

# The Bradford & Bingley plc Compensation Scheme

Independent Valuer – Peter J Clokey

Revised Assessment Notice in respect of shares and  
subscription rights

**14 March 2011**

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Any person who is affected by my determination in this Revised Assessment Notice of the amount of any compensation and who is dissatisfied with this Revised Assessment Notice may refer the matter to the Upper Tribunal (Tax and Chancery Chamber) in accordance with paragraph 12 of the Schedule to The Bradford & Bingley plc Compensation Scheme Order 2008 (as amended by The Transfer of Tribunal Functions Order 2010). Any such reference must be made using Form FTC3. Form FTC3 must be completed and signed by or on behalf of the person making the reference and received by the Upper Tribunal within the period prescribed in The Tribunal Procedure (Upper Tribunal) Rules 2008.

Paragraph 2(2) of Schedule 3 to those rules requires any reference to be received by the Upper Tribunal no later than 28 days after notice was given of this determination. At the same time a copy of the completed and signed Form FTC3 should be sent to: Peter Clokey, PricewaterhouseCoopers LLP, 1 Embankment Place, London WC2N 6RH.

For a copy of Form FTC3 and important information about how to complete it, please go to: [www.tribunals.gov.uk/financeandtax/FormsGuidance.htm](http://www.tribunals.gov.uk/financeandtax/FormsGuidance.htm)

The London address of the Upper Tribunal (Tax and Chancery Chamber) is:

The Upper Tribunal  
Tax and Chancery Chamber  
45 Bedford Square  
WC1B 3DN

The telephone numbers of the Upper Tribunal are 020 7612 9646 and 020 7612 9647.

# 1 Introduction

- 1.1. On 24 June 2009 I was appointed by Her Majesty's Treasury ("HMT") as independent valuer for the purposes of the Bradford & Bingley plc Compensation Scheme (the "Scheme") established under The Bradford & Bingley plc Compensation Scheme Order 2008 (as amended) (the "Compensation Scheme Order").
- 1.2. My role has been to determine the amount of any compensation payable by HMT under paragraphs 3 to 5 of the Schedule to the Compensation Scheme Order.
- 1.3. I issued an Assessment Notice on 5 July 2010 pursuant to paragraph 10 of the Schedule to the Compensation Scheme Order. In my Assessment Notice I set out the reasons why I had determined that no compensation is payable by HMT under the Scheme to:
  - Persons who held ordinary shares ("shareholders") in Bradford & Bingley plc ("Bradford & Bingley") immediately before they were transferred by The Bradford & Bingley plc Transfer of Securities and Property etc. Order 2008 (as amended) (the "Transfer Order"); and
  - Persons whose rights or other entitlements to receive ordinary shares ("holders of subscription rights") in Bradford & Bingley (within the definition of "subscription rights" set out in paragraph 4(3) of the Schedule to the Compensation Scheme Order) were extinguished by virtue of article 5 of the Transfer Order.

- 1.4. Paragraph 11(1) of the Schedule to the Compensation Scheme Order provides that any party affected by the determination of the amount of any compensation in my Assessment Notice who is dissatisfied with the Assessment Notice may require me to reconsider my determination. My Assessment Notice stated that any such requests should be submitted to me by 27 August 2010.
- 1.5. I have received requests for reconsideration of my Assessment Notice and I am therefore issuing a Revised Assessment Notice in accordance with paragraph 11(2) of the Schedule to the Compensation Scheme Order. This document is my Revised Assessment Notice. It is issued on 14 March 2011 and notifies all interested parties that, having considered carefully the arguments and evidence submitted to me with the requests for reconsideration of my Assessment Notice, I have decided to uphold my Assessment Notice. This Revised Assessment Notice therefore confirms that no compensation is payable by HMT under the Scheme to shareholders or holders of subscription rights.
- 1.6. In Sections 2 to 10 of this Revised Assessment Notice I summarise the main arguments and evidence submitted to me with the requests for reconsideration of my Assessment Notice and I set out my responses and my reasons for maintaining the conclusions reached in my Assessment Notice.

## 2 Procedure

### The 27 August 2010 deadline

- 2.1. My Assessment Notice included the following statement:  
  
*“Any party dissatisfied with this Assessment Notice may require me to reconsider my determination. To do so they should submit a request for me to reconsider together with the reason for the request and any supporting evidence. This request should be made to me by Friday 27 August 2010 at PricewaterhouseCoopers LLP, 1 Embankment Place, London WC2N 6RH. I will then consider all such requests and then issue a Revised Assessment Notice which will explain whether I have upheld or varied my Assessment Notice.”*
- 2.2. The deadline of 27 August 2010 that I imposed for requests for reconsideration to reach me has been criticised for giving insufficient time for affected parties to consider my Assessment Notice and decide whether, and if so on what basis, to request that I reconsider it. I have been asked to extend the deadline.
- 2.3. Paragraph 9 of the Schedule to the Compensation Scheme Order provides that “The valuer may make such rules as to the procedure in relation to the assessment of any compensation (including the procedure for the reconsideration of any decisions relating to the assessment of compensation) as he or she considers appropriate.”
- 2.4. When I issued my Assessment Notice, I considered the procedure set out in my Assessment Notice for the reconsideration of my decision relating to the assessment of compensation, including my requirement that I should receive any requests for reconsideration

by 27 August 2010, to be appropriate. In setting the 27 August 2010 deadline I sought to allow sufficient time for affected parties to have a fair opportunity to consider my Assessment Notice and to prepare any request for reconsideration and any evidence. I have considered the criticisms made of the deadline but I continue to consider it to be appropriate and I have therefore not extended it.

## **Publication of documents and evidence**

- 2.5. Another aspect of my procedure which has been criticised is my decision not to publish copies of documents and information, including documents to which I make specific reference in my Assessment Notice, that I obtained from various parties for the purpose of assessing the amount of any compensation payable under the Scheme by HMT or internal documents generated by me or my team since my appointment.
- 2.6. Paragraph 10 of the Schedule to the Compensation Scheme Order identifies the information that my Assessment Notice was required to contain. The required information is the date on which the notice is issued, the amount of any compensation that I determined as being payable and the reasons for my decision. There is no requirement for me to disclose any documents. I am satisfied that my Assessment Notice included the required information and, in particular, that it included a clear explanation of the reasons for my decision.
- 2.7. Paragraph 8D of the Schedule to the Compensation Scheme Order (as amended by The Bradford & Bingley plc Compensation Scheme (Amendment) Order 2009) provides that (subject to a requirement that I have regard to the need to exclude from disclosure so far as

practicable certain information) I may disclose documents or information that I obtained from any party for the purpose of assessing the amount of any compensation payable under the Scheme by HMT if and to the extent that I consider it necessary to do so for the purpose of exercising the functions of my office. When I issued my Assessment Notice I considered whether it was necessary for me to disclose any such documents or additional information for the purpose of exercising the functions of my office. I concluded that it was not and, having considered the arguments made, I remain of that view.

### **My independence**

- 2.8. In criticising my Assessment Notice a number of requests for reconsideration have questioned my independence and have suggested that I am biased in favour of HMT.
- 2.9. I can categorically state that in performing my task I have acted entirely independently of HMT and have reached what I consider to be the correct determination, applying the provisions of the Compensation Scheme Order, without favouring any party.

# 3 The Special Liquidity Scheme – “financial assistance” and “ordinary market assistance”

## **Section 5(4) of the Banking (Special Provisions) Act 2008**

3.1. Paragraphs 2.3 to 2.6 of my Assessment Notice address the assumptions (the “Statutory Assumptions”) set out in section 5(4) of the Banking (Special Provisions) Act 2008 (the “Act”). Those paragraphs state as follows:

*“2.3. Section 5(4) of the Banking (Special Provisions) Act 2008 (the “Act”) provides that in determining the amount of any compensation payable by HMT I must assume that:*

- all financial assistance provided by the Bank of England or HMT to Bradford & Bingley has been withdrawn (whether by the making of a demand for repayment or otherwise); and*
- no financial assistance would in future be provided by the Bank of England or HMT to Bradford & Bingley (apart from ordinary market assistance offered by the Bank of England subject to its usual terms).*

*I refer to these assumptions in the rest of this document as the “Statutory Assumptions”.*

*2.4. “Financial assistance” is given a broad meaning by sections 5(5)(a) and 15 of the Act. At the transfer time Bradford & Bingley had made use of the Bank of England’s Special Liquidity Scheme (the “SLS”). In my opinion the use of this scheme would constitute the provision of financial assistance by*

*the Bank of England. It follows that in determining the amount of any compensation payable by HMT the Statutory Assumptions require me to assume that assistance to Bradford & Bingley through the SLS has been withdrawn.*

*2.5. To give effect to the Statutory Assumptions, I have had to consider what sort of financial assistance constitutes “ordinary market assistance offered by the Bank of England subject to its usual terms”. The term “ordinary market assistance” is defined by section 5(5)(b) of the Act as being “assistance provided as part of the Bank’s standing facilities in the sterling money markets or as part of the Bank’s open market operations in those markets”. I have interpreted the terms “the Bank’s standing facilities in the sterling money markets” and “the Bank’s open market operations in those markets” to be references to two of the elements (“standing facilities” and “open market operations”) of the Bank of England’s published framework (the “Sterling Monetary Framework”) for its operations in the sterling money markets. The SLS was not part of those elements of the Sterling Monetary Framework and, indeed, when it launched the SLS in April 2008 the Bank of England announced that the SLS “will be ring-fenced and independent of the Bank of England’s regular money market operations” [Footnote reference to the Bank of England News Release – Special Liquidity Scheme, 21 April 2008]. Accordingly, I consider that assistance provided through the SLS does not constitute “ordinary market assistance” as that term is defined in the Act. This means that the Statutory Assumptions require me to assume that assistance through the*

*SLS would in future not be provided to Bradford & Bingley by the Bank of England.*

*2.6 Various parties have put arguments to me to the effect that, contrary to my expressed view, assistance through the SLS does constitute “ordinary market assistance”. I have considered carefully these arguments but do not accept them because I consider that they do not properly take account of the statutory definition of the term “ordinary market assistance”.*”

3.2. In summary my Assessment Notice set out that I had concluded that the use of the Bank of England’s Special Liquidity Scheme (the “SLS”) would constitute the provision of “financial assistance” but not “ordinary market assistance” by the Bank of England for the purpose of the Act. It followed that I decided that in determining the amount of any compensation the Statutory Assumptions required me to assume that all SLS funding had been withdrawn from Bradford & Bingley and that no SLS funding would in future be provided to Bradford & Bingley.

## **Financial assistance**

3.3. It has been submitted to me that I have failed to provide any analysis to support the statement in paragraph 2.4 of my Assessment Notice that the use of the SLS would constitute the provision of “financial assistance” by the Bank of England for the purpose of section 5(4) of the Act.

3.4. Section 15 of the Act gives a broad and non-exhaustive meaning to “financial assistance”. It provides that “financial assistance”, in relation to any person, includes:

- “(a) assistance provided by way of loan, guarantee or indemnity,
- (b) assistance provided by way of any transaction which equates, in substance, to a transaction for lending money at interest (such as a transaction involving the sale and repurchase of securities or other assets), and
- (c) assistance falling within paragraph (a) or (b) provided indirectly to or otherwise for the benefit of the person (including the provision of assistance within paragraph (a) or (b) to any group undertaking of that person),

whether provided in pursuance of an agreement or otherwise and whether provided before or after the passing of this Act.”

- 3.5. The purpose of the SLS was to improve the liquidity position of the banking system and restore confidence in financial markets by enabling qualifying institutions to borrow, for a period, Treasury bills against the collateral of certain illiquid assets. During the lifetime of a loan under the SLS the participating institution was required to pay a fee to the Bank of England. The intention and effect of the SLS was to provide the participating institution with assets (Treasury bills) that could be used as collateral or sold, by lending such assets to the institution against the collateral of other assets which had become illiquid because the markets in them had effectively closed.
- 3.6. In my view, this arrangement amounted to the provision of “financial assistance” within the non-exhaustive meaning given by the Act to those words. I also consider the SLS to have been “financial assistance” within the ordinary meaning of those words. It follows that I consider that the use of the SLS amounted to the provision of “financial assistance” within the meaning of section 15 of the Act.

## Ordinary market assistance

- 3.7. I have been asked whether my conclusion that the use of the SLS is not “ordinary market assistance” for the purpose of section 5(4) of the Act relies on any factors other than those set out at paragraphs 2.5 and 2.6 of my Assessment Notice. I confirm that my reasons for deciding that the use of the SLS is not “ordinary market assistance” are as set out in paragraphs 2.5 and 2.6 of my Assessment Notice and as further explained in paragraphs 3.8 to 3.42 below.
- 3.8. Various arguments have been made to me to the effect that I was wrong to decide (and had no proper basis for deciding) that the use of the SLS is not “ordinary market assistance” for the purpose of the Act. I have considered carefully all of the reasoning and evidence advanced in support of these arguments and I set out below my reasons why these arguments have not led me to change my conclusions.
- 3.9. It has been submitted that I have acted outside of my “statutory terms of reference” by placing my own interpretation on the statutory words “ordinary market assistance”. I explained in paragraph 2.5 of my Assessment Notice that to give effect to the Statutory Assumptions I have to consider what sort of financial assistance constitutes “ordinary market assistance offered by the Bank of England subject to its usual terms” for the purpose of section 5(4) of the Act. I must necessarily interpret these words to perform my role. I do not accept the criticism that by interpreting these words I am in some way exceeding my remit.

