the evidence which I was most surprised at was the bit that you have just focused on, where you asked, was there a letter and was this an issue of importance, because, let us be absolutely clear: Mr Diamond knew that there had been that letter. Indeed, at a subsequent meeting, which was on another subject—with myself, Hector Sants and Andrew, with the chairman, Chris Lucas, the finance director, and Bob Diamond—at the end of it, he said, "We would like to talk about the letter" and he said, "I am extremely concerned to receive this letter and we take very seriously what you said." And he said how distressed they were to have received a letter.
>
> ***Chair:*** Quite a gap.
>
> ***Lord Turner:*** So that was the bit. Quite a bit of the evidence—people sometimes do mis-talk under the pressure of your questioning. But that was the bit that, frankly, surprised me.
>
> ***Chair:*** I have never noticed you do that, Lord Turner. But in any case, you are basically saying that we were not left with a full and fair impression of what went on in those exchanges as a consequence. Is that correct?
>
> ***Andrew Bailey:*** Yes, it's a highly selective choice, in my view.
>
> ***Chair:*** Yes, and, taken together, could be construed as misleading, which seems to have some similarity—does it not?—with the accumulation of concerns at the regulatory level which you find of concern, where any individual one might not be. Is that fair?
>
> ***Andrew Bailey:*** Well, you can see a sort of similar strain of pattern of behaviour, yes.[204]

140. We raised the letter from Lord Turner with Mr Agius. He told us that the letter was discussed by the board of Barclays:

> ***Chair:*** You remember the letter very well, don't you?
>
> ***Marcus Agius***: Yes, I do.
>
> ***Chair:*** And it made an impact on you.

204 Qq 1059–61

Marcus Agius: It did.[205]

[...]

Mr Ruffley: [...] when this FSA letter on 10 April was received by you—the "Dear Marcus" letter—what discussions did you have with Mr Diamond thereafter? What day and how long did it last?

Marcus Agius: I cannot remember what day it was, but I remember discussing it with him and with other relevant officials inside Barclays.

Mr Ruffley: And what did Mr Diamond say when you informed him of it? No doubt you gave him a copy of this letter, didn't you?

Marcus Agius: I would certainly have given him a copy of this letter.

Mr Ruffley: You would or you did?

Marcus Agius: I would have.[206]

141. Mr Diamond wrote to the Committee on 10 July following his appearance before us, referring to the meeting with Mr Agius:

> Having watched the Committee's session today, I was dismayed that you and some of your fellow Committee members appear to have suggested that I was less than candid with the Committee last week. Any such suggestion would be totally unfair and unfounded.
>
> The focus of your concern appears to relate to correspondence between Messrs. Turner and Agius in April 2012. The questions asked of me, however, concerned the period of my promotion in September 2010 and the board meeting I attended in February 2012. As the letters of April 2012 make clear, those letters followed an April meeting between Messrs. Turner and Agius which I did not attend. I was not asked about the April 2012 meeting nor was I asked about nor shown follow up letters to that April meeting at our session.[207]

142. Mr Agius wrote to the Committee on 25 July and said in respect of Mr Diamond's evidence on the letter from Lord Turner:

> You also questioned Mr Diamond about whether the FSA's comments at the February Board meeting were followed up with a letter. It appeared from the questioning during Mr Diamond's appearance that there was a misunderstanding about the nature of that letter. In particular, the questions put to Mr Diamond implied that the letter followed the Board meeting directly. As you now know, the letter in question was sent by Lord Turner to me on 10 April 2012 to follow up on a

205 QQ564–5

206 Q 620–2

207 Letter from Bob Diamond to Andrew Tyrie MP, 10 July 2012

> meeting between Lord Turner and myself in March 2012—separate from, and two months after, the Board meeting.
>
> Based on the information given to Mr Diamond in the question asked, he explained his position clearly in his response to the Committee: "I don't remember anything—I didn't brief before this on the February meeting, so I don't mean to skip over anything, if I am. There was a conversation, I think. There had been a series of things, such as Protium, which became quite an issue between the FSA and ourselves."[208]

143. **Lord Turner's letter to Mr Agius was described by the former as a follow up to the meeting between them which was itself a follow up to the February 2012 Barclays board, meeting at which Mr Bailey spoke. The fact that it was not described to Mr Diamond as a follow up letter to the April meeting between Lord Turner and Mr Agius is scarcely relevant. What matters is that it was part of a process of following up a board meeting which he attended and about which he was prepared to tell us virtually nothing in evidence.[209] We accept Mr Bailey's conclusion that Mr Diamond's evidence on this point was "highly selective". We also note that Lord Turner was "surprised" at Mr Diamond's apparent ignorance of the letter. Our conclusion is that Mr Diamond's evidence was unforthcoming and highly selective on this point.**

Conclusion on Bob Diamond's evidence

144. **We have considered the evidence of Mr Diamond and other witnesses on Barclays' relationship with the FSA. His evidence denying that the FSA felt that trust had broken down between itself and Barclays is inconsistent with that of Mr Bailey. We are unable to accept Mr Diamond's assessment of the seriousness of the matters discussed at the February 2012 board meeting: in the light of all the circumstances, it seems to us inconceivable that Mr Diamond could have believed that the FSA was satisfied with the tone at the top of Barclays when the evidence from the FSA is that this was not the case. He did not mention the important and trenchant letter of Lord Turner to Mr Agius, setting out major concerns of the FSA, when he had ample opportunity to do so. It is very unlikely that he was unaware of that letter, or its significance as a follow up to the firm messages given to the Barclays board by Mr Bailey in February 2012.Having heard the evidence of Mr Diamond and the FSA on these points, the Committee prefers the evidence of the FSA. Select committees are entitled to expect candour and frankness from witnesses before them. Mr Diamond's evidence, in the Committee's view, fell well short of the standard that Parliament expects.**

208 Letter from Marcus Agius to Andrew Tyrie MP, 25 July 2012

209 It is true that Mr Diamond was not shown the follow up letters "at our session", but that was because they had not been seen by or sent to the Committee until Barclays supplied them to the Committee at our request on 9 July, five days after Mr Diamond's evidence.

Relations between Barclays and the FSA

The February board meeting

145. Mr Agius was asked by the Committee about the board meeting that Andrew Bailey of the FSA attended in February 2012 and the subsequent exchange of letters between Lord Turner and Mr Agius. He said that:

> Every year when the FSA comes to see us, they do not, as you would expect, say, "Everything that you are doing is absolutely perfect." They seek to find those areas where they think further attention needs to be paid, and that is what they tend to review with us. That is what tends to happen.[210]
>
> [...]
>
> When they come and do our annual reviews, what they always do is say, "These are the areas where we think you are doing well, and these are the areas where we think you need to try harder," like any other annual review. I do not mean to trivialise them, but that is the essence of what happens. When the FSA visits us and they say, "Here are areas where we would like to see progress," we take that as being part of the normal course of the interchange.[211]

146. The impression he was trying to give, however, that the February 2012 board meeting was part of the normal course of interaction with the regulator, is not borne out by the evidence we heard from Mr Bailey himself. Mr Bailey also noted that the Barclays board minutes had shown that the board had grasped the seriousness of what he had told them:

> ***Chair:*** Mr Bailey, may I turn to your appearance at the board? What led you to go to the board in February 2012 this year?
>
> ***Andrew Bailey:*** I aim to go to the boards of all major institutions around once a year, so in that sense it was not a special event. What led me to raise the points that I did, and particularly the point concerning our view on the behaviour of the firm, was—this was set out subsequently in a letter to Marcus Agius—a series of events, quite a few of which had occurred before I moved to the FSA, and some of which occurred subsequently. Those events led me to be concerned about the behaviour of the firm in relation to us, and there was a repeated pattern of such behaviour that was not showing signs of changing.[212]
>
> [...]
>
> ***Chair:*** [...] Did you make all the points that were set out in that letter much later?

210 Q 554

211 Q 561

212 Q 1041

Andrew Bailey: I think I made a number of those, and I think the letter then actually gives a complete set of the issues.

Chair: I'd be reluctant to ask too many leading questions, but let's just try a few. Would you say that it would be an unreasonable summary of the letter that you felt Barclays were trying it on?

Andrew Bailey: Yes. The sort of words that we would frequently use were that there was a sort of culture of gaming—gaming us.

Chair: And that the regulator had had enough.

Andrew Bailey: Yes.

Chair: And you were reading the Riot Act at that meeting in February.

Andrew Bailey: Yes. Bear in mind, this was very much consistent with the changes that we want to make in the style of regulation—that is judgment-based—and I always say to the boards when I go to see them, we are here only to highlight the big issues of concern in our judgment.

Chair: And you were saying to them, basically, "This is no way to run a bank".

Andrew Bailey: That it had to change.

Chair: You would agree with that phrase.

Andrew Bailey: Yes, I would.[213]

[...]

Chair: Could they have mistaken all these exchanges to be what goes on in any annual review?

Andrew Bailey: I don't think so, for two reasons. First of all, I can say that in all the ones I've done in the last about 15 months, this is the only time that we've followed it up with a letter from Adair, and a meeting with the chairman. Secondly, when I saw, as I quoted earlier, the minute of the board meeting, it left me, I think, convinced that there was no question that they understood the point.[214]

[...]

Jesse Norman: The FSA followed up your appearance on 9 February with a letter which was sent to Marcus Agius on the 10th. Now, you've suggested to us that just Mr Agius's characterisation of the relationship as, as it were, normal cut and thrust, or some concerns about Jerry at the top, was actually misleading. Is that right, Mr Bailey?

213 Qq 1046–51

214 Q 1057

> ***Andrew Bailey:*** Well, I think that, as the board minutes suggest, this is a wholly different magnitude of issue to the sort of things—we normally discuss big issues, but this was a wholly different magnitude.
>
> ***Jesse Norman:*** Right. It's a different scale.
>
> ***Andrew Bailey:*** Yes.
>
> ***Jesse Norman:*** You're going in there and you're giving them a bollocking.
>
> ***Andrew Bailey:*** Yes.
>
> ***Jesse Norman:*** Because a whole series of things have gone wrong and you're angry about it.
>
> ***Andrew Bailey:*** I'm angry about it and I'm also very clear that we had to grasp this nettle. This pattern of behaviour had been going on. You look at the cases in Adair's letter to Marcus Agius: they go back over a period of time. We had to grasp this issue.[215]

Mr Bailey also said that he had "never had a conversation of this type with a board" and that Barclays was an "outlier" compared with other institutions.[216]

Exchanges with Lord Turner

147. The FSA followed up Mr Bailey's comments to the board with a meeting between Lord Turner and Mr Agius and the subsequent letter of 10 April. This, Lord Turner said, was in order to "reinforce" Mr Bailey's visit to the board.[217] He would expect the bank to take such a meeting "very seriously" and for the chairman to talk to the chief executive about it.[218] His letter of 10 April was the only such letter he had sent in his time as Chairman of the FSA.[219]

148. We asked Mr Agius for his interpretation of his meeting with Lord Turner and the letter to him from Lord Turner of 10 April. He told us that:

> When any bank deals with its regulator, it has to deal with very complex matters. It is not like a speed cop catching you for going more than 30mph in a 30mph speed limit. Very often the points that are raised and the issues that are discussed are complex and capable of interpretation and are capable of debate. We have historically chosen to debate with our regulators whenever we thought it appropriate

215 Qq 1062–5

216 Qq1075–7

217 Q 1052

218 Qq1054–5

219 Q 1081

> in order to ensure that whatever regulatory decision arrived at was the appropriate one in all the circumstances.[220]
>
> [...]
>
> [...] we invariably seek to try to achieve the best regulatory outcome with our regulators by engaging them, not with a view to doing anything we should not do but just trying to manage the process. Very often we say, "Fine, we understand what you are trying to do and we are happy with that." Sometimes they say, "No, I see your point," and a different outcome is reached. What that letter is saying is that we overdid it.[221]
>
> I think that Lord Turner was interviewing me as Chairman of Barclays, as he should have done, to say, "Look, when we deal with you, you try too hard." He does not say that anything we are trying to do is improper or anything we are trying to do is incorrect, but that in trying to seek the best outcome for the bank we are testing the goodwill of his staff, and I understand that.[222]

In his letter to the Chairman in advance of his appearance before the Committee Mr Agius referred to his reply to Lord Turner:

> Robust expressions of particular concerns by a regulator in relation to regulated institutions take place in the normal course and do not of themselves merit the conclusion that there has been a breakdown of trust. You will see, however, from my reply, that Barclays accepted the importance of Lord Turner's comments and undertook to act upon them.

