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EXECUTIVE SUMMARY

The Bank established the Customer Review in February 2017 to compensate the victims of the fraud committed at the HBOS Impaired Assets unit based at Reading and Bishopsgate. Together with my team, I have spent seven months assessing whether the Customer Review achieved the purpose of delivering fair and reasonable offers of compensation.

In the first part of the Report, I explain how the Bank went about the task, before turning to customer and stakeholder views of the Customer Review. The next section of the Report contains the core of my assessment of the structure of the Customer Review and its implementation. My conclusions, at a high level, may be summarised as follows.

There was much about the Customer Review for which the Bank is to be commended. The Bank set out to provide swift and fair compensation to customers impacted by the fraud. It sought to cast the net wide in defining the cohorts in the Customer Review population methodology, and it provided generous payments for legal assistance, interim payments and, to compensate for delay, a payment of £35,000 to everyone in the Customer Review. It also wrote off significant amounts of outstanding customer debt.

The Bank took the innovative step of appointing Professor Griggs as an independent reviewer. Professor Griggs played an important role in the process. He acted independently from the Bank, and, as a result of the steps he took, some customers received increases, sometimes substantial increases, over what the Bank offered. In a number of cases he overruled the Bank.

Perhaps most importantly, the awards paid by the Bank under the heading of 'distress and inconvenience' (what in this report are called D&I payments) were generous, and beyond what a customer could hope to have been awarded under that head of loss by a court. Redress under this heading was, moreover, extended to those customers who had not necessarily been victims of the fraud, but only of what I have called bad or aggressive banking practices. Although I have concluded that there were some flaws with the Bank's methodology as regards D&I payments, my overall assessment was that the Bank's D&I redress was generous.

Despite the many merits of the Customer Review, I have concluded that it had serious shortcomings. For example, Professor Griggs was placed in an impossible position and his appearance of independence was undermined by the way the process was structured. The most serious shortcoming, however, concerned the Bank's approach when it came to the assessment of direct and consequential loss caused by the fraud (referred to in this report as D&C loss). Having taken a lenient approach to the assessment of D&I redress, the Bank then took an overly adversarial approach in its assessment of claims for D&C loss, which was inappropriate to the Customer Review. I have concluded that this part of the Customer Review, both in structure and in implementation, was neither fair nor reasonable.

This unfairness and unreasonableness manifested in a number of different ways. The Bank refused to disclose documentation to customers, and, in the main, to fund financial advice, whilst placing undue emphasis on the contemporaneous documents, at the expense of the

customer submissions. This was not sufficiently communicated to customers. On the contrary, the Bank publicly emphasised the non-legal, customer-focused nature of the Review.

The consequence was that, from the outset, customers' D&C loss claims were unlikely to ever be able to meet the standards being set by the Bank. This seriously disadvantaged customers. Nor did the Bank adequately undertake its own assessment to enable it to reasonably and fairly identify where D&C loss may have been suffered. The outcome was that the Bank did not make a single award acknowledging that any D&C loss had been caused to customers by the fraud. As a matter of analysis, therefore, on the Bank's approach, the Bank appears to have been the only victim of the fraud to have been caused financial loss.

Other inconsistencies also resulted in unfairness. The Bank wrote off debts of those customers who were still with the Bank, but not those customers who had repaid their debts or refinanced them elsewhere, sometimes at considerable personal expense, in the period between the fraud and the date of the Customer Review. The Bank's population methodology (as regards individuals to be included in the review) was overly strict. It was limited to directors and so excluded a number of impacted customers. The general failure to communicate in a sufficiently clear and transparent way caused confusion, in particular as to what D&I payments were for or represented. Finally, the effect of the terms of the various forms of settlement agreement used by the Bank unfairly stifled some potential claims.

Accordingly, for the detailed reasons set out in the body of this report, and adopting the language of my Terms of Reference, I have reached the conclusion that the methodology and process of the Customer Review did not achieve the purpose of delivering fair and reasonable offers of compensation.

My recommendations are set out in Chapter 15. The central recommendation is that the customers' claims to D&C loss must be reassessed. One way of doing this is by means of an independent panel, along the lines I set out in an appendix to this report. Before proceeding along those lines, however, the Bank must conduct a proper consultation with stakeholders and customers.

My conclusions and this recommendation come with an important note of caution. My review has not been an appeals process. I am therefore unable to comment on the scale and breadth of D&C loss that may in fact have been suffered by customers as a result of the fraud, whether in respect of individual cases or generally. Particularly in view of the generosity of the D&I payments, it may be that for many customers, they have already been adequately compensated. Accordingly, it may be that the reassessment process does not result in a materially different outcome for many customers. The key difference, however, will be that their claims will have been properly addressed, in an open and transparent manner.

PART A INTRODUCTION

CHAPTER 1: THE ASSURANCE ("CRANSTON") REVIEW

1.1 In replying to a debate initiated by Kevin Hollinrake MP in the House of Commons on 18 December 2018, the Economic Secretary to the Treasury, John Glen MP, announced that the Bank had agreed with the Financial Conduct Authority ("FCA") that it would commission "a post-completion review to quality-assure the methodology and process" of the Customer Review.

1.2 The Customer Review was the compensation scheme the Bank had set up for businesses affected by what in this report I call the IAR fraud.[1] It was sometimes called the Griggs Review, but it was a Bank review with Professor Russel Griggs as the independent reviewer.

1.3 The Minister acknowledged the concerns that MPs had raised about the Customer Review. He added:

> "I am pleased that Lloyds has committed to publishing the review once it has concluded, and I welcome Lloyds' commitment to implementing any recommendations it produces."[2]

1.4 On 7 May 2019 the Bank announced that I had been appointed to conduct the review which the Economic Secretary to the Treasury had foreshadowed. It was to be an "Assurance Review led by a high profile independent party to go above and beyond a customary lessons learned exercise undertaken following the completion of a customer rectification process."

1.5 The aim of the Assurance Review, the announcement added, was to provide assurance "that the Customer Review, overseen by Professor Griggs, has delivered fair and reasonable outcomes for customers." It also stated that the Bank

> "will act upon any recommendations made by Sir Ross Cranston and will provide his final report to the Financial Conduct Authority and ensure its findings be made publicly available."

1.6 In this chapter I give a short account of my appointment to conduct the Assurance Review (which I will call "the Cranston Review") and a brief overview of how I went about the task. The details of the assessment I undertook is contained in the following chapters.