- 3.10. Many of the arguments put to me amounted to the suggestion that I should have given a wide meaning to the statutory words “ordinary market assistance”. However, I do not consider that it is open to me to do so. An exhaustive definition of the words “ordinary market assistance” is set out in section 5(5)(b) of the Act. Section 5(5)(b) provides that “ordinary market assistance” means “assistance provided as part of the Bank’s standing facilities in the sterling money markets or as part of the Bank’s open market operations in those markets”. Consequently, those are the key words that I have to interpret.
- 3.11. In paragraph 2.5 of my Assessment Notice I explained that I have interpreted the terms “the Bank’s standing facilities in the sterling money markets” and “the Bank’s open market operations in those markets” to be references to two of the elements (“standing facilities” and “open market operations”) of the Bank of England’s published framework (the “Sterling Monetary Framework”) for its operations in the sterling money markets. It has been submitted that my interpretation is wrong because Parliament could have, but did not, refer to “the Sterling Monetary Framework document” (or similar) as being the statutory definition of “ordinary market assistance”.
- 3.12. I am not persuaded by this argument. Section 5(4) refers to two particular activities of the Bank of England in the sterling money markets, namely, (i) the provision of standing facilities and (ii) open market operations. The documentation governing participation in the Bank of England’s operations under the Sterling Monetary Framework (the “SMF Documentation”)<sup>1</sup> sets out, at all material

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<sup>1</sup> The SMF documentation is available at <http://www.bankofengland.co.uk/markets/money/documentation.htm>

times (by which I mean the date the Act came into force, the date of the Transfer Order and the date of the Compensation Scheme Order), an official statement of what its standing facilities and open market operations in the sterling money markets comprised. In my view, the references in section 5(4) of the Act to these activities are most naturally interpreted as being references to the activities described in that official statement as being the Bank of England's standing facilities and open market operations. This analysis is reinforced by the confirmation I have received from the Bank of England that at all material times the only activities that it considered to be standing facilities and open market operations carried out by it in the sterling money markets were those described in the SMF Documentation. Accordingly, I consider that the definition used in the Act requires me to consider whether the SLS was one of the Bank's standing facilities or open market operations as described in the SMF Documentation.

- 3.13. The Bank of England has explained to me the difference in structure and purpose between the SLS on the one hand and the Bank of England's standing facilities and open market operations on the other, making the following points:
- (a) The Bank of England's core purposes are to ensure monetary stability and to contribute to financial stability. The Bank of England's operations in the sterling money markets serve both. Those operations are designed to implement the decisions of the Monetary Policy Committee in order to meet the inflation target, and to reduce the cost of disruption to the liquidity and payment services supplied by banks to the UK economy, by

providing liquidity insurance to individual credit-worthy institutions and to the system as a whole.

- (b) The Bank of England's standing facilities and open market operations each contribute toward the pursuit of both of these objectives. In particular:
- The Bank of England's standing facilities are deposit and collateralised lending facilities available to eligible UK banks and building societies. They involve the deposit or lending of cash and therefore provide a form of liquidity insurance to eligible institutions. They are priced with reference to the official Bank Rate, in a manner that seeks to ensure that market rates are close to the official Bank Rate.
  - The Bank of England's open market operations comprise short and long term repos, and outright purchases of high-quality bonds at prices determined by tender. (Repos are contracts under which assets are bought and sold, with agreement for the seller to buy back the assets at a future date for a higher price. They are economically similar to secured loans, where the original seller is the borrower, and the difference in price operates as the interest rate on the loan.) As with the standing facilities, the open market operations provide a direct source of cash liquidity to the institutions which participate in the tenders. Open market operations are carried out primarily for rate setting purposes; they ensure that the required amount of reserves are available to meet banks' and building societies' demand for reserves. An excess supply of reserves, relative to that demand, would tend to push down on market interest rates,

and vice versa. By providing the right amount of reserves to the market, the Bank of England ensures that market rates are close to Bank Rate.

- (c) The SLS did not have the same structure or purposes. Its sole objective was to improve the liquidity of the banking system. It did not provide this liquidity directly in the form of cash (as with the standing facilities and open market operations). Instead, it allowed institutions to borrow Treasury bills from the Bank of England (that could readily be used as collateral for the borrowing of cash in the market) using, on a bilateral basis as collateral, various forms of securities that institutions had ceased to regard as acceptable collateral for loans to each other. As it was a temporary scheme, aimed at addressing a very specific liquidity shock, only securities on balance sheet (or formed of assets on balance sheet) at the end of December 2007 were eligible as collateral. No liquidity insurance against newly originated assets was provided by the SLS. Because the SLS was a form of asset swap, it had no impact on the supply of central bank money and thus no direct implications for monetary policy. Its structure was not designed to align market interest rates with the official Bank Rate.

- 3.14. Several of the arguments put to me have involved the suggestion that because the SLS shares with the Bank of England's standing facilities and open market operations the objective of providing liquidity, it should be regarded as being effectively the same thing. However, as is clear from the description above, the SLS only shares one of the objectives pursued by the provision of standing facilities and open market operations. It does not share the objective

of aligning market interest rates with the official Bank Rate. And though it shared with the standing facilities and open market operations the objective of providing liquidity, it achieved this in a very different way, as explained above. Consequently, I do not consider that it would be right to conclude that the SLS falls within the Parliamentary intention expressed by the use of the words “assistance provided as part of the Bank’s standing facilities in the sterling money markets or as part of the Bank’s open market operations in those markets”.

- 3.15. It has been submitted that because of the structure and widespread use of the SLS, if the Act had been introduced after the establishment of the SLS, it would have been made clear that the SLS should be regarded as ordinary market assistance for the purpose of the Act. In support of this submission I am asked to have regard to the following points: (i) the SLS was a “standing” facility because it was a current facility open to eligible banks (like the standing facilities under the Sterling Monetary Framework), (ii) at the time of the Transfer Order the SLS remained “standing” as it had not been withdrawn by the Bank of England, (iii) the SLS was made available to Bradford & Bingley and other banks as a “facility” from which they could draw down and the Bank of England had communicated to Bradford & Bingley its “facility limit” under the SLS, (iv) the Bank of England’s 2008 consultative paper published in October 2008 entitled “The Development of the Bank of England’s Market Operations” explained that the Bank of England was replacing its standing facilities with Operational Standing Facilities and a Discount Window Facility (“DWF”); the DWF forms part of the Sterling Monetary Framework and is regarded as the successor of

the SLS, (v) the references to “standing facilities” and “open market operations” in section 5(5)(b) of the Act are a product of the information available to the draftsman at the time the Act was drafted and not determinative of the types of financial assistance which should be regarded as “ordinary market assistance” for the purpose of the Act and (vi) as a result, the relevant question is whether the use of the SLS was “ordinary market assistance” rather than whether it was a “standing facility” or an “open market operation”.

- 3.16. I am not persuaded by these arguments. Firstly, in my view this submission does not properly take account of the actual exhaustive statutory definition of the term “ordinary market assistance” and invites me, in effect, to rewrite that definition by extending it to cover other activities of the Bank of England that Parliament might have chosen to include alongside standing facilities and open market operations if it had existed at the time of the drafting of the Act. I do not consider that it is open to me to do so. It was open to Parliament to include a mechanism allowing the definition of “ordinary market assistance” to be extended to cover newly introduced activities of the Bank of England, but that was not done. It was also open to Parliament to adopt a wider, non-exhaustive definition of “ordinary market assistance”, in place of the exhaustive definition that was adopted. Accordingly, I consider that I have no option but to consider whether the SLS was one of the Bank of England’s standing facilities or open market operations in the sterling money markets.
- 3.17. Secondly, as I have stated above, I consider that the SMF Documentation describes the only standing facilities made available, and open market operations carried out, by the Bank of England in

the sterling money markets at all material times, and that the SLS was not a “standing facility”.

- 3.18. Thirdly, the Bank of England has explained to me that it is not correct to say that Bradford & Bingley had a “facility limit” under the SLS. Rather, drawings under the SLS in excess of a certain amount would have required approval by senior management at the Bank of England.
- 3.19. Fourthly, I do not consider that the replacement of the Bank of England’s standing facilities with its newly introduced Operational Standing Facilities and the DWF indicates that the SLS falls within the definition used in the Act. The purpose of the change is explained in a speech on 30 September 2010 by Paul Fisher, the Bank of England’s Executive Director, Markets, that is published on the Bank of England’s website. As Mr Fisher explains, “Although similar in principle, the Discount Window is not intended to be a direct replacement for the Special Liquidity Scheme. It is both shorter-term and more expensive in steady-state, in line with the underlying principles for all the Bank of England’s permanent liquidity insurance operations: that commercial banks should be incentivised to manage their liquidity risk prudently in the market. The terms were also designed to protect the Bank against risk to its own balance sheet”. It is therefore not correct to regard the DWF as the direct successor to the SLS, let alone to reason backwards from the introduction of the DWF so as to conclude that the SLS was a “standing facility”. It is also far from clear that the DWF would fall within the statutory definition, since although it is part of a structure now operated in place of the Bank of England’s standing facilities, it

only covers one of the purposes (the provision of liquidity) previously promoted by the Bank of England's standing facilities.

- 3.20. A similar submission is based on the similarity between the SLS and the DWF in terms of structure, purpose and utilisation. The submission is as follows: (i) the DWF was introduced on 20 October 2008 and superseded the SLS and it has been formally recognised by the Bank of England as being part of its "standing facilities"; (ii) the SLS and the DWF are both facilities that involve an asset swap where participating financial institutions are able to borrow Government debt by posting collateral with the Bank of England; (iii) the SLS and the DWF were both introduced to deal with liquidity issues in the sterling money markets; (iv) eligibility to participate in both the SLS and the DWF is determined by reference to eligibility to participate in the Bank of England's other Sterling Monetary Framework facilities; (v) given these similarities and the roles played by the SLS and DWF it would be perverse if a bank taken into public ownership would be assumed by a valuer to have access to the DWF but not the SLS; (vi) if the SLS and the DWF are treated differently under the Act, such an approach would lead to markedly different valuations dependent solely on the precise date of nationalisation.
- 3.21. Again, in my view, this submission invites me effectively to rewrite the statutory definition of "ordinary market assistance" and I do not consider that it is open to me to do so. As explained above, the DWF is a new form of liquidity insurance provided by the Bank of England to the banking system. The fact that it has been introduced in order to promote one of the objectives previously sought to be promoted by standing facilities does not cause me to conclude that the SLS is

a “standing facility”. In my opinion, reinforced by discussions with the Bank of England, the SLS does not fall within the definition even if (which is far from clear as explained in paragraph 3.22 below) the DWF would have done so.

- 3.22. With regards to points (v) and (vi), I do not consider that it is part of my remit to consider whether, with hindsight, the Act produces an outcome that is rational from a policy perspective. The argument that I should avoid a “perverse” result assumes that I can and should extend the definition set out in section 5(4) of the Act to include other activities of the Bank of England that answer to similar policy criteria. I do not consider that it is open to me to perform such an exercise. Moreover, I do not consider that it is clear that the outcome of such an exercise would favour the conclusion that Parliament intended to include the form of assistance now constituted by the DWF. The Act restricts the definition to two activities of the Bank of England – the provision of standing facilities and open market operations – each of which served the dual purpose of setting interest rates and providing liquidity insurance, the former being the dominant purpose. By contrast, the DWF is solely designed to provide liquidity insurance. Consequently, it is not clear that Parliament would have chosen to include the DWF within the statutory definition if it had been part of the Bank of England’s activities when the Act was passed.
- 3.23. It has also been submitted to me by reference to the Bank of England’s October 2008 consultative paper (see paragraph 3.15 above) that it follows from the Bank of England’s decision to make changes to “its published framework of permanent facilities” that the Sterling Monetary Framework concerns only “permanent facilities” whereas “the Bank’s standing facilities in the sterling money

markets” include facilities “which may be available for a defined period”.