Mr Agius denied trying to play down the letter from Lord Turner, and told us that it was "a very serious letter".[223] Mr Agius did not accept that relations with the FSA were "desperate", but conceded that they could be described as "strained".[224]

149. Mr Agius attempted to draw a distinction between the message received from Mr Bailey at the board meeting and the exchanges with Lord Turner. Mr Agius said that "the letter from [Lord] Turner was separate".[225] He told us that "when Mr Bailey came to see us, he said the tone at the top was satisfactory". His response to Lord Turner's letter, however, said that "it was clear that the 'tone from the top' is one of the FSA's concerns".[226] The difference was because "that is a different exchange from the visit to the board, and it was as a result of my interview with Lord Turner and his subsequent letter".[227] He thought that

220 Q 522

221 Q 525

222 Q532

223 Q549

224 Q531 and Q 534

225 Q 553

226 Letter from Marcus Agius to Lord Turner, 18 April 2012

227 Q 591

the concern about the tone from the top was “a forward-looking statement”.[228] Mr Bailey, however, told us that his concern in February was specifically about the tone from the top: “the culture of this organisation was coming from the top”.[229]

A new approach by the FSA?

150. In 2009 Lord Turner said:

> [...] we are imposing at firm level a far more assertive style of supervision, no longer willing to assume that market discipline and incentives will always lead bank management to make optimal decisions; more willing to make judgements on whether business models and business strategies create undue risks for the whole financial system.[230]

The Governor of the Bank of England in his Mansion House speech in 2011 assessed the new system of financial regulation:

> The style of regulation will also change with the PRA. Process—more reporting, more regulators, more committees—does not lead to a safer banking system. [...] I believe that we can operate prudential supervision at lower cost than hitherto by reducing the burden of routine data collection and focussing on the major risks to the system. It is vital that we collect and process data only where the supervisors have a need to know. Targeted and focussed regulation, allowing senior supervisors to exercise their judgement, does not require ever-increasing resources. For example, we will reduce the number of people subject to the intensive regulatory interview process before appointment by limiting such interviews to the most senior people.[231]

Lord Turner and Andrew Bailey told us that their dealings with Barclays represented a different approach to regulation on the part of the FSA from that of the recent past:

> ***Jesse Norman:*** In your view, was the FSA tough enough before you came in, Mr Bailey?
>
> ***Andrew Bailey:*** You have to put this in the context of the change in approach to supervision over the last year since the crisis. This is exactly where we are taking it to now. This is the most dramatic intervention but it is consistent with—Adair and Hector were very much on side with this—what we are doing with supervision, to respond to the identified problems of the past.
>
> ***Lord Turner:*** I think the honest answer, Mr Norman, is that we would never have done this back in ’07 and ’08. We have been on a journey towards a tougher style of supervision in all sorts of ways. That has a tougher style in relation to issues of

228 Q 594–6

229 Q 1078

230 Speech by Adair Turner, Chairman, FSA, The City Banquet, the Mansion House, London, 22 September 2009

231 Speech by Sir Mervyn King, Governor of the Bank of England, Lord Mayor’s Banquet for Bankers and Merchants of the City of London, the Mansion House, 15 June 2011

substance like capital liquidity asset quality. But more recently and, indeed, Hector Sants signalled that in 2010 when he made a speech about culture, we have been saying, "Do we have to reinforce those tougher messages on the specific quantitative issues of capital liquidity asset quality with tougher messages on culture as well? It is the accumulation of a change in the style of FSA supervision which really began six months before I joined the FSA. I joined in September 2008 but a change had been launched initially in about April 2008 but it takes time to drive those changes through.[232]

View of the Bank of England

151. Lord Turner copied his letter of 10 April to the Governor of the Bank of England, Sir Mervyn King.[233] Sir Mervyn told us that "Adair Turner and Andrew Bailey had shared with me for many months their concerns about Barclays. If you read Lord Turner's letter of April to Mr Agius it could hardly be clearer. It is a very powerful and strong letter".[234] He also said that "I think that all of us involved have built up a genuine concern that it is possible to sail close to the wind once; you can sail close to the wind twice—maybe even three times—but when it gets to four or five times and becomes a regular pattern of behaviour, you have to ask questions about the navigational skills of the captain on the bridge. That is what Lord Turner and Andrew Bailey made very clear to the board".[235] He believed, however, that the Barclays board "was deeply reluctant to face up to the concerns that Lord Turner and Andrew Bailey suggested. I think it thought that it might be able to tough it out. It was not convinced that the regulators had lost confidence". The senior non-executive director told Sir Mervyn that only at their meeting on 2 July had he been fully aware of the loss of confidence of the regulators in the senior management.[236]

FSA governance review

152. Mr Agius told us that the FSA had recently undertaken a "governance review" of Barclays and that Barclays had received a letter saying that its governance was deemed "satisfactory". He added that the official conducting the review had said told him that she had ranked Barclays "best in class".[237] Mr Bailey told us that the governance review was part of the FSA's recently-introduced "core prudential programme" which focused on what he called "form of governance", and in particular the board and its committees. He contrasted this with his concerns about the substance of Barclays' governance, which was "not working".[238]

232 Q 1079

233 Q 1074

234 HC 535, Q28

235 HC 535, Q38

236 HC 535, QQ 39–40

237 Q 543

238 Q 1161

153. Barclays subsequently sent us the correspondence between the FSA and Mr Agius following this governance review. The FSA told Barclays that:

> [...] both the design and the effectiveness of the Board and Board Committees are satisfactory [...] Board members have a sound understanding of the role of the Board in setting the tone from the top [...] our conclusion was that the Board acts as a cohesive group and we saw no evidence of individuals trying to dominate the Board [...] In our assessment, the current Board is an effective counterweight and challenge to executive management.[239]

The FSA did raise "a handful of vulnerabilities", covering: "effective governance over a global investment bank"; "some growing tensions in the way that the Board process is managed"; "reliance on key individuals"; and "decision-making under pressure". The last point was in relation to the impairment and buy-back of Protium assets. The FSA was concerned that "the strengths we have seen throughout our Governance Review have the potential to turn into weaknesses when certain pressures are brought to bear". The FSA thought that specialism on the board meant that NEDs looked to one NED for comfort, who in turn worked closely with the finance director. It questioned how much challenge was provided by the board and its committees to the Executive on this matter.[240]

154. Mr Agius responded to the FSA on these points on 10 February, the day after the board meeting that Mr Bailey attended. He told the FSA that Barclays was determined "to build a world class corporate governance system that delivers outstanding results for our stakeholders. I am pleased that you have found the system to be both designed and operating effectively. We shall, of course, consider very carefully the issues raised in your report and how to address them". He disagreed with the FSA on Protium: "the governance over this issue was extremely thorough ... effective challenge was provided by the Board and its Committees and I do not accept that the decision-making on impairment was made primarily between two people".[241]

155. The FSA's report into the failure of the Royal Bank of Scotland raised questions about the former chief executive of that bank's capability, style and impact on the business. These included "whether his management style might have discouraged robust and effective challenge from the Board and senior management team", although it said that, based on interviews with RBS board members, the picture that emerged "was clearly more complex than the one-dimensional 'dominant CEO' sometimes suggested in the media".[242] As the FSA said, a dominant CEO "can result in a lack of effective challenge by the board and senior managers to the CEO's proposals, resulting in risks being overlooked and strategic mistakes being made".[243] In the case of Barclays, the FSA raised issues at the time of Mr Diamond's appointment and subsequently expressed concerns about the leadership of the

239 Letter from FSA to Marcus Agius, 11 January 2012

240 Ibid

241 Letter from Marcus Agius to FSA, 10 February 2012

242 The failure of the Royal Bank of Scotland, FSA, December 2011, paras 612, 610

243 Ibid, para 609

bank to the board. As described in the next chapter, the regulators lost faith in the Barclays Chief Executive. **The Parliamentary Commission on Banking Standards' examination of the corporate governance of systemically important financial institutions should consider how to mitigate the risk that the leadership style of a chief executive may permit a lack of effective challenge or to the firm committing strategic mistakes.**

Appointment of Jerry del Missier as Chief Operating Officer

156. On 22 June, only a week before the FSA published its Final Notice, Barclays appointed Jerry del Missier as its Chief Operating Officer. Mr del Missier was responsible for passing his instruction in October 2008 that Barclays should make LIBOR submissions that were 'within the pack' of other banks (see section 4 of this Report). Given this involvement, we asked Mr Agius about the decision. He replied:

> We debated that very carefully, as you would imagine. The factors that were in our mind were, first of all, whether it was a genuine misunderstanding or not, and secondly, because it was even better for them to ask whether the FSA concluded the same thing. The FSA specifically said there was no issue to raise in respect of Jerry del Missier's behaviour.[244]

When asked about the FSA's role, Lord Turner told us:

> It is important to realise that there was no formal approval process required for Mr del Missier, because the nature of the job that he was moving from to did not involve a change in status in terms of what he had already been approved for. I know that this is an issue to which Andrew Bailey gave consideration. It was not something that he and I discussed in detail. I trust Andrew's judgment and I left it to him. We did not have a discussion about it. [...] But his point of view I know, because he talked to me this morning and said, "If this question comes up, here's what I did." I know he did talk with Bob Diamond about it and say, "Look, do you want to do this, given what is about to happen on LIBOR, given that, although there is no case being found against Mr del Missier, there may be a lot of public comment?" But Andrew did not believe that it was sufficiently clear what had to happen there that he should stop it occurring at that stage, though I think he had doubts about it. But the crucial thing is, because he was not changing the definition of the role that he was doing, it did not involve a change of status. If he had been going to a chief executive role, it would have been a different position in our hierarchy of significant influence functions, and therefore there would have had to have been a formal approval process. But there did not need to be a formal approval process in this case.[245]

Mr del Missier resigned as Chief Operating Officer on 3 July 2012, just 11 days after his appointment.

244 Q 793

245 HC 535, Q 84

Conclusions on FSA relationship with Barclays

157. Mr Agius denied misunderstanding the seriousness of relations with the FSA, and sought to give the impression that the February meeting was one that might be expected between a regulator and a bank. He also drew a distinction between the messages delivered by Mr Bailey in February 2012 and that from Lord Turner in April. Both of these interpretations are contested by the FSA, who said that the Bailey visit and the Turner exchanges arose from the same concerns and were part of a single process, and that the visit of Mr Bailey was quite different in character from normal regulatory exchanges. For Mr Bailey the minutes of the Barclays board were significant. He considered that the board had realised the seriousness of affairs. Yet, according to Mr Agius, the Chairman only realised it when he later met and then, in April, corresponded with Lord Turner. This looks implausible, but the senior non-executive director told the Governor of the Bank as late as 2 July that he had not, until that moment, appreciated the loss of confidence on the part of regulators in the senior executive management of Barclays.