I APPOINTMENT OF CRANSTON REVIEW

Discussions about my appointment

1.7 On 14 March 2019 I was asked whether I would be interested in undertaking the review, of which this report is the product. I then met the Chief Executive of the FCA, Andrew Bailey, to explore my candidacy. An extensive check ensued about possible conflicts of interest.

[1] IAR refers to the Impaired Assets unit based in Reading, which I explain further in Chapter 2.
[2] House of Commons, Debates, Westminster Hall, Hansard v.651, 18 December 2018, c.285WH.

1.8 On 11 April 2019 I met representatives of the Bank for the first time. The meeting took place at 3VB, of which I am an associate member.[3] The Bank set out its understanding of the IAR fraud and its aftermath, including the criminal trial and the appointment of Dame Linda Dobbs DBE (see 1.22 below). They then explained the establishment of the Customer Review and the appointment of Professor Griggs. The Customer Review, I was told, used legal criteria to assess loss, but that was departed from with the use of a non-legal matrix to calculate distress and inconvenience payments for customers. The fraud had a range of impacts on customers and the matrix sought to capture them. The intention was to make offers quickly, but that proved unrealistic. Because payments for distress and inconvenience were non-legal in character, I was told, the usual rules on matters such as the disclosure of documents did not apply.

Principles for the Cranston Review

1.9 Prior to seeing the Bank on 11 April 2019 I had been given a set of principles to govern the Cranston Review ("Principles"). These had been agreed by the Bank, the FCA and key stakeholders in anticipation of its establishment.

1.10 The introduction to the Principles stated that the Cranston Review was "to deliver assurance that the Customer Review has delivered fair and reasonable outcomes." It would proceed by considering a sample of cases to provide independent assurance that the Customer Review had operated to deliver fair and reasonable outcomes. All interested parties would be able to submit evidence.

1.11 *Principle 1* was that the Cranston Review was to be conducted by a qualified and independent reviewer, which was to be achieved by appointing a person with appropriate senior legal experience and through the Bank conducting robust due diligence to ensure that the proposed candidate did not have any associations which could undermine confidence in his or her independence.

1.12 *Principle 2* was that stakeholders would be provided the opportunity to provide input into the scope of the Cranston Review.

1.13 *Principle 3* was that the Cranston Review would be conducted in as timely and efficient a manner as possible "recognising that the independent reviewer needs to be afforded the opportunity to conduct a thorough and robust review." That was to be achieved by adequate resourcing and by the Bank providing all the information and documentation required by the reviewer in a timely manner.

1.14 *Principle 4* was that the Cranston Review process should be transparent to all stakeholders. That was to be achieved by the reviewer publishing the final Terms of Reference, including the approach to the Cranston Review (including how it was intended to engage with interested parties) and expected timeframes. Further, the Bank "will publish the full final report."

[3] Like many former judges I have returned to the chambers where I practised as a barrister, 3 Verulam Buildings ("3VB") but as an associate, not a full member.

1.15 *Principle 5* was that the reviewer's findings were to be final. That was to be achieved by Bank committing "to acting upon any recommendations made by the Independent Reviewer" and to the outcome of the Cranston Review not being "subject to further submissions or analysis."

Cranston Review terms of reference

1.16 On 16 April I informed the Bank that I was prepared to conduct the Cranston Review.

1.17 There was a further meeting with representatives of the Bank at 3VB on 23 April 2019. The discussion focused on the proposed terms of reference for the Cranston Review ("the Terms of Reference"). The Bank told me that in proposing the matters to be investigated under them it had taken account of the complaints made about the Customer Review. We agreed that I would discuss the Terms of Reference with stakeholders.

1.18 About a week later I met with Professor Griggs and spoke to him and members of his legal team from the law firm Taylor Wessing LLP. They outlined their role in the Customer Review.

1.19 Under Principle 2 for the Cranston Review, stakeholders were to be given the opportunity to provide input into the draft Terms of Reference. Consequently I saw both the SME Alliance and the APPG on Fair Business Banking to discuss their views on the draft Terms of Reference and the conduct of my review.

1.20 The SME Alliance had various concerns. First, it raised the comparison between the compensation paid in the Customer Review and what a court would have offered. In its view, the Bank had promised "fair swift and appropriate compensation" not limited by legal rules. The offers made for distress and inconvenience may well have been better than a judicial award, it told me, but in the majority of cases losses (and more importantly consequential losses) were not considered. There was also the impact of the Draft Project Lord Turnbull Report, referred to in the following chapter, and its impact on what a court would have awarded.

1.21 The APPG had a number of comments when I met them. A major issue was the role of Professor Griggs as the independent reviewer and the need for a thorough assessment of what he did in that capacity. There was also a concern about the settlement agreements which customers accepting compensation had to sign, and the need for a close analysis of the restrictions which these imposed. As regards disclosure, the APPG wanted me to give careful consideration as to the impact of the Bank's denying access to the information it had, including on compensation levels.

1.22 As a result of these meetings, I made changes in the draft Terms of Reference to accommodate the concerns. I took the view that in as much as the matters raised with me were not dealt with expressly in the redraft, I was able to interpret what was there to catch the concerns in the course of my review. The exception was the potential impact of the Draft Project Lord Turnbull Report. I have taken the view that since that is a matter for the inquiry being conducted by Dame Linda Dobbs DBE – which I explain in the following chapter – it would be wrong for me to enter that territory.

1.23 The Bank made some comments on the redraft, which I adopted as improvements in expression. At that point the Terms of Reference were fixed. They are at Appendix 1 to this report.

1.24 In the meanwhile there had been discussions over my terms of engagement. Agreement was reached in early May. Under them the Bank agreed that I had an overriding duty to act with independence. The report was not to contain customer confidential information. The Bank needed to waive legal professional privilege before publication. It was to have the opportunity to comment and correct factual errors but my decisions about content were final.

1.25 Following agreement there was the announcement on 7 May 2019, as I have said, that I had been appointed to conduct the Cranston Review

The Cranston Review team

1.26 I had identified Rory Phillips QC, a member of 3VB, as senior counsel to advise me during the review. Mr Phillips has had extensive experience with government and inquiry work, and served as counsel to the Parliamentary Commission on Banking Standards during its report into the failure of HBOS.[4] Kate Holderness and Anne Jeavons had been specialist legal advisers for the Commission's work on HBOS and subsequently they, along with Mr Phillips, agreed to assist me. The legal team was completed by the appointment of two other counsel from 3VB, Teniola Onabanjo and Sophia Dzwig.