- 3.24. I do not agree. The fact that the Bank of England’s consultative paper (published after the Act came into force) referred to “its published framework of permanent facilities” does not, in my view, support the argument that the reference in section 5(5)(b) of the Act to “*the Bank’s standing facilities in the sterling money markets*” is intended to refer to something other than the “standing facilities” element of the Sterling Monetary Framework. The paper outlined the Bank of England’s proposed reforms of the Sterling Monetary Framework. As the Bank of England’s summary note accompanying the paper explained, “The paper is not about the range of exceptional operations and facilities currently being offered by the Bank. It is about plans for a permanent framework that will persist once the current crisis has eventually passed.” The “standing facilities” were available within that permanent framework.
- 3.25. The text from the Bank of England news release of 21 April 2008 that I quote in paragraph 2.5 of my Assessment Notice uses the word “regular”. It has been submitted that I wrongly regarded the words “regular” and “ordinary” (the word used in section 5(4) of the Act) as synonymous.
- 3.26. I do not accept this argument. I did not regard the word “regular” to be intended to contrast the SLS with “ordinary” money market operations. Rather, I regarded the Bank of England’s statement (and the similar statement in the Bank of England’s briefing note of 21 April 2008 that accompanied the news release – “This Scheme will be completely ring-fenced from, and independent of, the Bank of England’s money market operations” – that did not use the word

“regular”) as consistent with my understanding that the SLS was not part of the Sterling Monetary Framework. The Bank of England has confirmed to me that its use of the word “regular” was merely intended to emphasise that the SLS was not part of the Sterling Monetary Framework. I referred to the news release to support my immediately prior statement in paragraph 2.5 of the Assessment Notice that “*The SLS was not part of those elements of the Sterling Monetary Framework.*” I remain of the view that the SLS was not part of the Sterling Monetary Framework.

- 3.27. It has been submitted that the reference in the news release to the SLS being ring-fenced and independent must be construed in the light of the next sentence of the news release - “So it will not interfere with the Bank’s ability to implement monetary policy.” The argument is that this was the reason for the ring-fencing, not as I am said to imply, so as to distinguish the SLS from “ordinary” money market operations. As I explain above, I did not regard the word “regular” to be intended to contrast the SLS with “ordinary” money market operations and I referred to the news release to support my immediately prior statement in paragraph 2.5 of the Assessment Notice that “*The SLS was not part of those elements of the Sterling Monetary Framework.*” However, the fact that the SLS was ring-fenced highlights a key difference of substance between the SLS and the Bank of England’s standing facilities and open market operations, the primary purpose of each of which is to assist in the Bank of England’s function of setting interest rates.
- 3.28. It has been submitted that there was nothing in the Bank of England’s announcement of the SLS which describes it as extraordinary and that, although the SLS was “temporary”, it was of

a relatively long-term nature as when it was introduced it was announced that “the swap terms under it (the SLS) could be extended for up to 3 years”.

- 3.29. I am satisfied that the Bank of England did use language suggesting that the SLS is “extraordinary”. The name – “Special Liquidity Scheme” – suggests a scheme that is out of the ordinary, and it was described as “exceptional” by the Bank of England in October 2008 (see paragraph 3.24 above). The SLS was also clearly “extraordinary” in the sense that it was only open for drawdown for a limited period, and applied only to assets held at a particular balance sheet date. But, in any event, on my interpretation of the statutory definition of “ordinary market assistance” set out in section 5(5)(b) of the Act, the argument about whether or not the SLS was described by the Bank of England as “extraordinary” misses the key point, which is that the SLS was not part of the Bank of England’s “standing facilities” or “open market operations” in the sterling money markets, these being the two particular sets of activities that the Act uses in its exhaustive definition of the term “ordinary market assistance”. Similarly, I do not consider the fact that asset swaps under the SLS could be renewed for a total of up to 3 years to be relevant to the question of whether the SLS was part of the relevant elements of the Sterling Monetary Framework and therefore constituted “ordinary market assistance” for the purpose of the Act.
- 3.30. It has been submitted that it appears from the face of the Bank of England’s briefing note dated 21 April 2008 that the SLS was announced in the context of ordinary central bank operations, in the light of the circumstances prevailing in April 2008 and the failure of the measures taken prior to that date to alleviate the problems they

were intended to resolve. The passages from the briefing note relied on are as follows:

#### “Central bank operations

Banks routinely borrow money from central banks in exchange for assets. They do so to manage their day-to-day cash needs as they lend and borrow funds. In response to the stresses in financial markets, central banks worldwide have extended their lending facilities. Since August, the Bank of England has increased by 42% the amount of central bank money made available to financial institutions. It has increased from 31% to 74% the proportion of its lending to the market that is for a term of at least three months. Since December, the Bank has also widened the range of high-quality assets accepted in its 3-month lending operations to include mortgage-backed securities. The stock of outstanding lending against that wider range of collateral is £25bn. These changes have aimed to alleviate the problem of financing the large overhang of illiquid assets on banks’ balance sheets.

#### The new Scheme

To tackle this problem decisively, the Bank of England has designed a Special Liquidity Scheme.”

- 3.31. This does not change my view that the use of the SLS is not “ordinary market assistance” for the purpose of the Act. This argument does not address the key point that the SLS was not part of the Bank of England’s “standing facilities” or “open market operations” in the sterling money markets and therefore, on my interpretation of section 5(5)(b) of the Act, the use of the SLS was not “ordinary market assistance”.

3.32. It has been submitted that the SLS cannot be regarded as unusual or out of the ordinary because it was not assistance specific to one institution but an arrangement (which is argued to have been a “standing facility”) open to all qualifying banks. Reliance is placed in this regard on the third paragraph of the extract from the statement of Lord Myners in the House of Lords debate on 15 December 2008 set out below:

“Crucially, this compensation must be fair, which means that it should be based on a realistic assessment of the shares’ value without public support. It is fair and right that the Government should not be required to compensate shareholders, or others affected, to the extent that taxpayers’ support inflated the value of their shares. Taxpayers should not be expected to pay compensation for value that would not exist without their support. The mandatory assumptions in the Act give effect to that.

However, it is important to note that this order does not impose the same assumptions on the valuer of Bradford & Bingley that were imposed on the valuer for Northern Rock. In the Northern Rock compensation scheme order, as well as assuming that state support had been withdrawn and that no such support would be provided in future, the valuer was required to assume that Northern Rock was not a going concern and that it was in administration. That difference is because the position of Bradford & Bingley was not the same as Northern Rock’s.

When taken into public ownership in February 2008, Northern Rock had been in receipt of substantial institution-specific financial assistance for over five months, in the form of both loans from the Bank of England and the provision of Treasury guarantee

arrangements. By contrast, no such guarantee arrangements had been provided to Bradford & Bingley, and the Bank of England had provided no loan facilities to it that were not also open to all qualifying institutions. As a result, it is right to impose no further assumptions beyond the mandatory assumptions under the Banking (Special Provisions) Act 2008. It will be for the valuer to assess the implication of those assumptions.”

- 3.33. I recognise that all of the banks and building societies that were eligible to sign up for the standing facilities within the Sterling Monetary Framework were able to take part in the SLS. But this does not alter my view that the SLS was not “standing facilities” or “open market operations” and therefore was not “ordinary market assistance” for the purpose of the Act. Lord Myners was referring to the direct assumptions of being in administration or being unable to continue as a going concern that were required to be made in relation to Northern Rock (and which are expressly mentioned in section 9(2) of the Act). As he indicated, it was for me to assess the implications of the Statutory Assumptions (which he referred to as the “mandatory assumptions”).
- 3.34. I have been asked to consider whether the SLS was intended to form part of, or be a temporary extension to, the Bank of England’s ordinary market assistance on its usual terms in April 2008, given the circumstances then prevailing. I consider that it is only open to me to consider this question by reference to the statutory definition of open market assistance as being the Bank of England’s standing facilities or open market operations in the sterling money markets. As I have stated above, I do not consider that the SLS fell within either of those terms. Furthermore, for the reasons set out above, I

consider that the SLS was distinct in nature and purpose from the operations referred to in the Act as comprising the Bank of England's ordinary market assistance.

- 3.35. It has been submitted that the Bank of England's policies are not unchangeably set in stone. Rather, they can and do change as economic circumstances change and, although the SLS was not originally part of the regular money market activities, access to it had become a "de facto" part of regular money market activities and normal operations of the Bank of England to maintain adequate market liquidity and thus part of the Bank of England's "ordinary market assistance". Reliance is placed on the fact that (as I record at paragraph 3.7 of my Assessment Notice) the SLS was used by over 30 banks and building societies. I am asked to take into account that 32 banks and building societies accessed the SLS, borrowing some £185 billion of UK Treasury bills, that those firms accounted for more than 80% of the sterling balance sheet of the institutions eligible to use the SLS and that the disclosures in relation to the SLS in the various securities offering materials and annual reports and accounts of the banks and building societies which relied on the SLS demonstrate how widespread the use of the SLS was by financial institutions in 2008. This use occurred over a significant period of time. The argument is that what constitutes "ordinary market assistance" is determined by the regularity of use and the period over which that use occurs, not by any statements of the Bank of England which became outdated by market events.
- 3.36. For the same reasons as I give above I do not accept this argument. In my view what determines whether the SLS is "ordinary market assistance" for the purpose of the Act is whether it was provided

pursuant to the Bank of England's standing facilities or open market operations in the sterling money markets. In my opinion it was not.

3.37. It has been submitted that the UK Government has, in its negotiations with the EU Commission, adopted the position that use of the SLS is part of the "ordinary market assistance" provided by the Bank of England. Reliance is placed on an EU Commission document headed "Financial Support Measures to the Banking Industry in the UK" and dated 13 October 2008 by which the Commission notified its decision that various measures notified by the UK Government, including a proposal to make available about £200 billion to eligible banks under the SLS, were compatible with the common market. The document includes the following passage which, it is submitted, records that the UK Government has accepted that the SLS is part of the Bank of England's "ordinary market assistance":

"The UK authorities accept that the recapitalisation scheme and guarantee scheme contain State aid elements. In their view the extension of the SLS is part of the essential role of the Bank of England and therefore not a state aid. In the event that the Commission concludes that the Liquidity Measures do contain aid elements, the UK Government submits that they form part of a wider package to remedy a serious disturbance in the economy of the United Kingdom which is compatible with the common market."

3.38. I do not consider that these materials assist me to determine whether the use of the SLS constitutes "ordinary market assistance" for the purpose of the Act. That question relates to a statutory definition which has no necessary relationship to the criteria being applied by the EU Commission in relation to state aid.

- 3.39. I have been asked to consider whether the SLS was understood to be “ordinary market assistance” by the banks to which the SLS was made available. It is submitted that the fact that the SLS was introduced in a time of particular economic turmoil to deal with a lack of liquidity across the banking industry as a whole does not affect the fact that it was regarded by those that used it as part of the Bank of England’s ordinary market assistance regime. It was regarded as another source of funding, alongside the Bank of England’s long-term repo operations and the other standing facilities.
- 3.40. I do not regard this as a relevant enquiry. “Ordinary market assistance” is given a particular meaning by section 5(5)(b) of the Act. Whether participants in the SLS regarded its use as “ordinary market assistance” in a general sense is irrelevant.
- 3.41. It has been submitted that the SLS was replaced by other similar measures to improve liquidity in the money markets – specifically “the Quantitative Easing programme” which it is said included an “Asset Purchase Facility” and a “Secured Commercial Paper Facility” which it is said provided similar facilities to the SLS. These measures have continued to underpin the operation of the money markets and therefore, it is submitted, have in practice become a normal part of the operations of the Bank of England since 2008.
- 3.42. I consider that an assertion that other assistance that is similar to the SLS has in practice become a normal part of the Bank of England’s operations does not mean that the SLS was “ordinary market assistance” for the purpose of the Act. For the reasons given above I think it was not. I also do not consider that the measures referred to are in fact similar to the SLS. The Asset Purchase Facility (which included the Secured Commercial Paper Facility) is used to

inject cash into the system. The purchase of assets may be financed by the issue of Treasury bills or (where the purpose is to provide monetary stimulus to the economy) by the Bank of England creating money. Within this structure, the Secured Commercial Paper Facility also pursued the narrower objective of providing working capital to companies. These are very different activities from the SLS.

## 4 Alternatives to a transfer into public ownership

- 4.1. In Section 3 of my Assessment Notice I determined that, if there had been no Transfer Order, Bradford & Bingley would not have had adequate liquidity to continue as a going concern, that it would have applied to Court for an administration order before the “transfer time” (which term is defined in the Compensation Scheme Order as “8.00 a.m. on 29th September 2008”<sup>2</sup>) and that an administration order would have been made by the Court either before the transfer time or shortly thereafter. I refer to these as “my Section 3 determinations” below.
- 4.2. In this Section 4 I consider the main submissions that have been made to me to challenge my Section 3 determinations. Sections 5 (“Sale of deposit business and branch network”), 6 (“Possible bids for Bradford & Bingley”) and 7 (“Recent financial performance”) separately consider further submissions on specific topics that also challenge my Section 3 determinations.
- 4.3. It has been submitted that my Section 3 determinations were entirely reliant on my erroneous view that the use of the SLS was not “ordinary market assistance” for the purpose of the Act and that I was therefore wrong to proceed on the basis that further SLS funding would not have been available to Bradford & Bingley after the transfer time.

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<sup>2</sup> I have adopted this definition of “transfer time” in the rest of this document.