158. Barclays has told us that at the same time it was receiving the comments of Mr Bailey, it received more positive comments arising from the FSA's governance review. The FSA's governance reviewer reportedly described Barclays as "best in class" to Mr Agius for its forms of governance. Mr Bailey drew a distinction between the forms of governance that this review examined and the substance of governance he was concerned about. However, the evidence of the correspondence between the FSA and Barclays following the governance review is that the FSA did judge both the design and effectiveness of Barclays' governance structures to be satisfactory. The review fell short of giving Barclays a completely clean bill of health: it pointed out potential vulnerabilities in the firm's governance. The picture is therefore more nuanced than described either by Barclays or by the FSA in oral evidence, but **it is at least possible that the message from the FSA's governance review may have obscured some of the messages that Mr Bailey and Lord Turner thought they were hammering home to the Barclays board.**

159. **The messages that Lord Turner and Mr Bailey gave to the Barclays board this year provide evidence of the evolution of a more judgement-led approach on the part of the FSA. Lord Turner said that the change to this approach began as long ago as 2008, and it featured in his Mansion House speech in 2009. Judgement-led regulation is welcome: the FSA has concentrated too much on ensuring narrow rule-based compliance, often leading to the collection of data of little value and to box ticking, and too little on making judgements about what will cause serious problems for consumers and the financial system. In February, though, the FSA judged that it was the overall culture, rather than just a particular behaviour, of Barclays that represented a risk, and so took steps to address this directly. This intervention was not routine or coded. It was a loud and clear expression of the concerns the FSA had about the culture at Barclays and should have been clearly understood by the board. This innovative action is also welcome. The episode shows, however, that judgement-led regulation will require the regulator to be resolutely clear about its concerns to senior figures in systemically important firms.**

6 The resignations

Barclays' initial reaction to the Final Notice

160. The FSA Final Notice was published on 27 June 2012. That same day, Barclays put out a statement, *Barclays Bank PLC Settlement with Authorities.* The statement noted that the settlement was "part of an industry-wide investigation into the setting of interbank offered rates across a range of currencies" and that the bank had "received credit from the Authorities for its extensive co-operation, as well the actions it has taken to enhance its systems and controls in response to the identification of the past issues giving rise to these resolutions". The statement contained quotes from Mr Diamond and Marcus Agius. Mr Diamond said:

> The events which gave rise to today's resolutions relate to past actions which fell well short of the standards to which Barclays aspires in the conduct of its business. When we identified those issues, we took prompt action to fix them and co-operated extensively and proactively with the Authorities. Nothing is more important to me than having a strong culture at Barclays; I am sorry that some people acted in a manner not consistent with our culture and values.

Mr Agius stated:

> The Board takes the issues underlying today's announcement extremely seriously and views them with the utmost regret. Since these issues were identified, the Authorities acknowledge that Barclays management has co-operated fully with their investigations and taken, and continues to take, prompt and decisive action to correct them.

161. In the statement, Mr Diamond announced that "to reflect our collective responsibility as leaders, Chris Lucas, Jerry del Missier, Rich Ricci and I have voluntarily agreed with the Board to forgo any consideration for an annual bonus this year."[246] This gesture was welcomed by Mr Agius, who stated that "the Board welcomes the example set by Bob Diamond, Chris Lucas, Jerry del Missier and Rich Ricci in recognising their collective responsibility as leaders of Barclays."[247]

162. The decision by just four Barclays executives to "forgo any consideration for an annual bonus this year" was widely seen as an insufficient response by Barclays given the scale and gravity of the misdemeanours. In the days that followed the publication of the Final Notice there was much commentary in the media that the waiving of bonuses was not enough. For example, the Guardian wrote that "The outside world will want to know why no director of Barclays has offered his resignation - a voluntary waiving of boardroom

246 Chris Lucas is the Finance Director at Barclays and along with Mr Diamond one of only two executives to sit on the main board. Rich Ricci is Chief Executive of Corporate and Investment Banking and a member of Barclays Executive Committee

247 Barclays Announcement, *Barclays Bank PLC Settlement with Authorities,* 27 June 2012

bonuses is woefully inadequate [248] Barclays itself came to realise that it had misread the public mood.

Resignation of Mr Agius

163. On 2 July 2012 Barclays announced Marcus Agius' intention to resign as Chairman of Barclays, a post that he had held since 1 September 2007.[249] The resignation statement published by Barclays stated that:

> Barclays today announces the resignation of its Chairman, Marcus Agius. The search for a successor both from within the existing Board members and from outside will be led by Sir John Sunderland and will commence today. Mr Agius will remain in post until an orderly succession is assured and Sir Michael Rake has been appointed Deputy Chairman.

The statement also outlined Mr Agius' own reasons for resignation:

> last week's events—evidencing as they do unacceptable standards of behaviour within the bank—have dealt a devastating blow to Barclays reputation. As Chairman, I am the ultimate guardian of the bank's reputation. Accordingly, the buck stops with me and I must acknowledge responsibility by standing aside.[250]

Mr Agius stood down at the same time as Chairman of the British Bankers Association.

164. On the same day as Mr Agius' resignation, Mr Diamond wrote a letter to all Barclays staff. In the letter he announced that the Barclays board had "agreed to launch an audit of our business practices" to be "led by an independent third party reporting to Sir Michael Rake and a panel of Non-Executive Directors". The audit was to have three objectives:

- To undertake a root and branch review of all of the past practices that have been revealed as flawed since the credit crisis started and identify implications for our business practices and culture going forward;
- To publish a public report of its findings, and
- To produce a new, mandatory code of conduct that will be applied across Barclays.

The letter went on to say that "we will use the output of that review to adjust our HR processes so that the standards that emerge play a material role in hiring and induction; assessment and development; and reward. That will start with Executive Management." Mr Diamond ended his letter by stating that "I am committed to ensuring that the recommendations from this review are implemented in full".[251]

248 'Can Bob Diamond hang on after Barclays Libor scandal?', the Guardian, 27 June 2012

249 Mr Agius had been a member of the Barclays board since 1 September 2006 and became Chairman on 1 January 2007

250 Barclays Announcement, Board Changes, 2 July 2012

251 Subsequently, on the 24 July 2012, Barclays announced further details of what it termed an "independent review of its business practices". They said that the review would be led by Anthony Salz. Mr Salz is currently Executive Vice

165. However, on the following day, 3 July 2012, Barclays announced Mr Diamond's resignation as well as the fact that Marcus Agius was not resigning at once after all and would instead "become full-time Chairman" and "lead the search for a new Chief Executive" before leaving Barclays. Mr Agius would also "chair the Barclays Executive Committee pending the appointment of a new Chief Executive" and would "be supported in discharging these responsibilities by Sir Michael Rake, Deputy Chairman". The reason given for this decision in Mr Diamond's resignation statement was as follows:

> I joined Barclays 16 years ago because I saw an opportunity to build a business out of almost nothing. Since then, I have had the privilege of working with some of the most talented, client-focused and diligent people that I have ever come across. We built world class businesses together and added our own distinctive chapter to the long and proud history of Barclays.
>
> My motivation has always been to do what I believed to be in the best interests of Barclays. No decision over that period was as hard as the one that I make now to stand down as Chief Executive. The external pressure has reached a level that risks damaging the franchise. I cannot let that happen.[252]

Mr Jerry del Missier, Chief Operating Officer, resigned at the same time as Mr Diamond.[253]

166. We questioned both Mr Diamond and Mr Agius on the course of events which had led first Mr Agius and then Mr Diamond to resign. Marcus Agius told us that when the board met to discuss the FSA Final Notice, it "differentiated between culpability and responsibility".[254] He explained that what the board had taken "more than comfort from":

> was the fact that the FSA did not find against—if that is the right expression; forgive me if I am using loose language—Bob Diamond or any of the other senior management of the business in terms of culpability.

However, Mr Agius added that:

> you cannot see a settlement like that without recognising that responsibility is required, and the solution we devised was that the four senior executive officers who were on the deck when these matters occurred should recognise their responsibility by forgoing their bonuses.[255]

Mr Agius went on to tell us that the board "hoped" that the measures they were taking "would be deemed to be proportionate in the circumstances". He concluded that "evidently we were wrong, because the public outcry afterwards was extraordinarily great".[256]

Chairman of Rothschild and the Barclays announcement stated that "his appointment is in a personal capacity and Mr Salz will continue his role with Rothschild". Barclays also announced that the review would report to Deputy Chairman, Sir Michael Rake, and a sub-committee of the Barclays Board.

252 Barclays PLC, Board changes, 3 July 2012

253 Barclays PLC, Board changes, 3 July 2012

254 Q 541

255 Q 541

256 Q 541

167. Mr Agius told us that the board met again on Friday 29 June to "take stock" of where they were. Mr Agius went on to say that it was clear to the board "that the public clamour had been extraordinarily great", that the "reputational damage" was far greater than the board "had anticipated", and that "there was a requirement for some further action from the bank":

> that is why I felt, as the ultimate person responsible for the reputation of the bank, that I should resign. I made that decision personally on Saturday night and I conveyed it to the board on Sunday; it was announced on Monday morning.[257]

When pressed as to why he rather than Mr Diamond had initially resigned, Mr Agius explained that the board had taken "stock of how the news had been received, not just in the political world and not just in the media world, but amongst our customers, amongst our employers and amongst our shareholders". The message he told us that the board "received in strong terms from the market":

> the one outcome that the shareholders did not want to see was the removal of Bob Diamond. That was the outcome they did not want to see, as they believed in him as a very effective Chief Executive.[258]

168. We asked how the board had gauged the views of shareholders and come to the conclusion that there was strong support for Mr Diamond. Mr Agius told us that this view "was fed back to us through our stockbroker on Friday".[259] He ended by telling us that "if we do not listen to the views of our shareholders, then we are not doing our job as a board".[260] When challenged as to whether the corporate stockbroker had canvassed the views of shareholders, Mr Agius merely told us that they "were expressing an informed view". He explained that their opinion was important because "The job of a corporate stockbroker is to be close enough, both to the company and to its principal shareholders, that they understand how the shareholders view the company at any point in time".[261]

The resignation of Mr Diamond

169. We asked Mr Agius why, in that case, Mr Diamond subsequently resigned. He told us that it was "because it became clear that he had lost the support of his regulators".[262] When asked why Mr Diamond rather than Mr Agius had not initially resigned, Mr Agius replied that:

257 Q 541

258 Q 541

259 Barclays corporate stockbroker was Credit Suisse First Boston

260 Q 653

261 Q 714

262 Q 611

> At that point, the alternative of seeking the resignation of Bob Diamond was something that our shareholders did not want to see, and we believed at that time that Bob Diamond continued to have the support of his regulators.[263]

170. Mr Diamond confirmed to us that the lack of regulator support was one of the key reasons behind his subsequent decision to resign. He told us that:

> Let me explain why I changed my mind ... It was not over the weekend because we worked over the weekend on a communication to our colleagues internally. We did that knowing we had the support of the board and the support of our shareholders, with whom we had been working from the announcement toward the end of the week, of our colleagues, clients, customers and regulators. It was clear to me on Monday that that support wasn't as strong, and that I needed to take this step in this bridge. The support from the regulators was not as strong as it had been and I needed to take this step.

171. We examined how Mr Diamond had come to the conclusion that he had lost the support of the regulators. [264] Mr Diamond replied "I don't know", when asked whether Mr Agius had spoken to the regulators on this subject.[265] When asked whether Marcus Agius had discussed regulator support with him, Mr Diamond told us "that is probably a question for Marcus". Our further attempts to elicit a clear answer were unsuccessful:

> ***Chair:*** I am asking you to tell me what he would have told you in that conversation. You would have had a conversation with your chairman about this, and about the sustainability of your continued role as chief executive.
>
> ***Bob Diamond:*** I would say broadly speaking it was just as I said. With the focus of intensity on my leadership, it was better for me to step down.
>
> ***Chair:*** Why are you so reluctant to tell us what may have transpired with those regulators over the weekend? We are going to have them before us.
>
> ***Bob Diamond:*** I am trying to think if I had any conversations with regulators over the weekend.
>
> ***Chair:*** You didn't but Marcus Agius did, didn't he?
>
> ***Bob Diamond:*** Chairman, I think it is as simple as this. If Marcus had conversations with regulators, that is a conversation for him to have with you. I did not discuss that with him; I just discussed my reasons.[266]

172. Mr Agius subsequently confirmed to us that he had indeed spoken to the Governor of the Bank of England about Mr Diamond's position, albeit on Monday 2 July and not

263 Q 612

264 Qq 2–7

265 Q 3

266 Qq 3–7

during the weekend of 30 June.[267] The conversation between the two men took place because, on the morning of Monday July 2—the day on which Mr Agius' own resignation was announced—Mr Agius received a notification that the Governor wished to see him and Sir Mike Rake, the senior independent director at Barclays, that evening at six o' clock.[268] Mr Agius outlined the ensuing discussion between the three men:

> it was made very plain to us that Bob Diamond no longer enjoyed the support of his regulators. The Governor was very careful to say that he had no power to direct us, but he felt that this was sufficiently important, as indeed it was, for us to be told in absolute terms what the situation was.