1.27 For financial advice FTI Consulting LLP was one of a number of organisations the Bank mentioned to me. It is one of the largest financial consulting firms in the world, headquartered in the United States. I met two of their senior managing directors on 29 April 2019, including Simon Kirkhope. Subsequently I engaged the firm to provide me with financial advice. As with any such large firm operating in this area, it had undertaken work for the Bank. However, it had only begun restructuring work in Britain 11 years previously, so had not been affected by the culture prevalent with this type of activity at the time of the IAR fraud.

1.28 During the course of my review, the FTI team was led by Mr Kirkhope, who is a licensed insolvency practitioner, a fellow and member of the council of the Association of Business Recovery Professionals and a fellow of the Institute of Chartered Accountants in England and Wales.

1.29 To assist me with the media and with stakeholder and customer engagement, I chose Project Associates, which is a leading strategic communications consultancy based in London. During the course of my review the work was largely undertaken by four members of the firm, Joseph Hesketh, Michael Rose, Frederick Thiede-Merlo, and Rebecca Davies.

[4] House of Lords, House of Commons, Parliamentary Commission on Banking Standards, *"An accident waiting to happen": The failure of HBOS*, Fourth Report of Session 2012-13, HL Paper 144, HC 705, 4 April 2013.

1.30 Each of my advisers was subjected to the same rigorous conflicts check which I had undergone. As is usual in reviews of this nature, the Bank has been obliged to bear the cost of my review. However, my team and I have been and remain entirely independent.

II INPUT TO CRANSTON REVIEW

First customer letter

1.31 I sent my first letter to customers on 7 June 2019, introducing my review. After introducing my task – to inquire whether the Customer Review had delivered fair and reasonable outcomes for customers - I assured readers that I was committed to a thorough and robust process, that it was vitally important that my review was open, rigorous, and fair, and that the Bank would act upon my recommendations. I emphasised that I was not acting as an appeals process for those unhappy with the compensation offered by the Bank.

1.32 After setting out my task using the Terms of Reference, I stated that I would welcome information about readers' experience of the Customer Review. Comments could be submitted via the website (which was to go live shortly after the letter), in writing or via the email address info@cranstonreview.com. (The email address had been live from 17 May 2019.) Alternatively, if they preferred, I could meet customers by way of a meeting or telephone call. I asked for responses to the letter by Monday 8 July 2019.

The website

1.33 As part of my communications policy, I established a standalone website to provide information about my review. This was also part of my effort to be transparent about the Cranston Review's scope and purpose. There was text with sections outlining the Terms of Reference, my biography and information on how to get in contact. The Q&A section, about the key aspects of my review, was based largely on the Terms of Reference. However, it also gave reassurance that my review was wholly independent of any influence from the Bank. In addition it reiterated that it was vitally important that the review was open, rigorous, and fair, and that the Bank would act upon its recommendations.

1.34 As well as the text, the website included a video introduction from me. This two-minute clip was shot at 3VB and outlined the purpose of my review, its aims, my background and my intentions for how it would be conducted. The video has since been on the front page of the Cranston Review website. I felt it important for customers and interested parties to see and hear my aims first-hand.

1.35 The development of the site took a little longer than initially expected. It is understood that it went live on 15 June 2019. Upon the website going live, my team informed the Bank, the SME Alliance, the APPG on Fair Business Banking and other relevant stakeholders so that they could share a link to the website with their contacts and ensure people were aware of its existence. Additionally, customers inquiring about further information were referred to the website and its address was included in both the customer letters issued after it went live. I also made it clear in customer meetings that

this report would be published in full on the website, a point I also reiterated in customer letters.

Statements by the Bank, Professor Griggs, the SME Alliance and the APPG

1.36 As I explain further in Chapter 7, I requested that the Bank, Professor Griggs, the SME Alliance and the APPG prepare written submissions for the review. My intention was to use them as a basis for the analysis to be undertaken. It was always anticipated that once the submissions of the Bank and Professor Griggs were available it was likely that there would be requests for supplementary statements and inquiries on matters of detail in respect of individual cases and on wider methodology points. That proved to be the case.

1.37 The Bank provided everything I requested. However, Professor Griggs did not give me access to advice provided to him by his own advisers. He explained to me that his working papers, correspondence and the advice notes between him and his advisers were intended to be private, internal communications and were never intended to be made public. He went on to say that having a private space for himself and his advisers to consider and discuss opinions on individual cases allowed him to ensure that customer outcomes had been thoroughly challenged and tested before he reached a conclusion. Further, Professor Griggs took the view that the vast majority of communications between him and his advisers were privileged and therefore non-disclosable.

1.38 I did not agree with Professor Griggs' decision. I had access to the correspondence between the Bank and Professor Griggs, which was included in the Bank's files. However, my ability to consider the rationale and justification for some of his decision-making was restricted. I return to this in Chapters 12 and 13 below. Overall, I do not regard my conclusions and recommendations as in any way affected by Professor Griggs' decision. There was sufficient in the Bank's files and customer submissions to draw the conclusions I have.

Pre-publication comments and factual corrections

1.39 I provided the Bank and Professor Griggs with my draft report, so that they could comment on it and correct any factual inaccuracies, within an agreed timescale. Both took full advantage of this opportunity and submitted detailed comments and factual corrections. My team and I carefully reviewed all of the material we received and made factual corrections and other amendments, where necessary. I make it clear, however, that final decisions as to the content of the report were mine and mine alone. I am also able to confirm that I made no change of substance, either in my findings or in my recommendations, as a result of these comments.

Legal assistance for those making submissions to me

1.40 I had agreed with the Bank that, given the scope of my review, customers would not generally require legal support in providing their input. My review was not an appeals process for those unhappy with a specific outcome offered by the Customer Review; my primary focus was on the individual customers' experiences of the Customer Review and how it was conducted as a process. Since I would have access to all the information

provided by participants in the Customer Review, there was no need for customers to repeat the submissions they had already provided.

1.41 However, the Bank and I recognised that there might be a small number of customers in the Customer Review who for one reason or the other required some support from a third-party advisor in formulating their input. The agreement we reached was that the Bank would meet the reasonable costs of this assistance. Application in the first instance was to the Bank, but ultimately the question of whether any costs were reasonable was a matter for me. Once the agreement was in place matters worked relatively smoothly. I was required to decide on only one occasion whether what a lawyer had claimed was reasonable.