- 4.4. I have addressed the arguments on the meaning of “ordinary market assistance” in Section 3 above. It is not correct, however, that I have relied entirely on my view that the use of the SLS was not “ordinary market assistance” for the purpose of the Act in deciding that further SLS funding would not have been available to Bradford & Bingley after the transfer time. As I set out in Section 3 of my Assessment Notice, the Bank of England did not approve any additional access to the SLS following Bradford & Bingley’s indication that it would be seeking further SLS funding prior to the transfer time. This fact formed part of the basis for my Section 3 determinations. I made my Section 3 determinations (in paragraphs 3.20 to 3.24 of my Assessment Notice) independently of the Statutory Assumptions (and therefore independently of my view that the use of the SLS was not “ordinary market assistance” for the purpose of the Act). I explained, in paragraph 3.25 of my Assessment Notice, that the application of the Statutory Assumptions reinforced my conclusion that Bradford & Bingley would have been unable to continue as a going concern.
- 4.5. My Section 3 determinations are also criticised on the basis that:
- (i) Bradford & Bingley was solvent and had solvency ratios in excess of EU guidelines. It is said that it is not clear from the face of the Assessment Notice that Bradford & Bingley was in fact insolvent.
  - (ii) Bradford & Bingley had capital that not only exceeded the minimum regulatory capital requirements but also, at 9.4% for tier 1 capital, compared favourably with other UK banks.

- (iii) I did not express disagreement in my Assessment Notice with the statement of the Group Finance Director (referred to at paragraph 3.16 of my Assessment Notice) that the Board should have no concerns with regard to the regulatory capital position of Bradford & Bingley.
- (iv) The Bradford & Bingley unaudited Interim Financial Report for the 6 months ended 30 June 2008 recorded proforma shareholder equity of £1.54 billion.
- (v) The rights issue which closed on 15 August 2008 was approved by HMT and the FSA.
- (vi) Both before (including shortly before) and after the transfer time Bradford & Bingley and its directors made positive statements in relation to the financial standing of Bradford & Bingley (including statements that Bradford & Bingley was both solvent and well above its regulatory minimum capital requirements at the transfer time) and that at least some of these statements were approved by the FSA and the Bank of England. It is said that these statements contradicted the “Reasons for Action” given in the FSA First Supervisory Notice to Bradford & Bingley on 27 September 2008 (quoted in paragraph 3.15 of my Assessment Notice).

4.6. In Section 3 of my Assessment Notice, I recorded my determination that, if there had been no Transfer Order, Bradford & Bingley’s liquidity position would have prevented it from continuing as a going concern and that it would have applied to Court for an administration order. The submission summarised at (i) above states that Bradford & Bingley had “solvency ratios” in excess of EU guidelines.

Assuming that this is a reference to capital adequacy as opposed to liquidity, it is the case that Bradford & Bingley satisfied the applicable capital requirements as at the transfer time.

- 4.7. Bradford & Bingley was subject to liquidity requirements imposed by the FSA and set out in the Interim Prudential sourcebook for banks. These requirements included a floor level of liquidity and a forward looking ratio. Bradford & Bingley monitored its core liquidity and reported this to the FSA together with an assessment of its minimum liquidity requirement which was calculated as £750 million plus the next five working days of wholesale maturities.
- 4.8. Bradford & Bingley's closing core liquidity position on Friday 26 September 2008 was around £2.6 billion. Retail activity over the weekend was expected to continue and result in significant cash outflows on Monday 29 September 2008. These outflows together with wholesale funding maturities were such that, at 4pm on Sunday 28 September 2008, Bradford & Bingley was projecting a closing core liquidity position on that Monday of around £2.1 billion. The FSA had concluded by the morning of Saturday 27 September 2008 that Bradford & Bingley had inadequate liquidity resources. Given future wholesale maturities and continued uncertainty around further deposit outflows, I agree with this conclusion.
- 4.9. The submission summarised at (ii) above accurately repeats what I said in the final sentence of paragraph 3.11 of my Assessment Notice. This relates to Bradford & Bingley's capital position, not its liquidity position.
- 4.10. The submission summarised at (iii) above is accurate. In my Assessment Notice I did not express disagreement with the

statement of the Group Finance Director as to Bradford & Bingley's regulatory capital position. The question of Bradford & Bingley's capital position is different from that of its liquidity position and having concluded that Bradford & Bingley's liquidity position would have prevented it from continuing as a going concern it was not necessary for me to comment on the statement of the Group Finance Director. In making my determination in relation to liquidity I considered whether there was any realistic possibility that Bradford & Bingley could have disposed of assets to avoid breaching its minimum liquidity requirements. The nature of the assets that could have been sold was such that a disposal could only have been achieved at a significant discount in the prevailing market conditions. The value of assets that Bradford & Bingley would have been required to sell to avoid any breach of minimum liquidity requirements would have resulted in losses leading to a breach of its capital adequacy requirements.

- 4.11. The submission summarised at (iv) above is also accurate. The Bradford & Bingley unaudited Interim Financial Report for the 6 months ended 30 June 2008 recorded shareholder equity, at 30 June 2008, of £1.14 billion and proforma shareholder equity of £1.54 billion, which included the £401 million of new capital raised through the rights issue in August 2008. Bradford & Bingley Group shareholder equity at the end of the third quarter 2008 was lower at £1.37 billion, as a result of losses and net changes to reserves over the quarter of around £170 million. In reaching my Section 3 determinations, I have fully taken into account this shareholder equity.

- 4.12. In response to the submissions summarised at (v) and (vi) above, I should make it clear that it is not my role to express a view on whether statements made or actions taken or not taken by Bradford & Bingley or its directors or by the FSA, the Bank of England or HMT were correct, adequate or appropriate. My role, as set out in Sections 1 and 2 of my Assessment Notice, is to determine the amount of any compensation payable by HMT under the Scheme by establishing the value of the shares and subscription rights immediately before the transfer time. In doing so I have considered all available evidence as to Bradford & Bingley's financial standing, including its capital and liquidity position, immediately before the transfer time.
- 4.13. In the final two sentences of paragraph 3.12 of my Assessment Notice I stated that: "The Bank of England notified Bradford & Bingley that, if the covered bonds did become ineligible, it would require Bradford & Bingley to repay SLS funding to the extent that collateral had been provided in the form of such covered bonds. Of the £7.4 billion of collateral held by the Bank of England, £2.3 billion was in the form of Bradford & Bingley covered bonds." (I should add to this statement that if the covered bonds had been downgraded by Fitch it would have been open to Bradford & Bingley to tender any available eligible collateral to the Bank of England in substitution for the covered bonds previously tendered as collateral. To the extent that the Bank of England accepted that collateral, Bradford & Bingley would not have needed to repay the SLS funding.) It has been submitted that my Assessment Notice did not say over what period and on what terms any such repayment might have been required.

- 4.14. It is correct that my Assessment Notice did not address the timing and terms of any actual Bank of England demand for the repayment of SLS funding. This is because in the event no such demand was made prior to the transfer time. Paragraphs 5.6 to 5.11 of my Assessment Notice did, however, address the timing and terms of the withdrawal of SLS funding in the context of the application of the Statutory Assumptions. In paragraph 5.6 I also noted that if Bradford & Bingley had entered administration (which is what I determined in Section 3 of my Assessment Notice would have happened in the absence of the Transfer Order) the administration would itself have led to the withdrawal of SLS funding giving a similar impact to that set out at paragraphs 5.7 to 5.11 of my Assessment Notice. For completeness, I should also mention that, once effective, the variation of Bradford & Bingley's permission under Part IV of the Financial Services and Markets Act 2000 pursuant to the FSA's First Supervisory Notice to Bradford & Bingley on 27 September 2008 would also have led to the withdrawal of SLS funding over a similar period and on similar terms.
- 4.15. It has also been submitted that the covered bonds were not in fact downgraded and the Bank of England had not actually demanded the repayment of SLS funding, but only that the covered bonds required restructuring in order to remain eligible for tendering as collateral for the SLS, and that once restructured the covered bonds would again have been eligible as collateral within the SLS. It is submitted that the alternative of depriving Bradford & Bingley of that opportunity and permitting it to fail is not realistic and that the determination I make at paragraph 5.11 of my Assessment Notice (for the purpose of establishing the opening administration balance

sheet) that the withdrawal of SLS funding would have resulted in a loss of approximately £0.8 billion is therefore unjustified.

- 4.16. It is correct that the covered bonds were not downgraded by Fitch in the week leading up to the transfer time and the Bank of England did not demand repayment by Bradford & Bingley of SLS funding. Nor did it demand that the covered bonds be restructured. The Bank of England's position was that it was concerned about the possible downgrade of the covered bonds given the time frame required for the restructuring that Bradford & Bingley understood would meet Fitch's concerns and that if the covered bonds were downgraded Bradford & Bingley would have to remove the covered bonds it had already used as collateral in accessing the SLS. The covered bond restructuring options open to Bradford & Bingley, in particular a conversion of the covered bonds from "bullet" repayment (i.e. repayment of covered bond principal only at maturity) to a "pass through" profile (i.e. principal repayments from mortgages are used to repay the covered bonds as and when these mortgage repayments are received) would have taken some weeks to implement. I concluded that Bradford & Bingley would not have been able to restructure the covered bonds (or to take any other steps to manufacture eligible collateral for the SLS) sufficiently quickly to enable it to seek to obtain further SLS funding to address its liquidity issues and so to be able to continue as a going concern.
- 4.17. In relation to the submission that the alternative of depriving Bradford & Bingley of the opportunity to restructure its covered bonds and permitting it to fail was unrealistic, it is important to recognise that in valuing the shares and subscription rights immediately before the transfer time I must have regard to the actual

position at that time of Bradford & Bingley as well as the Statutory Assumptions. I determined in Section 3 of my Assessment Notice that, absent significant support from HMT (which the Statutory Assumptions require me to exclude), immediately before the transfer time there was no realistic alternative available to Bradford & Bingley other than administration. As I explained in paragraph 5.6 of my Assessment Notice, if Bradford & Bingley had entered administration that would have led to the withdrawal of SLS funding. Moreover, the Statutory Assumptions require me to assume that all financial assistance provided by the Bank of England had been withdrawn. This would include all SLS funding provided to Bradford & Bingley.

- 4.18. At paragraph 3.12 of my Assessment Notice I stated that Bradford & Bingley had informed the Bank of England on Monday 22 September 2008 that it would be seeking to access a further £700 million from the SLS that week. It is submitted that the evidence of Mr Richard Pym to the Treasury Select Committee on 18 November 2008 in relation to the outflow of funds during that week demonstrates that in fact only £328 million, not the £700 million originally anticipated, of short term liquidity was required.
- 4.19. I have read the transcript of the evidence of Mr Pym and Mr Rod Kent to the Treasury Select Committee on 18 November 2008 and note Mr Pym's reference to an outflow of funds from Wednesday 24 September 2008 to Saturday 27 September 2008 of a total of £328 million. I have checked the figures given by Mr Pym against the available evidence and confirmed that they correspond with the branch and online activity figures. These figures do not include outflow figures for 22, 23 or 28 September 2008, activity through the

Isle of Man subsidiary or wholesale funding maturities. The actual activity for the weekend of 27 and 28 September 2008 would have resulted in cash outflows of over £290 million over the settlement cycle of the following week. In any event, it is an oversimplification to equate the £328 million deposit outflow figure with Bradford & Bingley's liquidity requirements. For example, Bradford & Bingley's liquidity requirements were driven in part by forthcoming significant wholesale funding maturities as well as projected retail deposit outflows. As I have said, I am satisfied having reviewed all the available evidence that, if there had been no Transfer Order, immediately before the transfer time Bradford & Bingley's liquidity position would have prevented it from continuing as a going concern.

4.20. In the final sentence of paragraph 3.13 of my Assessment Notice I stated: "In addition, Fitch downgraded Bradford & Bingley's rating on 23 September 2008 and stated they expected "further deterioration in the bank's profitability and asset quality as the UK economy and mortgage market continue to worsen"." It has been submitted that my reference to the Fitch downgrade on 23 September 2008 makes no distinction between the rating of Bradford & Bingley and that of its covered bonds. For the avoidance of any doubt I confirm that the Fitch downgrade on 23 September 2008 to which I referred in the final sentence of paragraph 3.13 of my Assessment Notice was (as indicated in footnote 14 of my Assessment Notice) a downgrade in the rating of Bradford & Bingley itself (to BBB-) and not a downgrade of the covered bonds.

4.21. In the fifth sentence of paragraph 3.16 of my Assessment Notice I referred to the Board's consideration of the "potential downgrade". I

have been asked to confirm that the covered bonds were not in fact downgraded by Fitch after they were placed on negative watch (as referred to in paragraph 3.12 of my Assessment Notice) and prior to the Transfer Order. I confirm that that is correct.