Mr Agius said the Governor's statement came as "a shock". This he explained was "because only two working days beforehand we had released the announcement following the settlement with the three agencies, one of whom was the FSA, where the FSA had said nothing about the suitability or the unsuitability of Bob Diamond as Chief Executive, or indeed any of the other senior executives". He expressed puzzlement that:

> we went from Wednesday, when Bob Diamond had the support of the regulators, to Monday night, when we were told in no uncertain terms that he did not have support of the regulators.[269]

We asked Mr Agius what he thought had changed between the Wednesday and Sunday. He replied that "clearly the public outcry had been far greater than we had thought" and that his own resignation:

> which I had sought to offer in order to alleviate some of the pressure, was inadequate and, clearly, the regulators decided more was necessary.[270]

173. Mr Agius told us that he then had a further "conversation" with the non-executive directors of the Barclays board. At this stage, Mr Agius told us, the non-executive members of the board "concluded that we had no choice but to call for his [Mr Diamond's] resignation".[271]

174. Strangely, Mr Agius failed to disclose to us that he had in fact spoken to Lord Turner on the afternoon of Friday 29 June about Mr Diamond's future as Barclays Chief Executive. This only came to light subsequently, when Lord Turner confirmed to us that such a conversation had indeed taken place.[272] Lord Turner told us that the discussion he had with Mr Agius "was about the position of Bob Diamond" before outlining the exact message he conveyed to Mr Agius. He told Mr Agius—"Let me be clear. We have not found anything against Bob Diamond, so we are not in a position to give, and we are not giving, any

267 Q 633

268 Qq 633–634. Sir Mike Rake was appointed deputy chairman upon Marcus Agius' resignation on Monday 2nd July 2012

269 Q 635

270 Q 636

271 Qq 637–639

272 Q 1205

instruction or direction that we do not consider him fit and proper or appropriate to do this job". Lord Turner then went on to warn Mr Agius that he:

> had to think very seriously about the scale of change that Barclays had to make, in a substantive sense but also, as had then developed, regarding the need for them to have a leadership that could convince the external world that they had changed culturally and had addressed these issues. I said, "You have got to think about whether that is possible with Bob Diamond or whether it is simply impossible".[273]

Lord Turner reiterated that "it was absolutely clear we were talking about the role of Bob Diamond".[274] Indeed Lord Turner appeared so confident that Mr Diamond would resign following the discussion with Marcus Agius that he rang his colleague Andrew Bailey after the discussion with Mr Agius and told him "Look, I would be quite surprised if the net effect is not that Bob Diamond resigns".[275] When asked whether there was "any scope at all for a reasonable man to misunderstand what you were saying", Lord Turner replied "no". He added "that we were talking about Bob Diamond was absolutely clear":

> I can remember one thing I said, which stuck in my mind. I said, "One thing you'll have to think about is whether Bob as a brand is just holed below the water." I don't know whether I used the phrase "holed below the water", but I basically said "whether Bob the brand is now something which isn't going to work." [276]

175. Lord Turner told us that he was therefore "surprised" when he subsequently learnt (on the following Monday) that it was Mr Agius, and not Mr Diamond, who had resigned.[277] When asked about his reaction on hearing that Mr Agius and not Mr Diamond had resigned, Lord Turner said:

> I think that was an honourable thing to do. I think Mr Agius thought it was the right thing to do. It was not what I was expecting him to do, and I have to be blunt: I did not think it was the most sensible decision in the circumstances. But we were not informed beforehand of his intention to do that.[278]

176. We asked Lord Turner and the Governor of the Bank of England why the Governor then became directly involved. He met with Marcus Agius and Sir Mike Rake on Monday 2 2012. Lord Turner told us that he and the Governor spoke on Monday 2 July and that the Governor "was of the opinion that he should also have a meeting with Mr Agius" and reiterate the message Lord Turner had delivered to Marcus Agius on the previous Friday. Lord Turner stressed that it was "completely appropriate" for the Governor to meet with Marcus Agius and Sir Mike Rake:

273 Q 1205

274 HC (2012–13) 535, Q 1

275 HC (2012–13) 534, Q 4

276 HC (2012–13) 535, Q 2

277 HC (2012–13) 535, Q1

278 HC (2012–13) 535, Q 6

> I do not see a problem with the Governor of the Bank of England choosing to see the chairman and chief executive, if they want, or the chairman in this case, in order to express a point of view—a point of view which we had discussed in the course of the afternoon and were fully agreed on.
>
> I think this should fall between the FSA and the Bank of England. And a thing I would stress is that the fact that the FSA became the regulator in 1997 did not change the legitimate role of the Governor of the Bank of England in having a point of view on the confidence of the Bank—the Bank of England—in the leadership of the major banks, given, crucially that the Bank of England has to decide whether it is willing to provide liquidity support for banks. That should be something where a measure of confidence is required.[279]

177. The Governor defended the decision for him to meet Marcus Agius and Sir Mike Rake. He told us that Lord Turner and Andrew Bailey had both shared with him "for many months their concerns about Barclays" (discussed in detail in section 5 of this Report). Indeed, we learnt from Lord Turner that he had sent a copy of the letter written to Marcus Agius after their bilateral meeting in April 2012, which expressed the regulator's deep concern at developments in Barclays, to the Governor.[280]

178. The Governor explained that "the point of my meeting with them was to say, "Look you really need to understand the depths of the concerns that the regulators have about the executive management. I want you to go away and reflect on that". He told us that "all of us involved":

> had built up a genuine concern that it is possible to sail close to the wind once; you can sail close to the wind twice—maybe even three times—but when it gets to four or five times and becomes a regular pattern of behaviour, you have to ask questions about the navigational skills of the captain on the bridge".[281]

However, he added that Mr Agius' resignation signalled to him that "the board as a whole had not fully understood the nature of the concerns" and as a result "I thought it would be helpful to play a role in making sure that it did understand".[282] The Governor told us that the Barclays board—even in his 2 July 2012 meeting with Marcus Agius and Sir Mike—"was deeply reluctant to face up to [the regulators] concerns". He believed the Barclays board still thought "it might be able to tough it out", before adding:

> It was not convinced that the regulators had lost confidence. I put it to it very clearly and the senior independent director said to me, "Until today, we had not, and I, as senior independent director, had not been fully aware of the loss of confidence of the regulators in the executive management."[283]

279 HC (2012–13) 535, Q 10

280 Q 1074

281 HC (2012–13) 535, Q 39

282 HC (2012–13) 535, Q 38

283 HC (2012–13) 535, Q 39

The Governor told us that he did not deliver an ultimatum, but rather:

> The question was left absolutely with them. I made it very clear and finished the meeting by saying, "I would like you to make clear to the board that the regulators have expressed these concerns. The board as a whole needs to know that they are very concerned and have lost confidence in the executive management." I did not know what the outcome of that meeting would be. It was left to them to discuss it with their board.[284]

179. When challenged whether it was appropriate for him to play this role, given that the Bank of England currently lacks statutory responsibility in this area, the Governor replied:

> What has changed is that in the past 18 months, the regulatory part of FSA has worked very closely with me and others in the Bank to move towards a new regulatory framework so that we are already involved. Prior to 2010, I would not have felt able to carry out this conversation, because I would have known nothing about the letter that Lord Turner sent, the conversation that Andrew Bailey had, or, indeed, their concerns that had been building up, and I would have had no basis of information on which to carry out that conversation.[285]

180. We went on to examine how the initial FSA decision to tell Barclays that Mr Diamond had lost the support of the regulatory authorities was arrived at. Lord Turner told us that "it was entirely based on conversations between myself and Andrew Bailey" and that it was not the result of a meeting of a sub-committee of the FSA board.[286] Lord Turner attempted, once again, to differentiate between the use of a formal power of direction and delivering a message. He acknowledged that in the case of the former "it would have been essential to have a formal process set down, with an executive committee", but denied this was necessary in the latter instance. The Governor of the Bank of England was also asked whom he had consulted at the Bank or what processes were in place. The Governor rejected the assertion that he should have consulted with the Chairman of the Court and said he "could not discuss it with my two deputy governors, as I would usually do". This was because, as the Governor explained, "it would have compromised Mr Tucker because of the nature of the allegations that had been made".[287] Instead the Governor told us that he spoke to the Bank's chief legal advisor "to find out very carefully what I could and could not say" as well as Lord Turner and Mr Andrew Bailey.[288]

181. We asked Lord Turner whether it was appropriate for the regulatory authorities to use their informal influence effectively to dismiss CEOs. His initial response was to say that "part of the appropriate challenge to that is precisely what is going on here. It is the role of your Committee. If that occurs, you have an absolute right to ask searching questions

284 HC (2012–13) 535, Q 36

285 HC (2012–13) 535, Q 16

286 HC (2012–13) 535, Q 17–19

287 HC (2012–13) 535, Qq 31–34

288 HC (2012–13) 535, Qq 31, 37

about it".[289] However, Lord Turner did then go on to acknowledge that the manner in which Mr Diamond had eventually resigned did raise important governance and accountability questions:

> ***Chair:*** ... I'm talking about what the consequences of this case will be for the future and for precedent. You are agreeing with me that this is something that needs to be thought through and addressed?
>
> ***Lord Turner:*** Yes, I think I can agree with you that this does raise some issues about the future governance of these sorts of situation. It is of the nature of this that when you end up in these sorts of situation and you haven't written down a clear governance process in the past, you make sensible judgments about what you think is appropriate in the circumstances.[290]

The role of shareholders

182. As discussed previously, a major factor in the reluctance of the Barclays board to remove Mr Diamond was the perception—conveyed by Barclays corporate stockbroker, Credit Suisse First Boston on Friday 29 June 2012—that Mr Diamond enjoyed strong shareholder support.[291] Given this backdrop, we questioned Lord Turner whether it was appropriate for the regulatory authorities to take the action they did, when it appeared to go against the views of institutional investors in Barclays. Lord Turner's defence was that "there was almost certainly a change in shareholder attitude as the debates developed over the weekend". However, he then went on to suggest that the action taken by himself and the Governor was actually in the interests of shareholders:

> We were certainly aware that we would not want a degree of destabilisation which was harmful to the shareholders. Indeed, that was one of the things which the board needed to think about. Realistically, if Bob Diamond had stayed on, and given the extensiveness of the calls for his resignation from politicians and press, I strongly suspect that that would have been to the disadvantage of the shareholders as well.[292]

Non-executive directors

183. As of 27 June 2012 the Barclays board consisted of two executive directors—Mr Diamond and Chris Lucas, Finance Director—and ten non-executive directors. Mr Agius, the Chairman of the board, has subsequently announced his intention to resign once a successor is in post. Ms Alison Carnwath, Chair of the Remuneration Committee, resigned on 25 July 2012 citing "personal reasons".[293]

289 Q 22

290 Q 25

291 Qq 653, 714

292 Q 26

293 Barclays Announcement, 'Barclays announces Board change', 25 Jul 2012

184. That leaves in post a number of long-serving non-executive directors who would have been in post through all or most of the period of LIBOR manipulation and who, in some instances, held key positions on audit and risk committees through this period. For example, David Booth joined the Barclays Board on 1st May 2007. Fulvio Conti joined the Barclays Board on 1st May 2006 and has been a member of the Board Audit Committee since September 2006.. Sir Andrew Likierman joined the Barclays Board on 1st May 2004. Sir Andrew has been a member of the Board Audit Committee since September 2004 and a member of the Board Risk Committee since September 2004. Sir John Sunderland joined the Barclays Board on 1st June 2005. Sir John has been a member of the Board Citizenship Committee since August 2011.