1.42 As a result of these arrangements, the Bank paid a total of £66,000 (including VAT) for 28 customers' advisors in fees and expenses. That included three individuals who did not participate in the Customer Review. (31 individuals had their fees agreed by the Bank, but three did not take the matter further and no costs were incurred.)

Travel expenses

1.43 I was also able to agree with the Bank that it would cover reasonable travel costs for those who had participated in the Customer Review and who wished to meet me. Again, this was subject to the costs being agreed in advance with the Bank. Information relating to legal and travel costs were both communicated via the Cranston Review website. The arrangement worked well.

1.44 In all, the Bank paid a total of £3,000 to cover travel expenses for 14 individuals who met me during the review.

Meetings with stakeholders

1.45 During the course of the review I met with a number of stakeholders to explain how I was going about the work and to seek their assistance in engaging with customers.

1.46 After my initial meetings with the SME Alliance and APPG over the Terms of Reference, I met with both on a periodic basis. Early on, Heather Buchanan, the director of policy and strategy at the APPG, arranged two meetings at the House of Commons with some of the lawyers who had represented customers in the Customer Review. Subsequently, I had four meetings with the APPG, including two with its chair, Mr Kevin Hollinrake MP. I met the SME Alliance on four occasions, attended by Mrs Nikki Turner, the co-founder and director, together with (on two occasions) its chair, Mr Nick Gould. They were able to persuade a number of customers who were otherwise reluctant to do so to see me. I briefly addressed a general meeting of the SME Alliance on 2 July 2019 to explain how I was conducting the review.

1.47 Others I met on a periodic basis were the Economic Secretary to the Treasury, John Glen MP (three meetings) and the FCA (three meetings). I also saw the Rt Hon Nicky Morgan MP, then Chair of the Treasury Select Committee, Jonathan Reynolds MP, shadow Economic Secretary to the Treasury, and Anthony Stansfeld, the Thames Valley Police and Crime Commissioner to set out for them the nature of my review.

Engagement with customers

1.48 During the course of my review I also met many customers of the Bank and participants in the Customer Review. In summary, I had 49 meetings and met 62 customers. Most of these were in London, but I also travelled outside London where this was convenient for customers. This included trips to Oxford, Bristol, Milton Keynes, and Norwich. I also received letters and emails from customers separate from these meetings. In Chapter 9 I give further details. In Chapter 8 I spell out something of what they told me.

1.49 After my first letter to customers shortly after my appointment, I wrote again on 29 July 2019 to explain the progress of my review. By that time the date I had mentioned in the first letter for customers to get in touch with me had passed. I said that meetings with customers had been invaluable in helping to provide a picture of the Customer Review process, and that what I had been told would form a key part of my report. I thanked customers who had provided me with their perspective, both at these meetings and through submissions received via email. I acknowledged that in many cases the process had brought back difficult memories.

1.50 I wrote again to customers on 3 September 2019 announcing an extension of the deadline for the report from the end of September until mid-November. I apologised for this and explained that I had conducted a greater number of meetings than I envisaged at the outset. The result was that this aspect of my review had taken longer than anticipated. I also explained that the customer meetings had raised a number of matters which fell within my Terms of Reference and required further consideration by me and my team. I also wrote that I had reconsidered the number of cases to be sampled and on expert advice from the financial team had decided that 16, and not 21 businesses, was a sufficient sample size. I added that the change in the sample would allow a greater concentration on the matters arising from the customer meetings, which needed to be properly considered and analysed.

1.51 A further letter to customers was sent on 25 November 2019 to explain that I would not be able to publish the report in November as anticipated. The letter expressed regret about this and reassured customers of my determination to complete the work as soon as possible.

Meetings with the Bank

1.52 During my review it was necessary for me (and other members of the Cranston Review team) to have meetings with the Bank, which took place at the Bank's offices in London or at 3VB. In total, six meetings were held between April 2019 and August 2019. Initial meetings involved the Bank explaining, at a high level, the methodology behind the Customer Review and a "walk-through" of the case assessment process. At further meetings I explained to the Bank progress made in reviewing the sample cases and the anticipated timeframe for the delivery of my report.

PART B THE BANK'S CUSTOMER REVIEW

CHAPTER 2 BACKGROUND TO BANK'S CUSTOMER REVIEW

2.1 The Bank explained to me that it set up the Customer Review to compensate customers for any impacts on them following the events at IAR which led to the conviction of the former bankers, Lynden Scourfield and Mark Dobson.

2.2 The Bank told me that "[t]he critical evidence that ultimately resulted in the convictions was not available to HBOS at the time." It added that whilst the police investigation into the events at IAR was ongoing, it was constrained in what it could say and do and, as such, "a number of customer disputes were placed on hold until the trial concluded on 31 January 2017." After the trial concluded, the Bank announced on 7 February 2017 that it would undertake a review of all the customer cases which may have been affected by the criminal activities linked to IAR.

2.3 This chapter outlines the events leading up to the Customer Review including the trial and criminal convictions. It also covers two notable developments after the Bank's decision to set up the Customer Review. First, there was the Bank's appointment of Dame Linda Dobbs DBE to consider whether the issues relating to IAR were investigated and appropriately reported to authorities ("the Dobbs Review"). Second, the FCA issued a Final Notice on 20 June 2019 imposing a penalty of £45.5 million on the Bank of Scotland plc ("BOS") for regulatory failings in connection with the events at IAR.

2.4 The chapter proceeds as follows. Part I describes the role of IAR within HBOS and introduces Lynden Scourfield, Mark Dobson, QCS and other individuals connected with QCS. Part II describes the fraud. Part III outlines the 2007 investigations conducted by BOS into the events in IAR, the 2010 report of the "skilled person" and the Project Lord Turnbull report. Part IV deals with the criminal trial and sentencing. Part V outlines the remit of the Dobbs Review and the FCA's decision in the Final Notice.

2.5 Before setting out the background, let me explain briefly the corporate structure of BOS at the time of the events at IAR and subsequently, to assist the reader in understanding the summary that follows. In 2001, Halifax Group plc merged with BOS and the merged group was known as the HBOS Group. BOS was therefore part of the HBOS Group. On 19 January 2009, Lloyds TSB Bank plc acquired the HBOS Group and this led to the formation of the Lloyds Banking Group (referred to in this report as "the Bank"). BOS is now part of the Bank.