4.22. In Section 3 of my Assessment Notice I determined that, in the absence of the Transfer Order, Bradford & Bingley would not have been able to obtain an adequate source of necessary liquidity to replace the liquidity that had been consumed by cash outflows. This determination has been challenged. In summary the submissions in support of this challenge are as follows:

- (i) Bradford & Bingley had cash, Treasury bills and loans to other banks approaching £3 billion after adjusting for the withdrawal of SLS funding (see Figure 5 of my Assessment Notice). It would not have needed other funds prior to restructuring the covered bond programme and removing the basis for the potential downgrade of the covered bond programme by Fitch.
- (ii) The £328 million of short term liquidity required would have been available from third party institutions or from a further drawdown from the Barclays Senior Facility (described in paragraphs 5.25 and 5.26 of my Assessment Notice).
- (iii) The institutions and larger shareholders that had supported the recent Bradford & Bingley rights issue, and were in danger of losing all of that investment, could be expected to provide support (with security) to protect the investment they had just made had they been approached, which it is said they were not.
- (iv) It is inconceivable that nowhere in the world could finance be found to cover short term issues. Whilst many UK banks found

it convenient to obtain temporary funding from the Bank of England, other UK banks did, at the time, source funds from the Middle East, the Far East, China and Australasia. The £3 billion of liquid capital could have been supplemented if the search had been deemed necessary.

- 4.23. In relation to the submission summarised at (i) above, it is correct that Figure 5 of my Assessment Notice referred to £3 billion of cash, Treasury bills and loans to banks. However, not all of this can properly be characterised as liquidity available to Bradford & Bingley. In particular loans to other banks cannot always be redeemed quickly to generate funds. In fact, as set out at paragraph 4.8 above, as at 4pm on 28 September 2008 Bradford & Bingley was forecasting core liquidity to have fallen to around £2.1 billion by close of business on 29 September 2008. This liquidity position represented excess liquidity over Bradford & Bingley's minimum liquidity requirement of around £1 billion (on the most favourable of the bases reported by Bradford & Bingley to the FSA), a level which was insufficient to cover projected retail outflows and wholesale funding maturities in that week without breaching that requirement.
- 4.24. As I explain in paragraph 4.16 above, Bradford & Bingley would not have been able to restructure the covered bonds (or to take any others steps to manufacture eligible collateral for the SLS) sufficiently quickly to enable it to seek to obtain further SLS funding to address its liquidity issues. As I recorded in paragraph 3.16 of my Assessment Notice, the Board considered that Bradford & Bingley was likely to have unacceptably low levels of liquidity within a matter of days, possibly as early as 29 September 2008. I agree with this assessment.

- 4.25. The submission summarised at (ii) refers to £328 million being the short term liquidity requirement of Bradford & Bingley. This is inaccurate. The £328 million figure is the total of cash outflow of funds for the period 24 to 27 September 2008 referred to in Mr Pym's evidence to the Treasury Select Committee. It does not constitute Bradford & Bingley's "short term liquidity requirement" (see paragraph 4.19 above). In any event, as I explained in paragraph 3.20 of my Assessment Notice, I consider that Bradford & Bingley would not have been able to obtain an adequate source of liquidity sufficient to continue as a going concern. In relation to the Barclays Senior Facility specifically, this was not a potential source of further liquidity as it was already fully drawn.
- 4.26. In relation to the submission summarised at (iii) above, HMT and the FSA did engage in discussions with various significant institutional investors in Bradford & Bingley and a number of banks to gauge their appetite for extending support to Bradford & Bingley or assisting with a private sector solution. In the event it became apparent that any such support or solution would require the commitment of significant financial assistance from HMT or the Bank of England.
- 4.27. As to submission (iv), it is the case that a number of the UK banks were successful in attracting investment from overseas to strengthen their capital bases and this had also supported their liquidity positions. Although Bradford & Bingley had been able to access limited European Central Bank funding through a committed repo arrangement with a UK bank with eurozone subsidiaries, no further funding of this nature was available to Bradford & Bingley. At the transfer time Bradford & Bingley was not in discussions with any

other potential overseas source of liquidity and I have seen no evidence that any such source of liquidity would have been available. As I describe at paragraph 3.7 of my Assessment Notice, the almost total closure of the wholesale lending market meant that the principal source of liquidity to the banking system was the Bank of England.

- 4.28. It has been submitted that Bradford & Bingley could have borrowed funds from the Bank of England under the “lender of last resort facility” to enable it to continue as a going concern whilst it restructured its covered bonds so that they remained eligible for presentation within the SLS.
- 4.29. It is correct that the Bank of England has the power to go beyond the facilities and operations set out in the SMF Documentation and to provide support to an institution as “lender of last resort”. Such assistance would be discretionary and could in principle be provided in many different ways, at terms and against collateral determined in the individual case. However, in my view such support would not constitute “ordinary market assistance” for the purpose of the Act (see Section 3 above) and therefore the Statutory Assumptions require me to assume that this support would not have been available to Bradford & Bingley. Further, the Bank of England has confirmed to me that it would not have been willing to provide “lender of last resort” support to Bradford & Bingley.
- 4.30. It has been submitted that there were “a number of options” that should have been put in place to avoid a transfer to public ownership or an administration (such as a Government statement guaranteeing deposits to prevent a run on the bank) and that these

options were not sufficiently explored by the Board or the Government.

4.31. Again I emphasise that it is not my role to express a view on whether actions taken or not taken by Bradford & Bingley or its directors or by the Government were correct, adequate or appropriate. My role is to determine the amount of any compensation payable by HMT under the Scheme by establishing the value of the shares and subscription rights immediately before the transfer time. In doing so I have considered carefully what options might have realistically been available to Bradford & Bingley, immediately before the transfer time, as an alternative to administration. I have concluded, taking into account the Statutory Assumptions, that there were none.

4.32. On my website ([www.bandbvaluer.org.uk](http://www.bandbvaluer.org.uk)) I have a section covering Frequently Asked Questions. Question 14 is as follows:

*“14. Why did RBS and HBOS receive emergency assistance from the Bank of England and not Bradford & Bingley?”*

*According to the Bank of England, it is a core principle that when the central bank gives its assistance, it must only be done where absolutely necessary and it should always be a bridge to a solution of the underlying problem of the bank.*

*For both RBS and HBOS, short term liquidity measures allowed them to bridge through to the Government recapitalisation scheme and the merger with LloydsTSB respectively. In Bradford & Bingley’s case, no such longer term measure was available, except to enact the Transfer order.”*

- 4.33. It has been submitted that my response to question 14 is inconsistent with my Assessment Notice because Bradford & Bingley had at most only a short term liquidity issue and was in exactly the same situation as RBS and Lloyds. Reliance is placed in this regard on Bradford & Bingley's recent financial performance.
- 4.34. I do not accept that there is any inconsistency between my response to question 14 and my Assessment Notice. The substance of the complaint appears to be that the shareholders of Bradford & Bingley have been treated unfairly compared to the shareholders of RBS and HBOS. That complaint has been explicitly made in a number of submissions. I do not express any view on this as it is not relevant to my determination of any compensation under the terms of the Scheme.

# 5 Sale of deposit business and branch network

- 5.1. Article 16 of the Transfer Order effected the transfer of all rights and liabilities in respect of retail deposits with Bradford & Bingley and of Bradford & Bingley's branch network to Abbey National plc ("Abbey") immediately after the transfer time.
- 5.2. The payments to be made and the liabilities incurred in respect of this transfer are set out in articles 28 to 30 of the Transfer Order. In broad summary (and omitting a number of matters and details set out in the Transfer Order):
- (i) The Financial Services Compensation Scheme Limited (the "FSCS") was liable to pay to Abbey an amount equal to the amount that could have been claimed by depositors under the compensation scheme administered by the FSCS in respect of retail deposits with Bradford & Bingley immediately before the transfer time.
  - (ii) HMT was liable to pay to Abbey an amount equal to the aggregate amount of the liabilities transferred to Abbey less the amount described at (i) above and less £612 million.
  - (iii) HMT was to ensure that Bradford & Bingley obtained the benefit of the reduction of £612 million referred to at (ii) above.
  - (iv) Bradford & Bingley was liable to the FSCS in respect of the liabilities of the FSCS and HMT described at (i) and (ii) above (with the FSCS accounting to HMT in respect of money

received from Bradford & Bingley that was attributable to the liability described at (ii) above).

- 5.3. It has been submitted that in valuing the shares and subscription rights immediately before the transfer time, I have failed to take into account that the sale of Bradford & Bingley's deposit business and branch network to Abbey destroyed Bradford & Bingley as a viable business and that Bradford & Bingley was the only bank that was treated in this way.
- 5.4. It is correct that in valuing the shares and subscription rights immediately before the transfer time I have not taken into account the transfer to Abbey effected by article 16 of the Transfer Order described above. This is because I am required under the Compensation Scheme Order to value the shares and subscription rights immediately before the transfer time (see paragraphs 2.1 and 2.2 of my Assessment Notice). At the relevant valuation point (i.e. immediately before the transfer time) the transfer to Abbey had not yet occurred. Article 16 of the Transfer Order expressly provides that the transfer to Abbey occurred immediately after the transfer time. It follows that the impact of the transfer to Abbey on Bradford & Bingley and whether the transfer to Abbey constituted different treatment to the treatment of other banks are irrelevant to my determination of any compensation.
- 5.5. It has been submitted that I wrongly failed to give any value to shareholders in respect of the sale of the Bradford & Bingley deposit business and branch network to Abbey, whereas in fact the sale realised proceeds of £612 million and this money was actually payable to Bradford & Bingley at the relevant time for the purposes of my Assessment Notice.

- 5.6. For the reasons given at paragraph 5.4 above, I believe that I was correct in not taking into account the article 16 transfer to Abbey. (For completeness, I should also note that the Bradford & Bingley financial statements for the year ended 31 December 2008 record that the gain on the transfer to Abbey was £216.3 million.)
- 5.7. It has been submitted that I was wrong not to take account in my valuation of the £612 million figure (see paragraph 5.2 above) because the funds provided by HMT and/or the FSCS were in fact provided to Abbey not to Bradford & Bingley. I understand that the point being made here is that providing funds to an entity other than Bradford & Bingley cannot be “financial assistance” under section 5(4)(b) of the Act. I address this point at paragraph 5.14 below. In any event, the reasons why I have taken no account in my valuation of the gain achieved on the transfer to Abbey are as set out at paragraph 5.4 above.
- 5.8. It has been submitted that I have failed to take into account that the deposit business and branch network were transferred to Abbey at an undervalue and that Abbey’s owner, Santander, is extremely pleased at the cheap acquisition it made and has publicly boasted of the significant profits generated by that acquisition.
- 5.9. Again, for the reasons given at paragraph 5.4 above, I have not taken into account the article 16 transfer to Abbey and therefore the question of whether or not the transfer was made at an undervalue does not arise for the purpose of my valuation and determination of any compensation.

- 5.10. It has been submitted that Bradford & Bingley's deposit business and branch network were part of Bradford & Bingley at the transfer time and so should be included in my valuation.
- 5.11. As will be clear from what I have said above, I agree that the deposit business and branch network had not yet been transferred to Abbey at the relevant time for my valuation of shares and subscription rights (i.e. immediately before the transfer time). In light of my Section 3 determinations (see paragraph 4.1 above), in my Assessment Notice I consider how an administrator of Bradford & Bingley would have dealt with the deposit business and branch network. I did so on the assumption that there had been no transfer to Abbey. In paragraphs 5.37 to 5.40 of my Assessment Notice I explain that I have determined (taking into account the Statutory Assumptions) that an administrator of Bradford & Bingley would not have been able to dispose of the retail deposits and branch network and would therefore have incurred costs of closing the branch network of at least £30 million.
- 5.12. In paragraph 5.39 of my Assessment Notice I state as follows:
- "I have considered whether a similar sale could have been achieved within an administration process. As at 29 September 2008, the FSCS did not have the resources to fund a transfer of the deposit book without recourse to additional HMT funding or the ability to raise the resources through a levy. Through my discussions with the FSCS I understand that if Bradford & Bingley had entered administration, then it might have been possible to accelerate changes that subsequently took place to allow the FSCS to fund such a transfer in the interests of financial stability. However, given the level of market disruption and general shortage of liquidity and*

*that the FSCS maximum annual levy capacity was approximately £4 billion, the only credible sources of funding for the FSCS would have been either HMT or the Bank of England. I am required to assess compensation under the Statutory Assumption that no financial assistance would in future be provided by the Bank of England or HMT to Bradford & Bingley (apart from ordinary market assistance offered by the Bank of England subject to its usual terms). I have determined that funding the transfer of the deposit book would constitute financial assistance (and would not be ordinary market assistance). I have therefore concluded that the FSCS would not have funded any transfer of the deposit book and that the transfer would not have occurred.”*

5.13. My reasoning in paragraph 5.39 of my Assessment Notice has been challenged on the basis that:

- (i) section 5(4)(b) of the Act refers only to financial assistance to the “deposit taker in question” and the Act does not require me to assume that funding from HMT would not be available to a purchaser of Bradford & Bingley’s deposit business and branch network; and
- (ii) the Act does not require me to exclude monies actually owing to Bradford & Bingley at the relevant time for my valuation.