Conclusions on resignations

185. **Barclays' initial response to the publication of the FSA Final Notice was to announce that four senior executives would waive their bonus for one year. This proved to be a wholly inadequate response to the scale and severity of the wrongdoing discovered by the regulatory authorities. Barclays itself acknowledged that its response to the FSA Final Notice was inadequate and, as Mr Agius told us, "there was a requirement for some further action from the bank".**

186. **Both the Governor of the Bank of England and the Chairman of the FSA have stressed that they did not demand Mr Diamond's resignation, but instead pointed out the difficulties of Mr Diamond continuing in post and left the final decision to the Barclays board. However, both the Governor and Lord Turner must have been aware that it would have been extremely difficult, if not impossible, for Mr Diamond to stay in post after having lost the confidence and support of the regulatory authorities. Therefore, Mr Diamond's resignation as Barclays CEO was a *fait accompli* once both men intervened.**

187. **The FSA did not intervene with respect to Mr Diamond's future as Barclays CEO prior to, or on Wednesday 27 June 2012, when the FSA Final Notice was published. Indeed, the FSA only appears to have intervened on Friday 29 June, two days after the publication of the Final Notice. This perplexed Marcus Agius who told us "we went from Wednesday, [27 June] when Bob Diamond had the support of the regulators, to Monday night [2 July], when we were told in no uncertain terms that he did not have the support of the regulators". This about-turn by the FSA appears to have been the result of the vociferous public and media reaction in the days following the publication of the Final Notice. If this is indeed the case, then what many would consider the right decision was taken for the wrong reasons.**

188. **Neither the FSA or the Bank of England should intervene to remove senior bank executives to placate public, media and Parliamentary opinion. There will be circumstances in the future where they will need to act, but without the force of public opinion to support them. On other occasions the regulatory authorities will need to stand firm and not intervene despite public and political pressure for them to do so.**

189. **Lord Turner attempted to convince Marcus Agius that the Barclays board needed to give serious thought to whether Mr Diamond was the right person to lead Barclays in the future. Lord Turner appeared to come away from his discussion with Mr Agius confident that Mr Diamond would resign. However, Mr Agius then proceeded to resign himself in what we can only conclude was a last ditch attempt to keep Mr Diamond in post. Therefore, either Lord Turner's message to Mr Agius was not clear or forceful enough or Marcus Agius was deaf to Lord Turner's message. It then took the intervention of the Governor of the Bank of England before the Barclays board became convinced that Mr Diamond had to go. The Governor's involvement is difficult to justify. The Governor defends his involvement by pointing out that the Bank of England will soon have regulatory responsibility for the prudential supervision of banks. However, the Bank does not, at present, have regulatory responsibility for the banking system. Any attempt to discuss Mr Diamond's future as Barclays CEO should have come from the FSA and not the Governor of the Bank of England. The Governor's involvement is particularly surprising given that he has told the Treasury Committee in the past that he has been unable to act because the Bank did not have responsibility for this, or that, particular area of policy. Indeed, this is the very defence he and Mr Tucker have used when explaining why they did not intervene in LIBOR, despite suspecting problems.**

190. **Whatever the merits of the action taken by the Governor of the Bank of England and the Chairman of the FSA—and this Committee has sympathy with the conclusions they had drawn about the leadership of Barclays—the action they took has exposed implicit, and potentially arbitrary, power to force out senior figures in the financial services industry. The return of the 'Governor's eyebrows'—which many will welcome on this occasion—comes with the need for corporate governance safeguards.**

191. **In this case, the Governor of the Bank of England and senior FSA staff did discuss the issue and acted in concert. There was, as a result, some minimal check and balance. However, once the Bank of England assumes full responsibility for financial stability and micro-prudential supervision, even this minimal check and balance will disappear. The Governor of the Bank of England will stand all-powerful and able, by dint of raising his eyebrows, effectively to dismiss senior banking executives without discussing it with, or consulting, anyone. This is unsatisfactory. As the Treasury Committee has repeatedly stated, a much stronger governance framework is needed. Among other things this can ensure that the regulatory authorities are unable to remove senior bank executives arbitrarily or without just cause. We welcome the fact that the Chairman of the FSA agrees with us that governance processes must be put in place to ensure accountability and transparency for the process of removing senior bank executives in whom the regulators have lost confidence.**

192. **According to the Chairman of Barclays, Mr Diamond continued to enjoy strong shareholder support. If this is indeed the case, then the actions taken by the Governor and the Chairman of the FSA were in opposition to the position of major Barclays shareholders. Although Lord Turner asserts that support for Mr Diamond had fallen away over the course of the weekend of 30 June 2012, there was no strong public**

clamour from institutional investors for the removal of Mr Diamond. The regulatory authorities need to possess the ability to remove senior executives, but when they exercise this power, they should recognise their duty of care to shareholders. This issue should be examined by the Bank of England, the FSA and its successor bodies.

193. **The UK Corporate Governance Code is clear that "the board should set the company's values and standards". However, the misconduct of LIBOR and breakdown of trust with the regulatory authorities has demonstrated that the Barclays board has presided over a deeply flawed culture.**

7 Enforcement

The penalty levied by the FSA

194. A penalty of £59.5 million was imposed on Barclays Bank, reflecting a 30% reduction from the baseline penalty figure of £85 million which the FSA decided to impose owing to mitigating factors, in particular Barclays' level of co-operation with the investigation.[294]

195. The Committee was concerned to establish how the baseline figure was calculated, and whether it appropriately reflected the gravity of the misconduct, bearing in mind it represented approximately 1% of Barclays Bank's profit of £5,879 million before tax in 2010–11.[295] The FSA's Final Notice lists the factors taken into account when setting the level of fines under its Decision Procedures and Penalties Manual, but does not discuss the weighting given to each factor.[296]

196. Tracey McDermott, acting director of enforcement and financial crime at the FSA, explained that the FSA did not apply a formula when calculating penalties. Instead, there was a list of factors which were taken into account:

> The penalty is set in accordance with our penalty policy that was applicable to misconduct at the time. We are required by the Financial Services and Markets Act 2000 to publish a statement of our policy. At the time, there was no arithmetical calculation that applied. We take into account a number of factors, including the seriousness of the misconduct and including the level of co-operation during the investigation.[297]
>
> [...]
>
> We believe that it was appropriate. I think, as has been shown amply by this case, the impact of enforcement action is not just about the level of the penalty; it is also about what comes out in the public domain and the reputational impact that follows. This was the most significant penalty we have imposed. It was almost twice the highest penalty we have imposed in the past. That reflected our view that this was the worst misconduct.[298]

197. **The Committee regrets that the FSA's acting director of enforcement and financial crime did not take the opportunity to explain how the factors the regulator takes into account had been applied to Barclays in this case. We are concerned about the lack of transparency in the way in which the FSA calculated the amount of the fine.**

294 *Barclays fined £59.5 million for significant failings in relation to LIBOR and EURIBOR*, FSA Press Notice, 27 June 2012

295 Barclays Bank Plc Annual Report 2011

296 FSA Final Notice, 27 June 2012, p 44

297 Q 1088

298 Q 1091

Criminal enforcement

Legal lacunae

198. We recognise that the definition of market abuse punishable by financial penalty under section 123 of the Financial Services and Markets Act 2000 (FSMA) is insufficiently wide to capture the manipulation of the LIBOR rate. The LIBOR rate is not designated a qualifying investment for the purposes of the legislation. It is also not possible for the FSA to commence a criminal prosecution under section 397(3) of the Financial Services and Markets Act 2000 against Barclays, the submitters or derivatives traders for engaging in a course of conduct which created a false or misleading impression as to the market in or the price or value of a relevant investment. LIBOR is not classified as a relevant investment for the purposes of this section of the Act.

199. **The Committee urges the Wheatley review to consider the case for amending the present law by widening the meaning of market abuse to include the manipulation, or attempted manipulation, of the LIBOR rate and other survey rates. They should also consider the case for widening the definition of the criminal offence in section 397 of FSMA to include a course of conduct which involves the intention or reckless manipulation of LIBOR and other survey rates.**

Power to prosecute

200. Notwithstanding these limitations, the Committee asked the FSA about its power to bring criminal cases. Lord Turner told the Committee that:

> My understanding is that the FSA is not able to bring a criminal case in the UK. If it falls within the category of fraud, which is a general category of malfeasance quite separate from financial regulation, the Serious Fraud Office has a right to look at it, and we have been in contact with the SFO throughout this. I think that it announced a week or so ago that it would increase its focus on this issue. In the UK, this issue—as I understand it, but I would defer to my legal expert here—is not one where we, the FSA, have an ability to bring a criminal case, whereas there are some other specific categories of market manipulation where we are able to bring criminal cases.[299]

This statement was refined by Tracey McDermott:

> [...] we are not a general fraud prosecutor. We have specific powers to prosecute particular offences, and I am sure that you will be aware that we have spent quite a lot of time and energy on prosecuting both section 397 offences and indeed insider dealing offences in recent years. What we do not have is a remit to prosecute false accounting, conspiracy and so on in a general sense. We could prosecute it as ancillary to one of our main offences, so if there was a markets offence, you could

299 Q 1104

> throw in money laundering as well, but our investigative powers are limited to the offences that we have the ability to prosecute.[300]

201. Tracey McDermott subsequently confirmed that the FSA was also able to prosecute non-financial market offences in its capacity as a private prosecutor.[301] This is consistent with the ruling of the Supreme Court in the case of *R v Rollins* in 2010.[302] However, when asked whether there was enough evidence of fraudulent conduct to commence a criminal prosecution in this case, Tracy McDermott responded that "[this] is not our specialist area of expertise. It is not where our fees are raised to prosecute, that is to focus on the FSMA offences".[303]

202. **The FSA apparently believes that its fees are not raised for the purpose of prosecuting offences other than those set out in FSMA. The Committee is concerned by this. The FSA has responsibility for regulating the key participants in financial markets. The FSA's decision whether to initiate a criminal prosecution should not be influenced by the fact that its income is derived from firms which it regulates. The FSA has an obligation under section 2(1)(b) of FSMA to discharge its functions in the way in which it considers most appropriate for the purpose of meeting its regulatory objectives. Under section 2(2)(d) the reduction of financial crime is one of these objectives. Financial crime is defined in section 6(3) as including not only misconduct in relation to a financial market but also any criminal offence of fraud or dishonesty. The FSA took a narrow view of its power to initiate criminal proceedings for fraudulent conduct in this case. The Committee recommends that the Government, following the Wheatley review, should consider clarifying the scope of the FSA's, and its successors', power to initiate criminal proceedings where there is serious fraudulent conduct in the context of the financial markets.**

The FSA and the Serious Fraud Office

203. Tracey McDermott explained that there was a protocol between the FSA and the Serious Fraud Office (SFO) which provided that the FSA did not take the lead in prosecuting general fraud offences.[304] In this case, there was some discussion between the FSA and the SFO with reference to the artificial fixing of LIBOR but the purpose and content of the discussions, when they took place or those present, was not clear from her evidence.[305]

204. According to Ms McDermott, initially the SFO was keeping a "watching brief" to see whether it should take any action and there were meetings in 2011 at which information was shared.[306] The liaison between the FSA and the SFO was described as "constant",[307]

300 Q 1105

301 Qq1140–1

302 [2010] UKSC 39, see in particular Lord Dyson at paragraph 17 of the judgment

303 Q1143

304 Q1143

305 Qq1143 , 1201

306 Qq1145, 1146, 1199

although she said "it wasn't us saying, 'Oh, you should believe us that there's something dreadful going on here'. We were sharing evidence and information with them throughout".[308]

205. The SFO announced on 2 July 2012 that:

> The Serious Fraud Office has been working closely with the Financial Services Authority during its investigation into recently reported issues in relation to LIBOR. Now that the investigation into the issue of regulatory misbehaviour has concluded, the SFO are considering whether it is both appropriate and possible to bring criminal prosecutions.
>
> The issues are complex and the assessment of the evidence the FSA has gathered will take a short time, but we hope to come to a conclusion within a month.
>
> The SFO is aware of investigations in other jurisdictions and is working with the relevant authorities.[309]