I THE IMPAIRED ASSETS FUNCTION AND IAR

The Impaired Assets function

2.6 In its submissions to my review, the Bank explained that:

> "The Impaired Assets function within HBOS was established to work with corporate customers experiencing financial difficulties with a view to those customers maximising the repayment of their debts, ideally through improved trading performance but if this was not possible through some other form of restructuring or insolvency process..."

2.7 In a witness statement provided to Thames Valley Police in September 2010 as part of its investigation into the events at IAR (known as "Operation Hornet"), a senior employee of the Bank explained that "BOS policy required relationship managers within the Corporate or Business Banking divisions to refer their existing customers to [Impaired Assets] if warning signs indicated that there was a concern with respect to, for example…the trading position, or failure to adhere to the terms of the facility documentation."[5]

Impaired Assets Reading

2.8 The HBOS Impaired Assets London and South team dealt with customers whose relationships with the Bank were managed out of London and the South of England and who had been referred to Impaired Assets. The London and South team were split between an office in Reading and an office in Bishopsgate in London. The members of the team in London reported to senior management in Reading. IAR therefore refers to the London and South team, whether based in Reading or in London.

Lynden Scourfield and Mark Dobson

2.9 Lynden Scourfield was the lead director of IAR between 2002 and March 2007. He was based in the Reading office. He was suspended (in circumstances which I describe below) in March 2007 and resigned from BOS in April 2007. In the June 2019 Final Notice which I referred to above, the FCA noted that:

> "[a]s at 1 March 2007, [Lynden] Scourfield was the relationship manager of 25 business customers with a debt level of £274 million. There were at least a further 21 businesses whose relationship was managed by [Lynden] Scourfield at some point between 2002 and 2007."[6]

2.10 Mark Dobson was an associate director within IAR, based in the London office. He reported to Lynden Scourfield. After Lynden Scourfield's resignation, he continued to be employed by the Bank until June 2012 when he was dismissed for gross misconduct following his arrest in relation to the events at IAR.

Quayside Corporate Services Limited

2.11 Quayside Corporate Services Limited ("QCS") was a firm of "turnaround consultants". As further described below, the firm was engaged by IAR on various occasions to assist with the management of customer accounts.

2.12 QCS was owned and managed by David Mills. Other individuals connected with QCS included Alison Mills (David Mills' wife), Michael Bancroft and Anthony ("Tony") Cartwright. Other Mills entities were Sandstone Organisation Ltd and Richard Paffard Consultancy ("RPC").

[5] An extract from a witness statement of an official of the Bank dated 28 September 2010, page 3.
[6] FCA Final Notice, paragraph 4.13.

II THE IAR FRAUD

2.13 As I explain in section IV below, Lynden Scourfield, Mark Dobson and individuals connected with QCS were convicted of serious offences in relation to activities linked to IAR. This is what in this report is referred to as the IAR fraud. It was established in the criminal trial that the IAR fraud began in around 2003.

2.14 I set out below a summary of the IAR fraud which formed the basis of the criminal trial. I have taken this summary from the FCA's final notice which I referred to above[7]:

(1) Lynden Scourfield required many of the IAR business customers that he managed to appoint and pay fees to QCS (and related entities) as a condition of the customer receiving continued support from BOS.

(2) The involvement of QCS varied but in some cases individuals from QCS were appointed as directors of the distressed businesses. This resulted in QCS being involved in the decision-making over the strategy and finances of the businesses including the sale of a business to companies set up by QCS. In many cases, inappropriate or overly optimistic turnaround plans were implemented by QCS which increased the risk of losses to both the business customers and to BOS.

(3) As part of its proposed turnaround of the businesses, QCS would submit proposals for additional finance to BOS for approval by Lynden Scourfield. QCS would purportedly use the lending to fund its turnaround strategies. In some cases, the lending was granted beyond Lynden Scourfield's authority to do so and beyond the ability of the customer to repay the lending.

(4) In return for his part in the fraud, Lynden Scourfield received money as well as gifts and hospitality from QCS including holidays and prostitutes.

(5) As regards Mark Dobson, between 2005 and 2006, he allowed £152,750 to be paid to parties connected with QCS without the authority of BOS, the customer or the administrator and in return he received a payment of £30,000. In addition, he wrote off interest owed by another business customer to make a gain for QCS.

2.15 Where I refer in this report to the fraud or to sample cases where fraud is evident on the file, I am referring to cases where some elements of the pattern summarised above is present.

II THE INVESTIGATIONS AND REPORTS

2.16 What follows is a high-level summary of some of the background to the criminal trial, which led to the Customer Review. It does not pretend to be authoritative but is included to allow the reader to understand better the sequence of events leading to the trial. In addition to the formal inquiries into the IAR fraud mentioned here, there were informal investigations, notably by Nikki and Paul Turner, who had been victims of the fraud. As I describe in Chapter 7, Nikki Turner went on to be a cofounder of the SME Alliance.

[7] FCA Final Notice, paragraphs 4.14 – 4.19.

2.17 In the meetings with me and in submissions to my review, customers and other stakeholders stated that they believed that HBOS, and subsequently the Bank concealed the IAR fraud. Some referred to the Project Lord Turnbull report and that they considered this to be an issue relevant to my review. Under my Terms of Reference, I am limited to undertaking a review of the Bank's Customer Review. The alleged cover up is the subject of the Dobbs Review, the scope of which I outline below.

HBOS' internal investigations

The peer credit review

2.18 In late 2006, the head of IA, who had oversight over IAR, decided that IAR should be the subject of a peer credit review. This meant that a sample of cases managed by IAR would be reviewed by employees in other teams to check that, in their management of cases, employees in IAR were complying with BOS' policies and procedures. The head of IA decided that a peer credit review was required because there was a concern about increasing levels of debt in cases managed by IAR.

2.19 Following the review, a report was produced in February 2007 which made a number of findings. Those findings are summarised in the May 2007 report to which I refer below. The findings included that there was limited compliance within IAR with the procedure for approving increases in lending limits. Further, that unusual strategies had been employed in the management of cases, with cases exhibiting increasing rather than decreasing risk. This was noted in particular in relation to the cases within Lynden Scourfield's portfolio.

2.20 The result of the peer credit review was presented to Lynden Scourfield at a meeting with the head of IA on 8 March 2007. The following day, Lynden Scourfield advised that he was unwell and left work. He was suspended on 23 March 2007 pending further investigation and subsequently resigned on 27 April 2007.