5.14. I am not persuaded by these arguments. In relation to the first argument, I consider that HMT or the Bank of England putting the FSCS in funds to enable it to fund a transfer of Bradford & Bingley’s deposit business and branch network would in substance amount to the provision of financial assistance to Bradford & Bingley. It is relevant to note in this regard that “financial assistance” in relation to

any person is expressed in section 15 of the Act to include assistance provided (by way of loan, guarantee or indemnity or by way of any transaction which equates in substance to a transaction for lending money at interest) “indirectly to or otherwise for the benefit of the person ...”.

- 5.15. In relation to the second argument, I agree that I am not required in carrying out my valuation to ignore any monies actually owing to Bradford & Bingley at the relevant time for my valuation. The relevant time for my valuation is immediately before the transfer time. For the reasons set out above, at that time no monies were owing to Bradford & Bingley in respect of the article 16 transfer to Abbey. The article 16 transfer to Abbey was only effected after the transfer time.

# 6 Possible bids for Bradford & Bingley

6.1. Paragraphs 3.23 and 3.24 of my Assessment Notice state that:

*“3.23 I have also considered whether a sale of Bradford & Bingley to a larger institution would have allowed Bradford & Bingley to continue to operate by drawing on the financial resources (i.e. capital and liquidity) of a larger group. Bradford & Bingley had sought such a strategic solution from early 2008 and the Board and its advisers had explored many options.*

*3.24 Bradford & Bingley, its advisers Goldman Sachs and the FSA had spoken to potential acquirers over several months without securing an offer that would provide a suitable private sector solution. On 21 September 2008, Morgan Stanley had been engaged by HMT to assess, among other matters, whether there was any possibility of a private sector solution. By the middle of that week Morgan Stanley and HMT had concluded that the likelihood of a private sector solution during such a period of market disruption was highly unlikely in light of the fact that most potential acquirers were also affected by the global financial crisis and were focussed on maintaining their own liquidity and capital resources. The efforts that were made to find a private sector solution demonstrate that such a course of action would not have been possible without significant support from HMT.”*

- 6.2. Various submissions have been made in relation to these paragraphs. It has been submitted that I have given no details of the efforts that were made to find a private sector solution or of the investigations that I have undertaken on this topic. It has been submitted that I have not explained whether there were any other options considered by HMT or any other parties in addition to the transfer of the deposit business and branch network to Abbey and why they were not pursued.
- 6.3. As I explain above, it is not my role to express a view on whether actions taken or not taken by Bradford & Bingley or its directors or by the FSA or HMT were correct, adequate or appropriate. My role, as set out in Sections 1 and 2 of my Assessment Notice, is to determine the amount of any compensation payable by HMT under the Scheme by establishing the value of the shares and subscription rights immediately before the transfer time.
- 6.4. In addition to the explanations I gave in paragraphs 3.23 and 3.24 of my Assessment Notice as to the attempts made to find a private sector solution, I confirmed at paragraph 4.6 of my Assessment Notice that there were no offers at the transfer time for all or part of the equity of Bradford & Bingley.
- 6.5. Further to my description of the attempts to find a private sector solution set out in paragraphs 3.23 and 3.24 of my Assessment Notice, over the weekend of 27 and 28 September 2008, HMT, with the support of Morgan Stanley, explored private sector solutions and alternatives requiring public support with a number of parties. The steps taken included exploring the possibility of a bid for Bradford & Bingley by a consortium of banks and an auction of parts of Bradford & Bingley's balance sheet. The auction resulted in the transfer of the

deposit business and branch network to Abbey discussed at Section 5 above.

- 6.6. I am satisfied that I have properly investigated the position and that immediately before the transfer time there was no potential private sector solution available to Bradford & Bingley that did not require significant financial support from HMT (as was the case in relation to the transfer of the deposit business and branch network to Abbey). In my view the Statutory Assumptions preclude me from considering options that would have required significant financial support from HMT (other than “ordinary market assistance”).
- 6.7. It has been submitted that my valuation of the shares and subscription rights should take into account the indicative valuations of Bradford & Bingley that, it is said, can be obtained from the investments in Bradford & Bingley that were proposed by Texas Pacific Group and Resolution in June 2008.
- 6.8. I confirm that I have considered carefully the relevance to my assessment of any compensation of the proposals by Texas Pacific Group and Resolution. In my view the significant deterioration in market conditions from the time that such proposals were made up until my valuation point, immediately before the transfer time, as well as the other matters referred to in Section 3 of my Assessment Notice mean that I cannot place reliance on any aspects of these proposals. For completeness, I should also note that Texas Pacific Group withdrew its proposal on the basis of a downgrade in Bradford & Bingley’s rating and that the Resolution expression of interest in June 2008 did not progress to the stage where it was given access to the books and records of Bradford & Bingley.

6.9. It has been submitted that I have overlooked the possibility of a bid for Bradford & Bingley by Resolution or another party. I have not seen any evidence to support a view that, immediately before the transfer time, it was likely that any such bid would be made and I do not think there is any proper basis on which to value the shares or subscription rights by reference to such a bid.

# 7 Recent financial performance

- 7.1. A number of submissions have been made by reference to the financial performance of Bradford & Bingley since the transfer time. For example, it has been submitted that I should take into account the Bradford & Bingley unaudited Interim Financial Report for the 6 months ended 30 June 2010, which among other things reported that Group profit before tax for the first half of 2010 was £896 million (or £79.4 million when adjusted to exclude two significant one-off items<sup>3</sup>). It is submitted that these results show that there was material value in Bradford & Bingley at the transfer time.
- 7.2. I do not accept this submission. It is important to recognise that (as the unaudited Interim Financial Report for the 6 months ended 30 June 2010 itself makes clear) since the transfer time Bradford & Bingley has benefitted from significant financial assistance from HMT which the Statutory Assumptions require me to exclude.
- 7.3. The most significant form of financial assistance that Bradford & Bingley has benefitted from is the interest-free Statutory Debt provided by the FSCS. This Statutory Debt was initially provided by virtue of a loan of £18.4 billion to the FSCS from HMT and was required to replace the deposit balances that had been sold to Abbey. In addition HMT provided guarantees and an interest-bearing

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<sup>3</sup> The Interim Financial Report for the 6 months ended 30 June 2010 records that adjustments were made to profit before tax to reflect the following non-recurring items: the one-off gain on the repurchase of subordinated liabilities and the discounting arising due to the deferral of coupons on subordinated liabilities.

working capital facility, £8.6 billion of which had been drawn down as at 30 June 2010.

- 7.4. In any event, my role is to determine the amount of any compensation payable by HMT under the Scheme by establishing the value of the shares and subscription rights immediately before the transfer time. The Bradford & Bingley unaudited Interim Financial Report for the 6 months ended 30 June 2010 of course reflects events that occurred after the transfer time and which are irrelevant to my valuation.
- 7.5. It is also submitted that I should take into account the amount of shareholder equity reported in each of Bradford & Bingley's financial statements since the transfer time culminating in shareholder equity of £2.05 billion reported in the Bradford & Bingley unaudited Interim Financial Report for the 6 months ended 30 June 2010. It is said that these shareholder equity figures are equivalent to a value of between 76 pence and 143 pence per share, which value (it is said) the Treasury Solicitor, acting on behalf of HMT, has acquired for nil consideration. It is submitted that these figures should form the basis for compensation. Leaving aside the question of whether this valuation approach would otherwise be appropriate, I disagree with this submission for the reasons set out earlier in this Section 7.
- 7.6. Similarly, I am aware of the evidence given at the Treasury Select Committee hearing on 27 January 2011 to the effect that the nationalisation of Bradford & Bingley would result in a substantial profit to the Government. For the same reasons as are stated earlier in this Section 7 I do not consider this evidence to be relevant to my assessment of any compensation.

# 8 My approach to compensation

- 8.1. In Section 4 of my Assessment Notice I outlined the approach that I have taken to assess the value of the shares and the subscription rights immediately before the transfer time. The basis of value is not determined by statute. I determined that economic value is the appropriate basis of value and that there would only be value to shareholders or holders of subscription rights if they would have received a distribution from administration.
- 8.2. It has been submitted that since Bradford & Bingley did not in fact go into administration I was wrong to determine (as I do in Section 4 of my Assessment Notice) that compensation would only be payable if shareholders would have received a distribution at the end of the administration that I determined in Section 3 of my Assessment Notice would, absent the Transfer Order, have commenced before the transfer time or shortly thereafter. It is submitted that my assessment of compensation should instead be based on “what actually did happen and could have been achieved in public ownership”.
- 8.3. I do not accept this submission as it is inconsistent with the Scheme which requires me to value the shares and subscription rights immediately before the transfer time and to apply the Statutory Assumptions in doing so. The Statutory Assumptions do not permit me to value the shares on the basis that Bradford & Bingley is now in public ownership.
- 8.4. It has been submitted that, based on shareholder equity of £1.14 billion at 30 June 2008 supplemented by the £401 million raised

thereafter in the rights issue, Bradford & Bingley's "book value" was around £1 per share at the transfer time and that this should provide the basis for my assessment. Leaving aside the correct calculation of shareholder equity at the transfer time, in the light of my Section 3 determinations (see paragraph 4.1 above), I do not accept that a book value approach (which would be prepared on a going concern basis) is appropriate here. I have determined that if there had been no Transfer Order an administration order would have been made in respect of Bradford & Bingley either before the transfer time or shortly thereafter. In these circumstances I consider that the appropriate basis of valuation is a basis that considers the economic value of the shares (or subscription rights) represented by the value immediately before the transfer time of the cash flows that a shareholder would have received.

- 8.5. It has been submitted that I should interpret the words "immediately before the transfer time" in paragraphs 3 and 4 of the Schedule to the Compensation Scheme Order flexibly and that I should not adopt a valuation point on the morning of 29 September 2008 just before the Transfer Order came into effect.
- 8.6. I do not accept this submission and can see no basis on which I should ignore the events that occurred over the weekend of 27 and 28 September 2008 in my valuation. I consider that the words "immediately before" in paragraphs 3 and 4 of the Schedule to the Compensation Scheme Order require me to adopt a valuation point on the morning of 29 September 2008 just before the Transfer Order came into effect.

- 8.7. It has been submitted that I was wrong to reject the two other valuation bases, market value and fair value, that I discussed at paragraphs 4.3 to 4.7 of my Assessment Notice.
- 8.8. As I explained in paragraph 4.1 of my Assessment Notice the basis of value is not specified by statute. I have therefore had to determine the appropriate basis of value. For the reasons I give in paragraphs 4.3 to 4.7 of my Assessment Notice, I do not consider market value or fair value to be an appropriate basis of value.
- 8.9. It has also been submitted that the closing share price of 20 pence per share on Friday 26 September 2008 is relevant to my assessment and represents the minimum appropriate compensation that should be payable by HMT and that in fact that price was artificially low because it was fuelled by pessimism and fear and therefore did not reflect Bradford & Bingley's true value. It is submitted that I am wrong to reject this in paragraph 4.5 of my Assessment Notice and wrong in rejecting market value as a basis of value.
- 8.10. I explained in paragraph 4.5 of my Assessment Notice that given my conclusions on administration in Section 3 of my Assessment Notice, including my conclusion that the ordinary shares would have been suspended from trading before the transfer time, I consider that the closing share price on 26 September 2008 does not assist me in determining the value of the shares. In addition, I consider that simply adopting the closing share price on 26 September 2008 would not allow me to give effect to the Statutory Assumptions or to reflect the actual position of Bradford & Bingley immediately before the transfer time as it did not reflect events over the weekend of 27 and 28 September 2008.

# 9 Expected outcome of administration

## The administrator's opening balance sheet

- 9.1. I set out in Figure 5 of my Assessment Notice the balance sheet that I consider an administrator would have had control over at the start of the administration. I discuss this at paragraphs 5.6 to 5.13 of my Assessment Notice.
- 9.2. It is submitted that the adjustments I have made to produce the administrator's opening balance sheet set out at Figure 5 of my Assessment Notice have reduced the assets of Bradford & Bingley by £10 billion (from £52 billion to £42 billion) and have reduced shareholder equity by £1.1 billion. It has also been submitted that no detail has been given relating to the adjustments I have made to produce the administrator's opening balance sheet and that this detail is required to enable interested parties to consider whether the adjustments are appropriate.
- 9.3. It is correct that the total asset value in my administrator's opening balance sheet as at 29 September 2008 in Figure 5 of my Assessment Notice is £10 billion lower than the £52 billion asset value set out in the 30 June 2008 Group summary balance sheet at Figure 2 of my Assessment Notice. It is also correct that the shareholder equity value in Figure 5 of my Assessment Notice is approximately £1.1 billion less than the proforma shareholder equity of £1.54 billion recorded in the Bradford & Bingley unaudited Interim Financial Report for the 6 months ended 30 June 2008 (see

paragraph 4.11 above). I consider that the figures contained in Figure 5 of my Assessment Notice are correct for the reasons given in paragraphs 5.6 to 5.13 of my Assessment Notice and in paragraphs 9.4 to 9.6 below.