On 6 July the SFO formally accepted the LIBOR issue as a matter for investigation. The Serious Fraud Office announced on 30 July that:

> the Director of the Serious Fraud Office, David Green QC, is satisfied that existing criminal offences are capable of covering conduct in relation to the alleged manipulation of LIBOR and related interest rates. The investigation, announced on 6 July, involves a number of financial institutions.[310]

206. **The Serious Fraud Office (SFO) is now conducting a criminal investigation into LIBOR. The Committee was surprised that neither the FSA nor the SFO saw fit to initiate a criminal investigation until after the FSA had imposed a financial penalty on Barclays.**

207. **The evidence in this case suggests that a formal and comprehensive framework needs to be put in place by the two authorities to ensure effective relations in the investigation of serious fraud in financial markets. The lead authority must be clearly identified for the purposes of an investigation, and formal minutes of meetings between the authorities must be maintained. We recommend that the Wheatley review examine whether there is a legislative gap between the responsibility of the FSA and the SFO to initiate a criminal investigation in a case of serious fraud committed in relation to the financial markets.**

307 Q1147

308 Q1151

309 SFO press release, 2 July 2012

310 SFO press release, 30 July 2012

Conclusions and recommendations

Introduction

1. The Committee concurs with the FSA's assessment of the importance of the damage done to the benchmark rates by the attempted manipulation that the regulators discovered. Attempted manipulation of these reference rates reduces trust and confidence in markets and carries costs for end users. The Committee is concerned that the FSA was two years behind the US regulatory authorities in initiating its formal LIBOR investigations and that this delay has contributed to the perceived weakness of London in regulating financial markets. (Paragraph 7)

2. The Committee found Mr Diamond's attempt to subdivide the later period of wrongdoing neither relevant nor convincing. It does not appear that the conversation between Mr Tucker and Mr Diamond made a fundamental difference to Barclays' behaviour, given the repeated instances of 'low-balling' submissions to the LIBOR fixing process by Barclays set out in the FSA Final Notice covering the year running up to the phone call between Mr Tucker and Mr Diamond. (Paragraph 8)

3. Barclays is just one of many international banks under investigation for possible market manipulation. It is important that Barclays' serious shortcomings should not be seen in isolation from the possible actions of other banks and we await the results of ongoing investigations. (Paragraph 9)

4. It is important to state that Barclays' internal compliance department was told three times about concerns over LIBOR fixing during the period under consideration and it appears that these warnings were not passed to senior management within the bank. Statements that everything possible was done after the information came to light must be considered against a background of serious failures of the compliance function within the bank. In other words, the senior management should have known earlier and acted earlier. (Paragraph 13)

5. Barclays received a reduction in its fine because of its high degree of co-operation with the FSA in its investigation. Barclays also disclosed wrongdoing that it had itself found to the regulators. Any such disclosure is likely to have carried serious risk of reputational damage. Co-operation with inquiries needs to be encouraged by regulators, who need to take into account first mover disadvantage, but it does not excuse or diminish wrongdoing. Nor does the fact that others may have been engaged in similar practices. The FSA and its successors should consider greater flexibility in fine levels, levying much heavier penalties on firms which fail fully to co-operate with them. The FSA needs to give high priority to its investigations into other banks, including those largely owned by the taxpayer. (Paragraph 16)

6. Firms must be encouraged also to report to the regulator instances they find of their own misconduct. While such a firm should still be required to pay compensation to any other party who has been disadvantaged by the misconduct, in cases where a firm makes a complete admission of its own culpability the FSA should retain

flexibility in setting the fine payable. The FSA should have regard to the desirability of encouraging other firms to confess their misdemeanours in a similar way. The FSA may also need to re-examine its treatment of whistleblowers, both corporate and individual, in order to provide the appropriate incentives for the reporting of wrongdoing. (Paragraph 17)

Manipulation by individuals with the intention of personal benefit

7. The actions that have so far been discovered of Barclays and other traders were disgraceful. As the FSA's Final Notice states, the attempted manipulation of LIBOR "created the risk that the integrity of LIBOR and EURIBOR would be called into question and that confidence in or the stability of the UK financial system would be threatened". This attempted manipulation of LIBOR should not be dismissed as being only the behaviour of a small group of rogue traders. There was something deeply wrong with the culture of Barclays. Such behaviour would only be possible if the management of the bank turned a blind eye to the culture of the trading floor. The incentives and control systems of Barclays were so defective that they incentivised traders to benefit their own book irrespective of the impact on shareholders and the bank's overall performance. Now exposed, their actions are to the detriment of Barclays' reputation and the reputation of the industry. The standards and culture of Barclays, and banking more widely, are in a poor state. Urgent reform, by both regulators and banks, is needed to prevent such misconduct flourishing. (Paragraph 34)

8. The attempted manipulation of Barclays' LIBOR submissions with the intention of personal gain continued for four years. It is shocking that it flourished for so long. Any system may fail for a short period, but compliance at Barclays was persistently ineffective. Even when Barclays' compliance had indications that something was awry, it failed to take the opportunity to strengthen the bank's controls. Nor was there any pressure from senior executives within Barclays to ensure that effective LIBOR controls were in place, as it was considered low-risk, in particular where LIBOR setters sat, with no presence of the compliance function. These are serious failures of governance within Barclays, for which the board is responsible. The compliance function within a bank is very important. If it is weak or ignored in the practices of the bank that is reflective of a poor culture which does not take seriously enough abiding by the rules essential to proper functioning of the bank and the wider financial system. The serious failings of the compliance function during the period under examination suggest there was this kind of culture at Barclays. (Paragraph 38)

9. During this period of extremely weak compliance at Barclays, it was nonetheless subject to extensive regulatory oversight by the FSA. Despite the numerous ARROW visits that were conducted by the FSA during this period, we have seen no evidence that this weakness in compliance elaborated in the Final Notice was identified by the FSA in a timely manner, still less, dealt with. The FSA must report to this Committee on how it will alter its supervisory efforts to counter such weak compliance in future. (Paragraph 39)

Manipulation during the Financial Crisis

10. Barclays has suggested that there were numerous contacts between itself and the authorities over LIBOR during this period. The clearest message appears to have been given by Barclays to the Federal Reserve Bank of New York, rather than to the UK authorities. Lord Turner described some of Barclays' contact with the FSA as "elliptic". We have found little evidence that Barclays provided the UK authorities with a clear signal about dishonesty at other firms, or its own. We await the outcome of the other regulatory investigations to see whether other firms provided such a signal, were equally elliptical or even silent on this problem. The timeline of contacts between Barclays and regulators provided to the committee by Barclays is not, of itself, evidence of a proactive approach on trying to report irregularities in the setting of LIBOR rates. (Paragraph 60)

11. We would have expected the FSA and the Bank of England to have made efforts to identify and provide to the Committee documents clearly and directly relevant to our inquiry, subject to statutory restraints. (Paragraph 61)

12. The financial crisis, and the serious dysfunctionality of the interbank lending markets, meant that it was difficult during this period for firms to estimate their own funding costs. LIBOR submissions were being used by markets and regulators to assess the financial health of the institutions involved. The FSA and the Bank of England were engaged in crisis management, alert to the possibility of further bank failures, rather than LIBOR manipulation. This is understandable, given the circumstances of the financial crisis, but with the advantage of hindsight constitutes a failing by the authorities. (Paragraph 62)

13. Given the importance of LIBOR submissions in assessing banks' health, Bank of England staff were aware of the danger that banks might improperly manipulate their submissions. They noted that "banks have been subject to the more powerful incentive of avoiding stigma from being seen to submit high rates reflective of what they are actually paying". However, they primarily saw this as a matter for the regulator rather than the Bank of England. Mr Tucker told us that possible clues to dishonesty "did not set alarm bells ringing at the time". The evidence suggests that the Bank of England was aware of the incentive for banks to behave dishonestly, yet did not think that dishonesty was occurring. Nor did it appear to have asked the FSA to check to see if such dishonesty was occurring. With hindsight this suggests a naivety on the part of the Bank of England. They were certainly relatively inactive. This confirms evidence from other Treasury Committee inquiries of the dysfunctional relationship between the Bank of England and the FSA which existed at that time to the detriment of the public interest. (Paragraph 63)

14. Unlike the Bank of England, the Financial Services Authority was the prudential regulator. Its shortcomings at this time are therefore far more serious. The Committee is concerned about the FSA's failure to appreciate the significance of market rumours relating to the artificial rigging of the LIBOR rate. We therefore look forward to the result of the FSA's internal investigation, the existence of which was disclosed in evidence to us. The Committee will want the findings of that investigation to be published. (Paragraph 64)

15. The evidence we have received is that there was significant co-operation between the US and the UK authorities at the time of the 2008 BBA review. It is understandable that regulators, in response to the LIBOR crisis, may have placed information in the public domain to demonstrate their respective assiduity at the time. This release of information must complement co-operation between regulators. The Chancellor should stress to his counterparts the need for such co-operation at the next G20 meeting. (Paragraph 65)

16. The BBA's review of LIBOR in 2008, given that it focussed on the concerns of the market over the LIBOR setting process, appears to have been an opportunity missed to stop the attempted manipulation that was occurring. The Wheatley review should now look at the role of the BBA in LIBOR setting at that time in detail and publish its findings. This is essential if its recommendations for a more reliable LIBOR setting process are to carry credibility. The review should include how such systems work during times of financial crisis, when there may be little or no interbank lending taking place, and how the authorities should respond to signs of dysfunction. It should also consider whether a trade association is the appropriate body to perform that role. (Paragraph 66)

17. We have seen no explanation for the failure, both of Barclays' board and of senior executives, to question its own firm's LIBOR submissions, when its staff were complaining about the submissions of other firms, and media and academic reports questioned the incentives present in LIBOR setting. There appears to have been enough doubt being spread about the LIBOR setting process to suggest that a closer examination by Barclays board of its own practices should have taken place. It stretches credibility to suggest that Barclays was trying to alert regulators to inconsistencies in the LIBOR submissions of other banks yet had no idea about the repeated 'low-balling' of its own submissions during the financial crisis set out in the FSA Final Notice. We have found no evidence that the board of Barclays sought to conduct an investigation. This was one of a number of failings on the part of Barclays' board. Others can be found in Sections 5 and 6. (Paragraph 67)

The Tucker Diamond dialogue and the Diamond File Note

18. The evidence we received suggests that Whitehall was prompted to contact the Bank of England because of its concerns about whether the October 2008 rescue package for the UK financial system was working, as well as concerns about the financial health of Barclays. This was understandable given the fragility of the UK and international financial system in October 2008. (Paragraph 99)

19. We will never know the details of the discussion between the Mr Tucker and Mr Diamond. What we do know is that Mr Tucker denied ever having issued an instruction to Barclays whilst Mr Diamond denied having received an instruction from Mr Tucker. (Paragraph 101)

20. The File note is of secondary importance as far as the subsequent transmission of the instruction is concerned. This is because Mr del Missier told us that he acted, not on the basis of the File note, but on the basis of the 29 October 2008 discussion he had with Mr Diamond, following the conversation between Mr Diamond and Mr Tucker. Mr del Missier informed us that the File note correctly records the substance of the Tucker-Diamond discussion as relayed to him by Mr Diamond, but not the exact words. There is no File note of the conversation between Mr Diamond and Mr del Missier and no recording was taken of their discussion. (Paragraph 102)

21. It remains possible that the entire Tucker-Diamond dialogue may have been a smokescreen put up to distract our attention and that of outside commentators from the most serious issues underlying this scandal. (Paragraph 103)