The May 2007 Report

2.21 Following the peer credit review, a senior manager within BOS, who was independent of the IAR reporting line, was tasked with investigating the concerns raised by the peer credit review. In the report dated 21 May 2007, the senior manager reached similar conclusions. In particular, the May 2007 report stated that there was a culture of non-adherence to credit sanctioning policy within the IAR team which was allegedly endorsed by Lynden Scourfield. Furthermore, the strategies employed by Lynden Scourfield for the cases in his portfolio were different from the strategies employed by other members of IAR; Lynden Scourfield's portfolio demonstrated widespread dramatic increases in debt and capital risk and there were no formal sanctions for the increases. The report also noted that Lynden Scourfield appeared to rely heavily on QCS for advice and support on many of his cases and that there were no letters of engagement in respect of QCS' work for the Bank.

2.22 The May 2007 report recommended, amongst other things, that Mark Dobson, who was part of the team who failed to adhere to credit sanctioning policies, should be subject to a disciplinary process.

The CFCP investigation

2.23 As a result of the concerns raised by the peer credit review, the Bank's Corporate Financial Crime Prevention team ("the CFCP team") were tasked with ascertaining whether there was any evidence of criminal behaviour on the part of Lynden Scourfield (such as personal inducements or unauthorised benefits). They were also asked to investigate the background of David Mills of QCS.

2.24 The CFCP team produced a report in July 2007. I have not seen that report. In statements dated 19 March 2008 and 21 January 2009, the CFCP team explained that their conclusion was that there was no evidence that Lynden Scourfield's actions were for personal gain or of a fraudulent nature. They noted that there was some email correspondence referring to a business trip in the US and a holiday in Barbados but concluded that there was "nothing specific or substantiated"[8].

The skilled person's report

2.25 On 19 October 2009, the Financial Services Authority ("FSA"), the FCA's predecessor, issued the Bank with a notice requiring it to provide a report from a "skilled person" in accordance with section 166 of the Financial Services and Markets Act 2000. The skilled person was to investigate the FSA's concerns about HBOS' response to the discovery of issues at IAR. Those concerns centred on HBOS' efforts to investigate whether and to what extent it had been used for a purpose connected with financial crime, HBOS' handling of issues raised by customers who suffered losses, and the nature and extent of any action taken against culpable individuals.

2.26 The skilled person's investigation included a review of a sample of cases managed by IAR. They produced a final report dated 9 July 2010. Their main findings included the following:

(1) HBOS' efforts to investigate IAR lacked co-ordination and the resulting work was therefore fragmented. Furthermore, there was a failure to follow up on issues including questionable transactions and allegations made about Lynden Scourfield's conduct. No disciplinary action was taken against Lynden Scourfield, who had resigned, and whilst the May 2007 report recommended a disciplinary process be followed in respect of Mark Dobson, there was no evidence that action was taken.

(2) There was no direct evidence to suggest that Lynden Scourfield directly financially benefited from the lending activities he oversaw. However, there were a number of unanswered questions in relation to a number of issues, which if substantiated, could alter the skilled person's view.

[8] Statement dated 21 January 2009.

(3) There was no direct evidence of dishonesty or lack of integrity on the part of David Mills and associated QCS consultants. However, there were a number of unanswered questions and in the absence of answers, it was not possible to conclude that there was no improper conduct on their part.

(4) From the sample cases reviewed, the skilled person confirmed that £3.9 million was paid to QCS and related entities and individuals between August 2002 and December 2008. There was a further £4.1million that had potentially been paid out but which they could not confirm.

2.27 The FSA provided a copy of the draft skilled person's report to Thames Valley Police in July 2010 and provided the final report to Thames Valley Police in September 2010.[9]

Project Lord Turnbull Report

2.28 Thames Valley Police began investigating the events at IAR in 2010. As part of that investigation, on 10 and 11 July 2013, they interviewed a senior manager within the Bank's Commercial Banking (Risk) division. Following that interview, she prepared a report, at the request of an official of the Bank, which detailed matters raised in the interview with the police. The draft report, which is dated 9 January 2014, was titled "Project Lord Turnbull". The APPG published the draft report on 21 June 2018.

2.29 At the core of the report was the allegation that HBOS (and subsequently, the Bank) intentionally covered up the IAR fraud from at least January 2007 but possibly from early 2005. The report stated that initial concealment occurred when HBOS ignored early evidence of the fraudulent conduct, and then artificially reduced the 2007 provision for the fraud from nearly £1 billion to just over £200 million to engineer its exclusion from financial statements. Thereafter, it is stated that the board of HBOS continued to deliberately conceal the IAR fraud in order to: overstate profits, regulatory capital and credit quality; overstate the share price; mislead shareholders, the FSA, credit rating agencies and Lloyds TSB; and obtain reduced capital requirements under new financial regulations.

III THE TRIAL AND SENTENCING

The indictments and the trial

2.30 Following the investigation by the Thames Valley Police, a number of individuals were indicted.

2.31 The pre-trial indictment included some counts and persons which were not pursued at trial.

2.32 The trial indictment included charges against eight people, two of whom were subsequently acquitted. The charges against the six remaining individuals were as follows:

[9] FCA Final Notice, paragraph 4.173.

(1) Count 1 (conspiracy to corrupt): David Mills, Michael Bancroft, Mark Dobson and Lynden Scourfield conspired so that Lynden Scourfield and Mark Dobson would obtain gifts and other consideration as inducements to show favour to David Mills, Michael Bancroft and others.

(2) Count 2 (fraudulent trading): David Mills, Alison Mills, Lynden Scourfield and a fourth person were party to the carrying on of the business of Clode Group for a fraudulent purpose, namely, to obtain personal gain at the expense of the company and its creditors.

(3) Count 3 (fraudulent trading): David Mills, Michael Bancroft, Anthony Cartwright and Lynden Scourfield were party to the carrying on of the business of Frank Theak & Roskilly Ltd/Magenta Studios Ltd for a fraudulent purpose, namely, to obtain personal gain at the expense of the company and its creditors.

(4) Count 4 (fraudulent trading): David Mills, Michael Bancroft, Anthony Cartwright and Lynden Scourfield were party to the carrying on of the business of MSG Ltd for a fraudulent purpose, namely, to obtain personal gain at the expense of the company and its creditors.