- 9.4. As an administrator is appointed to consider realisations on an entity by entity basis it is only appropriate to consider assets over which the administrator would have direct control. The assets and liabilities recorded on the administrator's opening balance sheet would therefore be different from those recorded in a Group balance sheet. This (together with changes since 30 June 2008 and the accounting policy adjustment which I describe in paragraph 9.5 below) explains the reduction in shareholder equity. Figure 5 of my Assessment Notice is an aggregation of the material assets and liabilities of the main operating subsidiaries of the Group, i.e. Bradford & Bingley plc, Mortgage Express and Bradford & Bingley International Limited, that an administrator would have had control over. The balance sheet set out at Figure 2 of my Assessment Notice reflects the consolidated assets and liabilities as reported in the published accounts of the Group. The assets reported on the Group balance sheet include mortgages which, although subject to secured funding arrangements (as defined in paragraph 3.5 of my Assessment Notice), are included in the Group balance sheet because certain risks and rewards of ownership are retained. An administrator would have been restricted from disposing of those mortgage assets which were subject to the secured funding arrangements and these were therefore not reflected in Figure 5 of my Assessment Notice. Figure 1 sets out a reconciliation between Group shareholder equity as at 30 June 2008 and that recorded in the administrator's opening balance sheet.

**Figure 1: Reconciliation between Group shareholder equity and the administrator’s opening balance sheet**

<b>£ in millions</b>	
Group shareholder equity - 30 June 08	1,144.4
Equity raised through rights issue	400.5
<b>Proforma shareholder equity – 30 June 08</b>	<b>1,544.9</b>
Losses over the 3 months to 29 Sep 08	(152.8)
Net movements in reserves	(20.9)
Movement in Group shareholder equity over the 3 months to 29 Sep 08	226.8
<b>Group shareholder equity – 29 Sep 08</b>	<b>1,371.2</b>
Accounting policy adjustment	(262.6)
Withdrawal of SLS	(750.0)
Adjustments to Group shareholder equity	(1,012.6)
<b>Administrator’s opening balance sheet equity – 29 Sep 08</b>	<b>358.6</b>

Source: Interim Financial Report, management accounts, PwC analysis

- 9.5. The “Accounting policy adjustment” referred to in Figure 1 reflects the differing accounting treatment applied within the consolidated Group accounts to that applied by Bradford & Bingley at an entity level. Where Bradford & Bingley held securities issued by special purpose vehicles (which were consolidated in the Group balance sheet) as part of the secured funding arrangements, these were recorded at their market value and an adjustment made to equity through the available for sale reserve. The structure is eliminated on consolidation and the Group accounts record the underlying mortgages at nominal value net of recognised impairments.

- 9.6. The “Withdrawal of SLS” referred to in Figure 1 relates to the loss of approximately £0.8 billion that I described at paragraphs 5.6 to 5.11 of my Assessment Notice.
- 9.7. It has been submitted that I should not have reduced shareholder equity from £1.2 billion to £0.4 billion in the administrator’s opening balance sheet to reflect the withdrawal of SLS funding, in particular because SLS funding was not in fact withdrawn by the Bank of England prior to the transfer time. I consider that I was correct to do so, for the reasons I give in paragraphs 5.6 to 5.11 of my Assessment Notice and in Section 4 above.

### **The impact of administration on the assets and liabilities of Bradford & Bingley**

- 9.8. At paragraphs 5.14 to 5.40 of my Assessment Notice I assessed the impact of administration on the administrator’s opening equity position. I concluded that, for the reasons that I give in those paragraphs, the shareholder equity of £0.4 billion in the administrator’s opening balance sheet would have been reduced by approximately £1.3 billion to a position of negative shareholder equity of £0.9 billion. This is summarised in Figure 6 of my Assessment Notice.
- 9.9. It is submitted that in arriving at a position of negative equity of £0.9 billion I have made “a series of subjective and highly speculative calculations and assumptions”. It is of course true that it was necessary for me to make a series of calculations and assumptions in order to assess the impact of administration on the administrator’s opening equity position. I am satisfied that my calculations and assumptions were accurate and reasonable. Moreover, as I explained in paragraph 4.16 of my Assessment Notice:

*“In my estimation of the outcome from the administration I make a number of assumptions about the economic environment; the performance of the mortgage portfolios whilst in administration; and the behaviour of the administrator and creditors. I have adopted assumptions which I regard to be reasonable but that are generally favourable to shareholders and collectively result in a favourable scenario.”*

9.10. Paragraph 5.22 of my Assessment Notice stated:

*“I have assumed that, with the exception of holdings of two debt securities, counterparties would have valued the debt securities held as collateral at the book value of the securities. The two holdings of debt securities that I treat as exceptions were holdings in Bradford & Bingley’s covered bond programme that were not publicly traded. Due to the lack of any reference point for their market value, these notes were recorded on the balance sheet at their nominal value of £0.6 billion. Around the transfer time, investment banks indicated that the market value of these notes would likely have been at a discount to nominal value of 15%. Based on this discount, the impact on the balance sheet of Bradford & Bingley on closing out the repo agreements would have been a loss of £0.1 billion.”*

9.11. Paragraph 5.34 of my Assessment Notice stated:

*“In terminating the derivative positions counterparties would have submitted a value for the outstanding position that would take into account the significant costs associated with exiting positions and replacing Bradford & Bingley as the counterparty. This would have resulted in losses for Bradford & Bingley due to derivative balances being valued on the balance sheet on a ‘mid market’ basis in line*

*with accounting standard requirements rather than an exit or replacement basis. I have assessed that the cash received from the asset derivative position would have been £0.7 billion (a loss of £0.1 billion) and the value of the unsecured administration claim of derivative counterparties would have been £0.8 billion (a loss of £0.2 billion). The total impact on Bradford & Bingley would have been a loss of £0.3 billion.”*

- 9.12. In relation to paragraphs 5.22 and 5.34 of my Assessment Notice it has been submitted that I did not consider whether counterparties might have been prepared to take a “haircut” to full valuation in order to exit the positions. It is also submitted that my Assessment Notice contains insufficient detail to assess this.
- 9.13. Paragraph 5.22 of my Assessment Notice relates to debt securities subject to repo agreements. When a counterparty to a repo agreement is in default then the market value (in relation to the debt securities which are the subject of the repo agreement) that applies on termination is determined in accordance with specified procedures. As a result I consider that counterparties would not need to negotiate any haircuts as they would be entitled to exercise their rights to exit the repo in accordance with the terms of the relevant repo agreement.
- 9.14. Paragraph 5.34 of my Assessment Notice relates to derivative positions. In relation to those positions representing an asset of Bradford & Bingley, in paragraph 5.33 of my Assessment Notice I noted that *“where counterparties had a liability to Bradford & Bingley, they may have sought to delay or reduce amounts payable by them.”* Erring in favour of shareholders’ interests in this matter, I took no account of this potential delay in determining the losses

incurred by Bradford & Bingley. As regards those positions representing a liability of Bradford & Bingley, for the reasons given in paragraph 9.15 below, I consider that an administrator would not have sought or reached early settlement with the relevant counterparties.

9.15. The administration scenario that I have modelled indicates an expectation that unsecured creditors would receive full payment and an element of post-administration interest. An administrator with this information would not seek to induce a creditor to settle at undervalue or otherwise compromise its claim, as to do so could expose the administrator to liability. In common with other creditors generally, a creditor seeking early settlement would be advised by the administrator, throughout the course of the administration, of the level of distribution it might expect. Furthermore, accelerated settlement of individual claims would require that sufficient liquid funds were available to meet such claims. I therefore consider that an administrator would not have sought or reached early settlement with any more than an insignificant number and value of non-financial trading counterparties and accordingly I have modelled a scenario in which funds are distributed to unsecured creditors without preference or early settlement.

9.16. Paragraphs 5.25 and 5.26 of my Assessment Notice stated:

*“Bradford & Bingley had borrowed £1.0 billion from Barclays Bank plc under the Barclays Senior Facility and had granted security over £1.7 billion of mortgage assets together with £0.2 billion of liquid assets as collateral in favour of a Security Trustee. The residual interest in the Barclays Senior Facility would thus have been £0.9 billion. An administration of Bradford & Bingley would have triggered*

*an event of default, following which Barclays would have had the right to accelerate the loan made by them in full and trigger enforcement action. Enforcement of security would have meant the disposal of the assets over which security was granted to realise proceeds to repay Barclays.”*

*“I consider that Barclays would have sought repayment of the loan and enforced the security and that the proceeds realised would be sufficient to discharge the Barclays Senior Facility in full. As the markets were depressed at the time, I have assumed that the assets over which security was granted would have been able to be disposed of at a discount of approximately 15%. This is based on discounts being applied in transactions and attempted transactions around that time. I therefore expect the assets subject to security to have been disposed of for around £1.6 billion. This would result in a return of £0.6 billion of assets to Bradford & Bingley and a loss of around £0.3 billion.”*

- 9.17. It has been submitted that taking into account the £200 million of liquid assets held by Barclays as collateral to cover a loan of £1 billion, additional collateral with a market value of £800 million was required and that, assuming a discount of 15%, this required additional collateral with a nominal value of £940 million. Since Barclays had security over £1.7 billion of mortgage assets it is submitted that assets with a nominal value of £760 million would have been returned to Bradford & Bingley (with a market value of £645 million at the 15% discount) and that this would have implied a loss of about £245 million, rather than the £300 million that I calculated in paragraph 5.26 of my Assessment Notice.

9.18. Bradford & Bingley's entry into administration would be an event of default under the terms of the Barclays Senior Facility. I have determined that in such a scenario, Barclays would exercise its right to require that the entire pool of collateral be disposed of by a security trustee (or a receiver) on behalf of the secured creditors, including Barclays. As I explained in paragraph 5.26 of my Assessment Notice, *"I therefore expect the assets subject to security to have been disposed of for around £1.6 billion"*. This is calculated by applying a 15% discount to the mortgage collateral (£1.736 billion), generating cash of around £1.476 billion, which is added to the cash collateral held (£145 million) to meet the outstanding loan (£1 billion) before returning the surplus (£621 million) to the administrator. As a result, following the enforcement of security on behalf of Barclays, Bradford & Bingley would incur a loss of £260 million. In the Assessment Notice I rounded this to a loss of £0.3 billion.

9.19. Paragraphs 5.35 and 5.36 of my Assessment Notice stated:

*"Bradford & Bingley had a defined benefit pension scheme with a deficit (being the difference between the plan assets and plan liabilities) of £11 million. In administration, the trustees of the pension scheme would trigger a winding up of the scheme so that it would become an unsecured creditor on the administration of Bradford & Bingley in the amount of a (Pensions Act) section 75 debt. The impact of the section 75 debt would be to increase the pension plan deficit to at least £0.3 billion."*

*"Based on my assessment, I consider that there would not be any taxable profits during the course of administration and therefore no tax charge. The tax assets on the balance sheet would therefore be*

*of no value, resulting in a reduction in the value of assets of £0.3 billion.”*

- 9.20. It has been submitted that the reductions in the administrator’s opening balance sheet set out in these paragraphs are wrong. The essence of this submission is that, in light of the subsequent trading of Bradford & Bingley, my Section 3 determinations (see paragraph 4.1 above) are wrong. I do not agree with this for the reasons I give in Section 7 above.
- 9.21. It has been submitted that my Assessment Notice failed to take into consideration “the uplift to shareholder funds from the standard mark-to-market approach”. The argument is that the methodology adopted in paragraphs 5.14 to 5.40 of my Assessment Notice applies a haircut to the assets of the company, but fails to consider an uplift to shareholder equity from applying a haircut to the company’s liabilities to “reflect fair valuation in contrast to carrying value” or “mark-to-market rather than carrying value” or “the observed market value of the liabilities”.
- 9.22. In support of this submission it is said that the marking of assets and liabilities to market or fair values is a not uncommon feature in bank reporting. Gains on repurchases of subordinated liabilities at a discount to carrying value are an addition to shareholder funds. It is also said that I should take into account the financial results of Bradford & Bingley from after the transfer time up to the end of June 2010. The published accounts for the years ended 31 December 2008 and 31 December 2009 include notes to the accounts (note 40 in 2008 and note 41 in 2009) that reflect assets and liabilities at “fair” values rather than “carrying” values. It is submitted that “this treatment reflects the market determined valuations”. In 2008 there

is an effective uplift of £5.3 billion to shareholder funds and in 2009 £4.0 billion. It is further submitted that in June 2010 Bradford & Bingley repurchased a substantial quantity of its market traded subordinated debt liabilities at a price which resulted in a profit of £712 million. In addition a further £104 million surplus was realised from the discounting of subordinated liabilities.