22. From Mr del Missier's evidence it appeared that Mr Dearlove was comfortable with the instruction that was passed to him following his 29 October 2008 conversation with Mr Diamond. There was some resistance from the submitter, who emailed compliance with his concerns. However, he or she ultimately acted on the instruction. There appears to have been, once again, no real 'push-back' from the compliance function when they were informed by Group treasury of the instruction. This lack of 'push back' demonstrates the weakness of the compliance function in Barclays at that time. It may also reflect the fact that Group treasury had been submitting false rates since September 2007 and that, to this end, Mr del Missier's instruction was not a departure from prevailing practice. It is unclear to the Committee why Barclays has attempted to place such weight on the Tucker-Diamond phone call given the pattern of repeated dishonesty in LIBOR submissions in the months running up to this phone call set out in the FSA Final Notice. Barclays did not need a nod, a wink or any signal from the Bank of England to lower artificially their LIBOR submissions. The bank was already well practised in doing this. Mr del Missier appears to have stressed the fact that what he saw as an instruction came from the Bank of England and that this may have muted resistance to it. Mr del Missier's evidence, that he received such an extraordinary instruction from the Bank of England, yet subsequently queried it neither with Mr Diamond nor with those to whom he passed the instruction, is not convincing. He would have known that falsifying LIBOR submissions was not permitted. (Paragraph 105)

23. The Committee remains sceptical about the importance of the Tucker-Diamond phone call given the already established pattern of dishonest LIBOR submissions from Barclays set out in the FSA Final Notice. The lack of a record by the Bank of England of the conversation between Mr Tucker and Mr Diamond is of great concern. The fact that Mr Tucker failed to make a contemporaneous note of the conversation is explicable given that the UK was in the midst of the most serious financial crisis in modern times: there was unprecedented pressure on senior Bank of England staff at this time. Nonetheless, the Bank of England should have had adequate procedures in place for at least the making of a File note of such conversations. We recommend that the Bank undertake a review of its note keeping systems, especially those involving senior executives, and publicly report its conclusions. (Paragraph 107)

24. If Mr Tucker, Mr Diamond and Mr del Missier are to be believed, an extraordinary, but conceivably plausible, series of misunderstandings and miscommunications occurred. The evidence that they separately gave describes a combination of circumstances which would excuse all the participants from the charge of deliberate wrongdoing. (Paragraph 108)

Barclays and the FSA

25. We endorse Mr Diamond's view, which echoes that of the Group of Thirty, that the culture of an organisation is demonstrated by how people behave when no-one is watching. In this case, however, the culture of the Barclays allowed people to do the wrong thing quite openly over a long period, with the attempted manipulation being shouted about across the dealing room floor. Barclays was found to have fallen lamentably below the standards that the former Chief Executive suggested should be set for his own firm. (Paragraph 112)

26. We appreciate that Mr Diamond may not have recently read the letter of September 2010 from Mr Sants to Mr Agius in connection with his appointment as Chief Executive when he appeared before us, or have had the discussions about his appointment as chief executive at the front of his mind. However, we find it difficult to accept Mr Diamond's evidence with respect to his apparent unawareness of the matters raised by the FSA with the Chairman of Barclays in connection with his appointment as chief executive in September 2010. The evidence of the Chairman of Barclays is that he did raise them with Mr Diamond, as one would expect. It seems unlikely that they were not raised with him. If they were appropriately raised, it seems unlikely that they would be quickly forgotten. (Paragraph 122)

27. The FSA expressed concerns in connection with the appointment of Bob Diamond as chief executive to Barclays. The concerns were about an attitude to risk and a tendency to "push the limits" in areas where Mr Diamond was directly involved. The concerns were not, however, serious enough to prevent the regulator from approving his appointment. Barclays appears to have regarded the points raised by Mr Sants as "issues" rather than "concerns". On the basis of the evidence it is unclear whether Barclays 'got the message'. To avoid the scope for misunderstanding in future, we recommend that the regulator set out clearly for firms any concerns it has about a senior appointment, listing any actions that it requires. It should ensure that a response is obtained in writing from the firm, undertaking to meet each of the requirements. Failure by the firm to show evidence that the regulatory messages have been seen and acted upon should be considered a serious matter. (Paragraph 124)

28. Mr Bailey does not recall saying that he was "specifically happy" about the tone at the top—in fact he says that the phrase "tone at the top" is Barclays' own. Mr Diamond, however, told us that the regulator was specifically pleased with his relationship with the FSA. The FSA told us that it had concerns about its relationship with the firm, but was not able to point to evidence directly linking those concerns to the behaviour of Mr Diamond. However, as Chief Executive he was responsible for the state of his firm's relationship with the regulator, and for demonstrating to the regulator that the necessary action was being taken to remedy shortcomings. The fact that the Barclays board discussed the need to get the "tone from the top" right, and how important this was to Barclays, after Mr Bailey left the board meeting, suggests that the Barclays board did appreciate his message. This appreciation was lacking in Mr Diamond's evidence. We do not accept Mr Diamond's evidence on this point. It stands in contrast to the evidence of Mr Bailey and the minutes of the discussion at the board meeting. It seems certain that Mr Bailey did express concern to the board. It is possible that Mr Diamond did not appreciate the significance of what was said. If so, this lack of appreciation could be considered part of the problem which the FSA was seeking to address. (Paragraph 134)

29. The impression that Mr Diamond gave to the Committee as to the significance of the FSA's message to the 9 February 2012 board meeting sits uneasily with Barclays' own board minutes. Mr Bailey of the FSA has also told us that in his view the evidence from Mr Diamond to the Committee failed to convey the severity of the matters under discussion. (Paragraph 138)

30. Lord Turner's letter to Mr Agius was described by the former as a follow up to the meeting between them which was itself a follow up to the February 2012 Barclays board, meeting at which Mr Bailey spoke. The fact that it was not described to Mr Diamond as a follow up letter to the April meeting between Lord Turner and Mr Agius is scarcely relevant. What matters is that it was part of a process of following up a board meeting which he attended and about which he was prepared to tell us virtually nothing in evidence. We accept Mr Bailey's conclusion that Mr Diamond's evidence on this point was "highly selective". We also note that Lord Turner was "surprised" at Mr Diamond's apparent ignorance of the letter. Our conclusion is that Mr Diamond's evidence was unforthcoming and highly selective on this point. (Paragraph 143)

31. We have considered the evidence of Mr Diamond and other witnesses on Barclays' relationship with the FSA. His evidence denying that the FSA felt that trust had broken down between itself and Barclays is inconsistent with that of Mr Bailey. We are unable to accept Mr Diamond's assessment of the seriousness of the matters discussed at the February 2012 board meeting: in the light of all the circumstances, it seems to us inconceivable that Mr Diamond could have believed that the FSA was satisfied with the tone at the top of Barclays when the evidence from the FSA is that this was not the case. He did not mention the important and trenchant letter of Lord Turner to Mr Agius, setting out major concerns of the FSA, when he had ample opportunity to do so. It is very unlikely that he was unaware of that letter, or its significance as a follow up to the firm messages given to the Barclays board by Mr Bailey in February 2012.Having heard the evidence of Mr Diamond and the FSA on these points, the Committee prefers the evidence of the FSA. Select committees are entitled to expect candour and frankness from witnesses before them. Mr Diamond's evidence, in the Committee's view, fell well short of the standard that Parliament expects. (Paragraph 144)

32. The Parliamentary Commission on Banking Standards' examination of the corporate governance of systemically important financial institutions should consider how to mitigate the risk that the leadership style of a chief executive may permit a lack of effective challenge or to the firm committing strategic mistakes. (Paragraph 155)

33. Mr Agius denied misunderstanding the seriousness of relations with the FSA, and sought to give the impression that the February meeting was one that might be expected between a regulator and a bank. He also drew a distinction between the messages delivered by Mr Bailey in February 2012 and that from Lord Turner in April. Both of these interpretations are contested by the FSA, who said that the Bailey visit and the Turner exchanges arose from the same concerns and were part of a single process, and that the visit of Mr Bailey was quite different in character from normal regulatory exchanges. For Mr Bailey the minutes of the Barclays board were significant. He considered that the board had realised the seriousness of affairs. Yet, according to Mr Agius, the Chairman only realised it when he later met and then, in April, corresponded with Lord Turner. This looks implausible, but the senior non-executive director told the Governor of the Bank as late as 2 July that he had not, until that moment, appreciated the loss of confidence on the part of regulators in the senior executive management of Barclays. (Paragraph 157)

34. It is at least possible that the message from the FSA's governance review may have obscured some of the messages that Mr Bailey and Lord Turner thought they were hammering home to the Barclays board. (Paragraph 158)

35. The messages that Lord Turner and Mr Bailey gave to the Barclays board this year provide evidence of the evolution of a more judgement-led approach on the part of the FSA. Lord Turner said that the change to this approach began as long ago as 2008, and it featured in his Mansion House speech in 2009. Judgement-led regulation is welcome: the FSA has concentrated too much on ensuring narrow rule-based compliance, often leading to the collection of data of little value and to box ticking, and too little on making judgements about what will cause serious problems for consumers and the financial system. In February, though, the FSA judged that it was the overall culture, rather than just a particular behaviour, of Barclays that represented a risk, and so took steps to address this directly. This intervention was not routine or coded. It was a loud and clear expression of the concerns the FSA had about the culture at Barclays and should have been clearly understood by the board. This innovative action is also welcome. The episode shows, however, that judgement-led regulation will require the regulator to be resolutely clear about its concerns to senior figures in systemically important firms. (Paragraph 159)

The resignations

36. Barclays' initial response to the publication of the FSA Final Notice was to announce that four senior executives would waive their bonus for one year. This proved to be a wholly inadequate response to the scale and severity of the wrongdoing discovered by the regulatory authorities. Barclays itself acknowledged that its response to the FSA Final Notice was inadequate and, as Mr Agius told us, "there was a requirement for some further action from the bank". (Paragraph 185)

37. Both the Governor of the Bank of England and the Chairman of the FSA have stressed that they did not demand Mr Diamond's resignation, but instead pointed out the difficulties of Mr Diamond continuing in post and left the final decision to the Barclays board. However, both the Governor and Lord Turner must have been aware that it would have been extremely difficult, if not impossible, for Mr Diamond to stay in post after having lost the confidence and support of the regulatory authorities. Therefore, Mr Diamond's resignation as Barclays CEO was a fait accompli once both men intervened. (Paragraph 186)

38. The FSA did not intervene with respect to Mr Diamond's future as Barclays CEO prior to, or on Wednesday 27 June 2012, when the FSA Final Notice was published.

Indeed, the FSA only appears to have intervened on Friday 29 June, two days after the publication of the Final Notice. This perplexed Marcus Agius who told us "we went from Wednesday, [27 June] when Bob Diamond had the support of the regulators, to Monday night [2 July], when we were told in no uncertain terms that he did not have the support of the regulators". This about-turn by the FSA appears to have been the result of the vociferous public and media reaction in the days following the publication of the Final Notice. If this is indeed the case, then what many would consider the right decision was taken for the wrong reasons. (Paragraph 187)

39. Neither the FSA or the Bank of England should intervene to remove senior bank executives to placate public, media and Parliamentary opinion. There will be circumstances in the future where they will need to act, but without the force of public opinion to support them. On other occasions the regulatory authorities will need to stand firm and not intervene despite public and political pressure for them to do so. (Paragraph 188)

40. Lord Turner attempted to convince Marcus Agius that the Barclays board needed to give serious thought to whether Mr Diamond was the right person to lead Barclays in the future. Lord Turner appeared to come away from his discussion with Mr Agius confident that Mr Diamond would resign. However, Mr Agius then proceeded to resign himself in what we can only conclude was a last ditch attempt to keep Mr Diamond in post. Therefore, either Lord Turner's message to Mr Agius was not clear or forceful enough or Marcus Agius was deaf to Lord Turner's message. It then took the intervention of the Governor of the Bank of England before the Barclays board became convinced that Mr Diamond had to go. The Governor's involvement is difficult to justify. The Governor defends his involvement by pointing out that the Bank of England will soon have regulatory responsibility for the prudential supervision of banks. However, the Bank does not, at present, have regulatory responsibility for the banking system. Any attempt to discuss Mr Diamond's future as Barclays CEO should have come from the FSA and not the Governor of the Bank of England. The Governor's involvement is particularly surprising given that he has told the Treasury Committee in the past that he has been unable to act because the Bank did not have responsibility for this, or that, particular area of policy. Indeed, this is the very defence he and Mr Tucker have used when explaining why they did not intervene in LIBOR, despite suspecting problems. (Paragraph 189)

