House of Commons
Treasury Committee

Project Verde: Government Response to the Committee's Sixth Report of Session 2014–15

Fifth Special Report of Session 2014–15

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Treasury Committee

The Treasury Committee is appointed by the House of Commons to examine the expenditure, administration, and policy of HM Treasury, HM Revenue and Customs and associated public bodies.

All publications of the Committee (including press notices) and further details can be found on the Committee’s web pages at www.parliament.uk/treascom.

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The Committee is one of the departmental select committees, the powers of which are set out in House of Commons Standing Orders, principally in SO No 152. These are available on the Internet via www.parliament.uk.

Publication

The Reports and evidence of the Committee are published by The Stationery Office by Order of the House. All publications of the Committee (including press notices) are on the Internet at www.parliament.uk/treascom.

Committee staff

The current staff of the Committee are Chris Stanton (Clerk), Anne-Marie Griffiths (Second Clerk), Adam Wales and Gavin Thompson (Senior Economists), Hansen Lu, Gregory Stevens (on secondment from the Bank of England), Callum Saunders (on secondment from the NAO), and Laura Saks (on secondment from the FCA) (Committee Specialists), Steven Price (Senior Committee Assistant), Alithea Williams (Committee Assistant), and Sanjay Odedra (Media Officer).

Contacts

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Fifth Special Report

The Treasury Committee published its Sixth Report of Session 2014–15, Project Verde, on 23 October 2014, as House of Commons Paper No. 728 (incorporating HC 300, Session 2013–14). The Government Response to this Report was received on 12 January 2015. It is published as an appendix.

The response from the Government is in plain text and the Committee’s conclusions and recommendations are in bold text.

Appendix: Government Response

Overview

In October 2014, the Treasury Committee published the report of its inquiry, launched in June 2013, into the divestment of 632 branches of Lloyds Banking Group under ‘Project Verde’, and the collapse of the Co-operative Bank’s bid for them.

As the Committee notes (Paragraph 1), in November 2013 HM Treasury announced that it would direct the Regulators to conduct an investigation into events at the Co-operative Bank and the circumstances surrounding them, using its powers under the Financial Services Act 2012; this investigation will be led by an independent person appointed by the Financial Conduct Authority (FCA) and the Prudential Regulation Authority (PRA) with the approval of HM Treasury.

The Government welcomes the thorough inquiry conducted by the Committee, and detailed summary of its findings from the evidence presented to it over these 16 months. The Government has no doubt that this will provide a profoundly helpful contribution to the independent investigation and ongoing inquiries by other bodies.

The Committee’s conclusions and recommendations for other authorities

The Committee’s report (pages 104 ff) sets out a range of detailed conclusions, and a number of recommendations for other bodies, including the Financial Reporting Council and the financial services regulators (FCA and PRA). These independent bodies are expected to respond separately to the Committee’s recommendations. Responses to recommendations directed at the Government are set out below.

The Government notes in particular the conclusions of the Committee’s inquiry that:

- notwithstanding any shortcomings in the respective oversight roles played by the auditor and the regulator that may be uncovered by the other inquiries, banks—in this case the Co-op Bank—bear primary responsibility for their own prudent management (Paragraph 129); and
the Committee has seen no evidence that the goodwill expressed by the Government towards Co-op Bank’s bid amounted to pressure on any party, and that that witnesses have presented the Committee with overwhelming evidence to the contrary (Paragraph 276).

**Recommendations for the Government**

The Government and the regulators should at the earliest opportunity make proposals to extend the coverage of the Senior Managers and Certification Regimes to, and remove the application of the Approved Persons Regime from, other parts of the financial services industry. (Paragraph 207)

The Government notes the Committee’s recommendation. The Fair and Effective Markets Review is considering whether to extend the Senior Managers and Certification Regimes to non-bank firms active in fixed income, foreign exchange and commodities markets. The Review will report in June 2015. Further primary legislation would be needed to extend the Senior Managers and Certification Regimes beyond banks, building societies, credit unions and PRA-regulated investment firms.

The independent inquiry into events at Co-op Bank and the circumstances surrounding them should consider:

- Whether the FSA could or should have developed superior stress-testing tools sooner than it did;
- Whether superior stress-testing tools would have led to Co-op Bank’s loan impairments being discovered sooner;
- Whether Co-op Bank’s impairment profile—which appeared to differ from that of other banks throughout the financial crisis—should have led the regulator to inspect it more closely prior to 2012;
- Why the FSA’s analysis on the Britannia merger failed properly to account for the prudential risks attached to the Britannia assets that have since been uncovered by the PRA;
- Whether the work provided by KPMG and JPMC on the Britannia merger met a reasonable standard, in substance as well as form;
- Whether the FSA was made aware of the change made by Co-op Bank to the accounting treatment for its IT platform replacement programme in 2010, and whether the FSA should have foreseen and acted on its consequences—that is, delaying the effect of the IT programme on the bank’s regulatory capital;
- Whether—given the conclusions of the independent inquiry on the forgoing points and the FRC’s investigation on the late emergence of Co-op Bank’s capital shortfall—Co-op Bank’s Verde bid could or should have been halted sooner;
I) What, if anything, further can be learnt from the record of the Government’s contacts with Co-op Bank and Group, Lloyds Banking Group, the regulator, UKFI and NBNK during the Verde bidding process. (Paragraph 303)

The Government welcomes the Committee’s work in this area and will consider its recommendations when determining the scope of the investigation under the Financial Services Act 2012, in consultation with the independent person appointed to lead it and in the light of any issues that may arise from the enforcement investigations which the FCA and PRA have confirmed that they are undertaking.

The Government has committed to ensuring that this investigation will cover the actions of relevant authorities (regulators and government) and the institution itself, including prudential issues, governance (including the appointment of senior staff) and acquisitions. The direction and the investigation’s report will be laid before Parliament.

The period that the investigation will review will start from at least 2008 and run to at least the time when the investigation was announced. The Government can confirm the review will cover the period of the merger between the Co-operative Bank and the Britannia Building Society in 2009.

In respect of the Government’s contacts with Co-op Bank and Group, Lloyds Banking Group, the regulator, UKFI and NBNK during the Verde bidding process, HM Treasury has undertaken to ensure that the independent investigator will have access to all of the relevant information from the Treasury’s records. A summary of the Treasury’s contacts with the various parties, and the underlying purpose of those contacts, was included in the Chancellor of the Exchequer’s letter to the Committee of 1 August 2014, published by the Committee as Written Evidence PV 44 for this inquiry.

The independent investigation will not start until it is clear it will not prejudice the FCA and PRA enforcement investigations.