- 9.23. The fair value of liabilities has no impact on the value of claims against a company in administration. The full nominal value of claims remains enforceable post insolvency and any discount would only result from a commercial negotiation. The only credible reason why a creditor would agree to accept a discount would be the early receipt of payment. Accelerated settlement of the claim would require that sufficient funds were available. For the reasons set out in paragraph 9.15 above I consider that an administrator would not have sought or reached early settlement with creditors.
- 9.24. I do not accept the submission that the repurchase of subordinated debt by Bradford & Bingley in June 2010 provides evidence of the opportunity to reduce the liabilities of the administration at a discount to nominal value. This type of liability management was undertaken in very different circumstances to that of an administration and would not have been available to an administrator.
- 9.25. At paragraph 5.15 of my Assessment Notice I explain that I have assumed that the head office of Bradford & Bingley would be retained until the end of the administration and then sold at book value. It has been submitted that it is impossible to assess this conclusion without knowing when the head office was last revalued in the accounts. It is further submitted that I should explain why this book value is appropriate to take as a proxy for the realisation

proceeds in 2018. It has also been submitted that I do not explain whether any branches were owned freehold by Bradford & Bingley and, if so, the value which might be realised from these.

- 9.26. I concluded that any realisation proceeds from a disposal of the head office were not material to my assessment. In response to the enquiry about the valuation of the head office in the accounts, I can confirm that the head office was revalued at approximately £12 million in December 2008.
- 9.27. Bradford & Bingley held the freehold of 44 of its 197 branches immediately before the transfer time. I have had access to a breakdown on the most recent market valuations carried out on these properties before their transfer to Abbey which, in aggregate, was £40 million. I have concluded that the realisation proceeds of these properties is not material to my assessment.
- 9.28. At paragraph 5.40 of my Assessment Notice I explained that I estimated the overall impact of closing the branches of Bradford & Bingley would be a cost of at least £30 million based on, among other things, an estimate of lease termination costs. It is submitted that I have had no regard to the possibility of securing purchasers for the residues of at least some leases and of underletting others to mitigate losses. I am asked to reconsider my estimate of lease termination costs on this basis and to set out the assumptions I have made in more detail.
- 9.29. I have considered all of the available evidence relating to lease termination costs and concluded that these costs are not material to my assessment.

- 9.30. It has been submitted that I have not addressed the “brand value” of Bradford & Bingley within my Assessment Notice and that I should provide further guidance as to how this has been considered within my conclusions. It has also been submitted that I have not addressed the insurance brokerage arm of Bradford & Bingley within my conclusions.
- 9.31. Although I accept that brand assets can, in some instances, be sold by an administrator for material value I do not consider this to be the case in the administration scenario that I have modelled. Much of the value of a bank’s brand assets arises through the confidence that customers, particularly depositors, derive. If Bradford & Bingley had entered administration, this would have eroded this confidence and with it the value of the brand assets. I do not consider that an administrator could have realised significant value from a disposal of the brand or related assets. I note that Abbey continued to use the Bradford & Bingley brand for a period of time but ultimately undertook to rebrand Bradford & Bingley. Taking into account these factors, I have concluded that the value of Bradford & Bingley’s brand assets is not material to my assessment.
- 9.32. In relation to the insurance brokerage business, although I believe that an administrator would have been able to dispose of this business I do not believe that such a disposal would have realised material value for creditors. Insurance brokers can be valued by reference to the commission income that they might be expected to generate in the future. In 2007 the insurance brokerage business generated commission income of under £20 million. A disposal by an administrator at any reasonable multiple applied to commission

income would not have generated sufficient value to be material to my assessment.

### **Potential to generate profits over the course of the administration**

9.33. Paragraph 5.41 of my Assessment Notice stated:

*“Having decided that an administrator would continue to manage the customer loans and not seek an immediate sale, I have assessed the extent to which Bradford & Bingley would have been able to generate profits in administration that might allow for the recognition of a surplus over the liabilities. In order to make this assessment I have developed a financial model to forecast the cash flows and associated profits or losses that would have been generated from the run-off of the mortgage book over a ten year administration period.”*

9.34. It has been submitted that I should give the “validation detail” of the model and the choice and sensitivity of the parameters used in the model. I have assumed that this submission refers to the parameters considered in assessing the run-off of customer loans in an administration scenario as set out in Figure 8 of my Assessment Notice.

9.35. The modelling undertaken in relation to the run-off of customer loans was required for me to determine whether sufficient funds would be generated to allow for the repayment of the principal outstanding on all debts (excluding subordinated securities). Having satisfied myself that this was indeed possible I also used the model to assess the extent to which funds generated from the run-off of customer loans would have been sufficient to meet the accrued post-administration interest.

- 9.36. As I state at paragraph 5.42 of my Assessment Notice “Bradford & Bingley would have accrued post-administration interest throughout the administration period at the greater of the applicable statutory rate of 8% per annum as at the transfer time and the rate applicable to the debt apart from administration.” I developed a scenario based on favourable assumptions that would generate around £5 billion to meet post-administration interest. As I state in my Assessment Notice, eligible creditors would have received a yield at a level significantly below the statutory rate.
- 9.37. In undertaking the modelling I prepared sensitivity and scenario analyses to test whether there was any set of conditions under which the run-off of the customer loan portfolio would generate sufficient funds to yield a return to eligible creditors greater than the statutory rate. The modelling parameters allow me to assess the impact that different economic conditions might have on the levels of cash flow that the administration is able to generate. The most sensitive element within this assessment is the level of losses that an administrator might suffer in the event of mortgage customers defaulting on payments.
- 9.38. I have considered an extreme scenario that considers an economic environment with low interest rates resulting in a probability of default of zero across the whole portfolio – i.e. Bradford & Bingley would experience no losses as a result of individuals defaulting on mortgages. Even under this unrealistic scenario creditors would still receive a yield around 5%, a level which remains below the statutory rate. As a result I have concluded that there are no reasonable scenarios under which the administration would generate any residual surplus for distribution to shareholders.

- 9.39. At paragraphs 5.43 and 5.44 of my Assessment Notice I consider the performance of customer loans. It has been submitted that the provisions for impairment losses in the opening balance sheet were made “during the doom and gloom era at the time of nationalisation” and that Bradford & Bingley’s buy to let customers have enjoyed boom times in terms of the strength of rental income over the last few years, leading to much reduced risk of shortfalls on their loans. It has been submitted that therefore a significantly smaller amount is in fact needed to cover the impairment of the mortgage book.
- 9.40. As illustrated in the scenario set out in paragraph 9.38 above, even a zero loss scenario does not generate any residual surplus for distribution to shareholders.
- 9.41. A related submission is that the economic and other parameters that I have used to model the performance of customer loans (as described at paragraph 5.43 and Figure 8 of my Assessment Notice) rely inappropriately on historic information available immediately before the transfer time and should have taken into account the best up to date information now available as to actual performance of customer loans. In this regard it is submitted that the recent recession was unlike other historic recessions and up to date data should therefore be used by me in my modelling.
- 9.42. I do not accept this submission. As I explain above, even a zero loss scenario does not generate any residual surplus for distribution to shareholders. In any event, my role, as set out in Sections 1 and 2 of my Assessment Notice, is to determine the amount of any compensation payable by HMT under the Scheme by establishing the value of the shares and subscription rights immediately before the transfer time. To do so, as I explain at paragraph 4.2 of my

Assessment Notice, I have estimated the cash flows that would arise in an administration, based on information that was available immediately before the transfer time. I would have regard to information that was not known immediately before the transfer time only if it shed light on the position that existed or could reasonably be forecast immediately before the transfer time. I do not consider it appropriate to apply knowledge of the actual performance of either the economy or the resulting performance of Bradford & Bingley's customer loans since the transfer time.

## **Conclusion**

- 9.43. In paragraph 6.1 of my Assessment Notice I concluded that the effective yield for creditors had Bradford & Bingley been placed in administration would have been significantly below the statutory rate of 8% at which post-administration interest would accrue to creditors. I therefore concluded that no residual surplus would be available for distribution to shareholders.
- 9.44. It has been argued that this analysis neglects “that there might have been instituted a suspension of interest to creditors for a period of years until Bradford & Bingley managed to secure the requisite statutory rate of 8%, thereby preventing total loss of shareholdings and allowing the administration to be more effective.”
- 9.45. I assume that this submission suggests that it would have been possible for an administrator either to defer or avoid payment of post-administration interest. Insolvency Act Rule 2.88(7) provides that “any surplus remaining after payment of the debt proved shall, before being applied for any purpose, be applied in paying interest on those debts”. As a result, the creditors' entitlement to interest is a

statutory right. In my assumed administration scenario statutory interest is assumed to accrue and to be paid towards the end of the process, after the repayment of principal in full. I know of no basis on which payment of interest could be deferred for a longer period or could be avoided in its entirety or in part. Further, I do not believe that a delay in the payment of a distribution to creditors which such an approach would cause would be in accordance with the principal purpose of the administration being, as stated in paragraph 4.10 of my Assessment Notice, to achieve a better result for the creditors of Bradford and Bingley as a whole than would be likely from liquidation.

# 10 The scope and structure of the Scheme

- 10.1. A large number of requests for reconsideration were based on submissions that amounted in effect to a challenge to the scope and structure of the Scheme itself. I do not agree with these submissions. My role is to determine whether any compensation is payable under the Scheme. It is not part of my role to assess the appropriateness or otherwise of the Scheme itself.
- 10.2. Some parties submitted that the Scheme is unfair, in particular because it is said that the Statutory Assumptions are artificial and render inevitable the determination that SLS funding would be withdrawn, that Bradford & Bingley would enter into administration and that no compensation is payable. Other parties invite me to express my view on the reasonableness or otherwise of the Statutory Assumptions. As I indicate above, it is not part of my role to assess the appropriateness or otherwise of the Scheme itself.
- 10.3. It has been submitted that notwithstanding that the Scheme requires me to value shares and subscription rights immediately before the transfer time (see paragraphs 2.1 and 2.2 of my Assessment Notice) I should in fact conduct my valuation as at the earlier time of the rights issue (see paragraph 3.11 of my Assessment Notice). I do not agree with this submission. My role is to apply the terms of the Scheme. The Scheme requires a valuation immediately before the transfer time.

- 10.4. It has also been submitted that I should conduct my valuation at a later time than immediately before the transfer time because otherwise former shareholders and holders of subscription rights will be deprived of the opportunity to benefit from an improvement in the fortunes of Bradford & Bingley. Again, I do not agree with this submission. My role is to apply the terms of the Scheme.
- 10.5. It has also been submitted that my determination of any compensation under the Scheme should take into account claims that shareholders were misled or mis-sold shares by Bradford & Bingley, in particular in connection with the rights issue. I have received many allegations that Bradford & Bingley and its directors made misleading statements in relation to the rights issue and in the period leading up to nationalisation. It is no part of my role to assess whether anyone has a claim outside of the Scheme in relation to any statements or actions of Bradford & Bingley or its directors.
- 10.6. Similarly it has been submitted that there were various failings by the Government and the regulatory authorities, including that they should have provided additional support to Bradford & Bingley and that the Government manipulated the media by creating a false market in Bradford & Bingley shares. Again, it is no part of my role to assess the strength of such claims.
- 10.7. Some submissions were to the effect that my determination of any compensation under the Scheme should take account of the loyalty and length of relationship with Bradford & Bingley of shareholders as both customers and shareholders of Bradford & Bingley. These are, however, not relevant factors under the Scheme.

- 10.8. A number of submissions proposed that compensation should be awarded in the form of shares in Santander, the owner of Abbey, since it acquired the Bradford & Bingley deposit business and branch network (see Section 5 above). As indicated above, the Scheme requires me to value ordinary shares in Bradford & Bingley (and subscription rights in respect of such shares) immediately before the transfer time (see paragraphs 2.1 and 2.2 of my Assessment Notice). Since I have concluded that these shares and subscriptions rights had no value immediately before the transfer time, there is no basis on which I could conclude that compensation, whether in the form of cash or shares in any company, is payable by HMT to shareholders or holders of subscription rights under the Scheme.
- 10.9. It has been submitted that my determination that no compensation is payable under the Scheme breaches rights under Article 1 of Protocol 1 of the European Convention on Human Rights. Again I emphasise that my role is to apply the terms of the Scheme. This submission amounts to an attack on the Scheme itself.
- 10.10. It is clear from the submissions made to me that some former shareholders do not fully understand or accept that the shares that they used to own in Bradford & Bingley have been transferred by the Transfer Order into public ownership. Some former shareholders complain that they were neither consulted about nor given any notice of the transfer. These matters are not relevant to my determination of compensation under the terms of the Scheme. The Scheme requires me to value the shares and subscription rights immediately before the transfer time.

- 10.11. Many submissions have been made on the basis of financial hardship. The Scheme makes no provision in respect of financial hardship and I am not entitled to take financial hardship into account in determining whether any compensation is payable by HMT under the Scheme.
- 10.12. It has been submitted that I should adopt a different approach in determining compensation depending on whether a former shareholder purchased shares or was given “free” shares. Again, this is not a relevant distinction under the terms of the Scheme and I am not entitled to take it into account.