41. Whatever the merits of the action taken by the Governor of the Bank of England and the Chairman of the FSA—and this Committee has sympathy with the conclusions they had drawn about the leadership of Barclays—the action they took has exposed implicit, and potentially arbitrary, power to force out senior figures in the financial services industry. The return of the 'Governor's eyebrows'—which many will welcome on this occasion—comes with the need for corporate governance safeguards. (Paragraph 190)

42. In this case, the Governor of the Bank of England and senior FSA staff did discuss the issue and acted in concert. There was, as a result, some minimal check and balance. However, once the Bank of England assumes full responsibility for financial stability and micro-prudential supervision, even this minimal check and balance will disappear. The Governor of the Bank of England will stand all-powerful and able, by dint of raising his eyebrows, effectively to dismiss senior banking executives without discussing it with, or consulting, anyone. This is unsatisfactory. As the Treasury Committee has repeatedly stated, a much stronger governance framework is needed. Among other things this can ensure that the regulatory authorities are unable to remove senior bank executives arbitrarily or without just cause. We welcome the fact that the Chairman of the FSA agrees with us that governance processes must be put in place to ensure accountability and transparency for the process of removing senior bank executives in whom the regulators have lost confidence. (Paragraph 191)

43. According to the Chairman of Barclays, Mr Diamond continued to enjoy strong shareholder support. If this is indeed the case, then the actions taken by the Governor and the Chairman of the FSA were in opposition to the position of major Barclays shareholders. Although Lord Turner asserts that support for Mr Diamond had fallen away over the course of the weekend of 30 June 2012, there was no strong public clamour from institutional investors for the removal of Mr Diamond. The regulatory authorities need to possess the ability to remove senior executives, but when they exercise this power, they should recognise their duty of care to shareholders. This issue should be examined by the Bank of England, the FSA and its successor bodies. (Paragraph 192)

44. The UK Corporate Governance Code is clear that "the board should set the company's values and standards". However, the misconduct of LIBOR and breakdown of trust with the regulatory authorities has demonstrated that the Barclays board has presided over a deeply flawed culture. (Paragraph 193)

Enforcement

45. The Committee regrets that the FSA's acting director of enforcement and financial crime did not take the opportunity to explain how the factors the regulator takes into account had been applied to Barclays in this case. We are concerned about the lack of transparency in the way in which the FSA calculated the amount of the fine. (Paragraph 197)

46. The Committee urges the Wheatley review to consider the case for amending the present law by widening the meaning of market abuse to include the manipulation, or attempted manipulation, of the LIBOR rate and other survey rates. They should also consider the case for widening the definition of the criminal offence in section 397 of FSMA to include a course of conduct which involves the intention or reckless manipulation of LIBOR and other survey rates. (Paragraph 199)

47. The FSA apparently believes that its fees are not raised for the purpose of prosecuting offences other than those set out in FSMA. The Committee is concerned by this. The FSA has responsibility for regulating the key participants in financial markets. The FSA's decision whether to initiate a criminal prosecution should not be influenced by the fact that its income is derived from firms which it regulates. The FSA has an obligation under section 2(1)(b) of FSMA to discharge its functions in the way in which it considers most appropriate for the purpose of meeting its regulatory objectives. Under section 2(2)(d) the reduction of financial crime is one of these objectives. Financial crime is defined in section 6(3) as including not only misconduct in relation to a financial market but also any criminal offence of fraud or dishonesty. The FSA took a narrow view of its power to initiate criminal proceedings for fraudulent conduct in this case. The Committee recommends that the Government, following the Wheatley review, should consider clarifying the scope of the FSA's, and its successors', power to initiate criminal proceedings where there is serious fraudulent conduct in the context of the financial markets. (Paragraph 202)

48. The Serious Fraud Office (SFO) is now conducting a criminal investigation into LIBOR. The Committee was surprised that neither the FSA nor the SFO saw fit to initiate a criminal investigation until after the FSA had imposed a financial penalty on Barclays. (Paragraph 206)

49. The evidence in this case suggests that a formal and comprehensive framework needs to be put in place by the two authorities to ensure effective relations in the investigation of serious fraud in financial markets. The lead authority must be clearly identified for the purposes of an investigation, and formal minutes of meetings between the authorities must be maintained. We recommend that the Wheatley review examine whether there is a legislative gap between the responsibility of the FSA and the SFO to initiate a criminal investigation in a case of serious fraud committed in relation to the financial markets. (Paragraph 207)

Appendix: exchange of letters between Lord Turner, Chairman of the FSA, and Marcus Agius, Chairman of Barclays, 2012

Letter from Lord Turner to Marcus Agius, 10 April 2012

Dear Marcus

As promised, this letter follows up our recent meeting and sets out FSA concerns relating to aspects of Barclays' approach to regulatory and other issues.

Obviously where we have specific areas of concern which merit it, our Supervisory Team will directly make those concerns known at the appropriate level, and require any appropriate action in response. The purpose of my meeting with you was therefore not to focus on any one specific issue which requires remedial action. Rather I wished to bring to your attention our concerns about the cumulative impression created by a pattern of behaviour over the last few years, in which Barclays often seems to be seeking to gain advantage through the use of complex structures, or through arguing for regulatory approaches which are at the aggressive end of interpretation of the relevant rules and regulations. Andrew Bailey also expressed these concerns at your Board meeting on 9th February.

The specific examples which I mentioned at our meeting included two examples which I accept are 'old news', but also four relating to recent events.

<u>Old news</u>

I cited two examples.

- The development of the Protium structure in 2009 which, although not delivering Barclays any regulatory capital advantage and while within accounting rules, was perceived by many external commentators as a convoluted attempt to portray a favourable accounting result.
- The approach to the valuation of monoline CVA positions which became apparent in FSA analysis in early 2009, and which showed Barclays choosing valuations clearly at the aggressive end of the acceptable spectrum.

<u>More recent events</u>

Examples I cited were:

- Our concern that in the run up to the latest year-end, Barclays was not fully transparent with us about the RWA impacts of a proposed extension of model approaches (AIRB and IMM) applied in Barclays Capital Inc. Ultimately, we felt that the need for us to unpick the real impact of these proposed changes caused unnecessary friction and burdened our internal processes.

- [Redaction]
- Protracted communication between ourselves and Barclays about your desire to move index hedges of own credit from the trading book to the banking book, with the impact of materially reducing RWAs. In this case, after the initial outcome was not resolved in Barclays' favour, our team felt that Barclays continued to argue for capital optimization in a way which inefficiently used up our resource and goodwill.
- The confusing and potentially misleading impression created by Barclays' initial presentation of its position under the EBA stress tests, which appeared to be an attempt to leave FSA senior management with the impression that Barclays would be above the then intended 10% CT1 threshold, whereas at the relevant date of September 2011 it was actually at 9.8%. In fact given that the eventually chosen 'pass mark' was 9%, this did not turn out to be of crucial importance. But it nevertheless left our senior management with an impression that Barclays were seeking to 'spin' its messages in an unhelpful fashion.

I also mentioned at our meeting the recent publicity in relation to Barclays UK tax management. I recognise that since adequate provisioning had been put in place, this was not a regulatory issue per se. But as I know you recognise, and whatever the extent of advice which Barclays received in advance, the net impact has clearly been unfavourable to the degree of external trust in Barclays' approach to issues such as tax, regulation and accounting.

Clearly these examples vary in both currency and importance. And it is of course acceptable for a bank to argue for a favourable approach on any one specific issue, even if the regulator does not immediately agree. But the cumulative effect of the examples set out above has been to leave us with an impression that Barclays has a tendency continually to seek advantage from complex structures or favourable regulatory interpretations. These concerns are sufficiently great that I felt it was appropriate to communicate them directly to you, and to urge you and the Board to encourage a tone of full co-operation and transparency between all levels of your Executive and the FSA.

I know from our conversation that you take these issues seriously.

[Redaction]

Yours sincerely,

[Signed]

Adair Turner

Letter from Marcus Agius to Lord Turner, 18 April 2012

Dear Adair,

Thank you for your letter of 10 April, 2012.

It is a matter of regret for us that you have the concerns outlined in your letter. Barclays has invested significant effort and time in building and improving its relationship with the FSA. It is very important to us to have a strong, open, cooperative and transparent relationship with the FSA and with all of our regulators globally. The Board and I took note of Andrew Bailey's comments in our February meeting and, while he specifically excluded Bob Diamond and Chris Lucas from his comments, it was clear that "tone from the top" is one of the FSA's concerns. Our objective is and has always been to have a strong and mutually beneficial relationship with the FSA and you have my commitment that we will work harder in the future to procure this outcome.

Your letter notes six examples of areas of concern to the FSA and without wanting to prolong the debate on these; I do feel the need to make one or two comments in relation to these specific points.

- With regard to Protium, I believe this has been discussed exhaustively. As you know, we reconfirm that our objective at the time was to change the repayment profile and maximize shareholder value. As it turned out, this is exactly what occurred. As you note, this was done within accounting rules and with no regulatory capital advantage and with explicit FSA approval.

- The monoline CVA positions from 2009 represent a highly subjective area where we are and were aware of at least one other major European based bank which had valuations very similar to Barclays. As you note, these valuations were within the acceptable spectrum. Time and markets have proven these to be less aggressive than suggested.

- On the more recent experience of the run up to year-end, we recognise that we asked a lot of your team with regard to model approvals. These were waiver requests which came about later than expected but they were necessary given the late changes to our capital guidance at year end via the FPC to FSA. A guideline of 10% was moved to 10.30% at the very end of the year and so the criticality of these model approvals was paramount for us. We greatly appreciate the time and effort contributed by your team to facilitate these reviews.

  [Redaction]

- The discussions surrounding the index hedges of own credit were protracted because we had very strongly held views. Of course, the FSA has the ability to set rules and we respect the outcome of those discussions.

- We believe the concern you mention regarding capital stress tests refers to two separate but parallel requests from last year to assess the effect of EBA capital definitions: 1) an FSA request to ascertain whether 10% CT1 could be achieved by mid-2012 using a constant balance sheet and Basel 2.5 for December 2011 and 2) an EBA stress test request to estimate CT1 for June 2011 assuming the early adoption of Basel 2.5. Although both requests were related, we thought we were clear where differences existed in our responses because of the slightly different requests. We did not intend to mislead in any way and we will ensure that we communicate more clearly in the future.

Finally with regard to the UK tax issue, we fully understand the potential damage to our reputation. On the other hand, as tested recently through a third party review, our tax procedures are robust and sound but no procedure can guard against retroactive tax law changes. We acknowledge that this is not a comfortable place for us to be. Despite our voluntary disclosure to HMRC of the transactions, they did not inform us of their intention to change the law.

I appreciate your taking the time to write. I can assure you that the points you have raised have my full attention as well as the Board's. We are committed to ensuring the full cooperation of all levels of our Executive when engaging with the FSA and we take these matters very seriously, particularly as they relate to the transparency and openness of our interactions.

Yours sincerely,

[Signed]

Marcus Agius

Formal Minutes

Thursday 9 August 2012

Members present:

Mr Andrew Tyrie, in the Chair

Mark Garnier
Andrea Leadsom
Rt Hon Pat Mcfadden
John Mann
George Mudie
David Ruffley

Draft Report (*Fixing LIBOR: some preliminary findings*), proposed by the Chair, brought up and read.

Ordered, That the draft Report be read a second time, paragraph by paragraph.

Paragraphs 1 to 207 read and agreed to.

A Paper was appended to the Report.

Resolved, That the Report be the Second Report of the Committee to the House.

Ordered, That the Chair make the Report to the House.

Ordered, That embargoed copies of the Report be made available, in accordance with the provisions of Standing Order No. 134.

[Adjourned to a day and time to be fixed by the Chairman

Witnesses

List of Reports from the Committee during the current Parliament

Session 2012–13

First Report	Financial Services Bill	HC 161