(5) Count 5 (fraudulent trading): David Mills, Michael Bancroft and Lynden Scourfield were party to the carrying on of the business of Remnant Media Ltd for a fraudulent purpose, namely, to obtain personal gain at the expense of the company and its creditors.

(6) Count 6 (conspiracy to conceal criminal property): David Mills, Michael Bancroft, Mark Dobson, Alison Mills, Anthony Cartwright, Lynden Scourfield and two other persons conspired to conceal, disguise, convert and transfer criminal property, the criminal property being the proceeds of the corrupt relationship described in Count 1.

2.33 The businesses which were defrauded and named in the indictment were customers of HBOS, managed by IAR.

2.34 The trial commenced on 26 September 2016. Lynden Scourfield had pleaded guilty on 12 August 2016 and therefore did not stand trial. He was given a 25 percent discount on his sentence for his guilty plea.

2.35 The jury reached a verdict on 30 January 2017. Michael Bancroft, Mark Dobson and David Mills were convicted on all counts. Anthony Cartwright was convicted on counts 4 and 6 and Alison Mills was convicted on Count 6.

Sentencing

2.36 All six individuals were sentenced on 2 February 2017 and received the following sentences in total: David Mills – 15 years; Lynden Scourfield – 11 years and three months; Michael Bancroft – 10 years; Mark Dobson – four and a half years; Anthony Cartwright – three and a half years; and Alison Mills – three and a half years.

2.37 In his sentencing remarks on 2 February 2017, His Honour Judge Beddoe summarised the case in the following terms:

> "…It primarily involves an utterly corrupt senior bank manager letting rapacious, greedy people get their hands on a vast amount of HBOS' money and their tentacles into the businesses of ordinary decent people – in the cases certainly of Theros, Remnant and Simon Jay - and letting them rip apart those businesses, without a thought for the lives and livelihoods of those whom their actions affected, in order to satisfy their voracious desire for money and the trappings and show of wealth.
>
> The corruption, which profited mostly the first three defendants [David Mills, Lynden Scourfield and Michael Bancroft] subsisted for at least four years. It involved Lynden Scourfield engaging in as extensive an abuse of position of power and trust as can be imagined and was motivated on both sides of the corruption by the expectation of, and the very considerable realisation of, immense financial gain. That was at the cost of enormous losses to BoS of some £245 million [gross], but also and, in many respects worse, the destruction along the way of the livelihoods of a number of innocent hard-working people. Some of these connections were capable of rescue but what Lynden Scourfield let happen through David Mills and Michael Bancroft predominantly ensured that they would not.
>
> The harm for which you were individually and collectively are responsible can of course be quantified in cash terms, but cannot be so in human terms. Lives of investors, employers and employees have been prejudiced and in some instances ruined by your behaviour. People have not only lost money, but in some instances their homes, their families, and their friends. Some who would have expected to be comfortable in retirement were left cheated, defeated and penniless…"

IV THE AFTERMATH OF THE TRIAL

2.38 Apart from the establishment of the Customer Review there were two significant developments following the conclusion of the criminal trial.

The FCA final notice

2.39 On 20 June 2019, the FCA issued BOS with a final notice by which it fined it £45.5 million for contravening its obligations to be open and cooperative with the regulator. The period of contravention was from 3 May 2007 to 16 January 2009.

2.40 The FCA stated in the final notice that during that period, BOS failed to disclose information to the FSA appropriately in relation to its suspicions that fraud may have taken place within IAR. The FCA noted that by 3 May 2007, BOS had identified suspicious conduct, including suspicions of fraud. On a number of occasions between May and January 2009, internal reports within BOS referred to the issues that had been identified as the "Reading fraud". However, it was not until July 2009, and after BOS became part of the Bank, that BOS provided the FSA with full disclosure in relation to its suspicions and the report of the investigation that it had conducted.

The Dobbs Review

2.41 On 26 April 2017, the Bank announced that it had appointed Dame Linda Dobbs DBE:

> "as the independent legal expert to consider whether the issues relating to HBOS Reading were investigated and appropriately reported to authorities at the time by [the Bank], following its acquisition of HBOS."[10]

2.42 The Dobbs Review is tasked with assessing whether, in the "relevant period":

(1) matters which the Bank knew or which it should have known about through reasonable diligence, and which, if properly investigated, might have led to evidence of fraud and/or corruption, were properly investigated; and

(2) information suggesting fraud and/or corruption, which the Bank knew or which it should have known about through reasonable diligence, were appropriately reported to the police and/or the FSA and its successors (the FCA and the Prudential Regulation Authority).[11]

2.43 The relevant period is from 19 January 2009, when the Bank acquired HBOS, to 30 January 2017, when the verdicts in the criminal trial were returned.

2.44 The scope of the Dobbs Review includes an assessment of whether any individuals within the Bank deliberately sought to supress or cover up information relating to the issues at IAR.

2.45 The Dobbs Review is ongoing. Questions as to the Bank's inquiry into the IAR fraud and whether the Bank covered it up are for that review. They are not within the scope of my review and I am unable to address them. It would be wrong for me to trespass in any way onto Dame Linda's investigations, or to anticipate her findings. My task is to review the Customer Review. So let me turn to a description of the establishment and methodology of the Customer Review.

[10] LBG press release dated 26 April 2017.
[11] www.dobbsreview.com

CHAPTER 3 THE CUSTOMER REVIEW: FIRST STAGES

3.1 Immediately after the trial, in February 2017, the Bank established the Customer Review, it told me, to ensure "that customers were treated fairly, given the unique circumstances surrounding the conviction of the two former employees and others."

3.2 It was intended, the Bank said, as a voluntary process designed to be without prejudice to both sides should the customer choose to leave it without accepting an offer. The customer could then choose to undertake civil litigation. The Bank told me that the voluntary nature of the Review was an important protection for customers and:

> "an important design principle in the information gathering approach and the ability for documents to be considered in assessment without the need to pre-empt potential disclosure considerations in later litigation."

I ESTABLISHING THE CUSTOMER REVIEW

3.3 The broad contours of the Customer Review were put in place over the period from early February to late April 2017.

Customer Review announced: those affected by IAR criminal activity

3.4 The Bank announced the establishment of the Customer Review on 7 February 2017. The press statement said that the Bank would undertake a review of all those customer cases:

> "which might have been affected by criminal activities linked to the former Halifax Bank of Scotland (HBoS) Impaired Assets Office based at Reading ('IAR')".

3.5 Customer cases would be considered afresh in light of all relevant evidence, including that which emerged at the trial. The press statement expressed deep regret for the distress the IAR fraud caused to a number of HBOS business customers.

3.6 In consultation with the FCA, the press release stated, an independent third party ("the independent reviewer") would be appointed as part of the Customer Review, with whom the Bank would agree its scope and methodology and individual case outcomes.

3.7 Relevant customers would be contacted, but those who believed they may have been affected could also raise concerns directly. Customer cases to be reviewed included, the press release continued:

(i) those cases referred by the convicted former HBOS employees to QCS;

(ii) customer cases that involved or were managed by QCS; and

(iii) all previous and any new customer complaints regarding the convicted former HBOS employees and/or QCS services as they related to IAR.

Consultation on Customer Review's working

3.8 Some three weeks later, on 27 February 2017, the Bank wrote to a number of high-profile IAR-affected customers to invite them to meetings with the Bank, to discuss how the Customer Review process might work. That included what they hoped the Customer

Review would consider and how it might work. Several meetings were held in early March 2017.

3.9 The Bank told me that a variety of views were expressed at the meetings which were helpful to it in the design of the Customer Review, particularly in relation to the way in which customers would interact with it and the Independent Reviewer.

Announcement of Professor Griggs' appointment

3.10 On 20 March 2017 the Bank announced that Professor Russel Griggs OBE had been appointed as the Independent Reviewer. The press release stated that he had been selected for his experience in overseeing high-profile reviews, his clear understanding of SME businesses and his track-record in ensuring that principles of fairness were followed in previous joint Government, banking and industry initiatives. That track-record included his appointment as the Independent External Reviewer in 2011 to the SME Appeals process set up to consider credit applications which had been declined, and his chairmanship of the CBI's UK SME Council from 2017 to 2010.

3.11 The press release referred to Professor Griggs' role as follows:

> "The role of the Independent Reviewer will be to agree the scope, methodology and individual case outcomes of the review in order to ensure fair outcomes and that the review is undertaken effectively."

3.12 In concluding, the press release stated that the Bank would now work with Professor Griggs to agree the methodology of the Customer Review. The intention was to commence the formal review of customer cases in short order so that customers could receive an outcome as quickly as possible.

Redress c£100m for "impacted customers"; professional fees, interim support, debt (mortgage) relief

3.13 There was a further press release on 7 April 2017. It noted that the Bank was working at pace with Professor Griggs to ensure appropriate redress was provided to "impacted customers". The Customer Review was in its initial stages, it said, but to provide additional help to those customers, the Bank would:

> "Provide interim payments on a case-by-case basis to assist victims in financial difficulty with day to day living costs;
>
> Cover reasonable fees for professional advice whilst in the Professor Griggs' review [sic] to enable customers to access appropriate legal and financial advice;
>
> Write off customers' remaining relevant business and personal debts currently owed to [the Bank], where they were victims of the criminal conduct, and not pursue them for any repayment."

3.14 The press release added that the Bank:

> "currently anticipates that compensation for economic losses, distress and inconvenience will be in the region of £100 million..."

3.15 There were then quotations in the press release from the chief executive and the chairman of the Bank, expressing deep regret to the customers affected. The chief executive added:

> "We are absolutely determined that victims of the crimes committed at HBOS Reading are fairly, swiftly and appropriately compensated. We take responsibility for putting right the wrongs that were committed at HBOS Reading at the time."

Expected timetable

3.16 There was a further update press release dated 26 April 2017, under the heading "Timetable for customer compensation". It noted that Professor Griggs had formally commenced his appointment. It observed that the Bank had announced on 7 April that there was a £100 million provision for estimated compensation to 64 customers.

3.17 The press release added that it was the intention of the Bank and Professor Griggs to begin making compensation offers from late May onwards.

II REVIEW POPULATION: BUSINESSES

3.18 In broad terms, the Bank told me, it sought to identify customers for the Customer Review on the basis of their proximity to potential detriment as a result of the criminality established at the trial.

3.19 To do this the Bank used three cohorts to define the Customer Review population of businesses, in other words, those falling within the scope of the process. Regardless of which cohort they fell into, the Bank assured me, all customers in the Customer Review population were assessed using the same methodology throughout the process.

The three cohorts

3.20 The methodology defined the review population as those customers managed within the former HBOS IAR within the relevant time period and falling into three cohorts:

> Cohort 1: Customers managed by Lynden Scourfield and/or Mark Dobson who were referred to QCS;
>
> Cohort 2: Customer cases involved with or managed by QCS, or which had any other involvement with QCS and/or David Mills and/or the other convicted individuals (Michael Bancroft, John Cartwright or Alison Mills), regardless of the proximity of Lynden Scourfield and/or Mark Dobson;
>
> Cohort 3: All previous and any new customers who had complained, which met one or more of the scoping criteria, if the complaint was received during the course of the Customer Review, regarding the conduct of Lynden Scourfield and/or Mark Dobson and/or QCS and/or David Mills as it related to IAR.

Details of the cohort methodology

3.21 According to the population methodology, the following customers were considered to fall within the Customer Review ("the Customer Review population"):

"those referred by the convicted former HBOS employees to Quayside Corporate Services Limited (QCS);

those involved with or managed by QCS;

those who have complained about the convicted former HBOS employees and/or QCS in the context of HBoS IAR".

3.22 The "Design Principles" expand on this:

(1) The Customer Review was to cover the period when "Lynden Scourfield was based in HBOS IAR to the end of the indictment period used during the criminal trial", being the period during which "LBG considers the conduct of the former convicted employees and/or QCS and/or David Mills potentially leading [sic] to the unfair treatment of the customers of the former HBoS IAR".

(2) The Review Population was to be "determined by whether the customer was referred to and managed by the former convicted employees of HBoS IAR and/or whether the customer had involvement with either QCS and/or David Mills and/or other convicted individuals (Michael Bancroft, John Cartwright or Alison Mills)".

(3) LBG would proactively contact individuals and entities with whom QCS and/or David Mills were known to be involved, and they would be "considered eligible for inclusion in the review".

(4) Any entities (and individuals associated with them) proven to be involved in the criminal conduct in the criminal proceedings would be excluded from the Customer Review (the population methodology lists these entities and individuals).

3.23 The population methodology divided the Customer Review population into the three cohorts which I set out above. However, it goes on to state that: "Customers not referred to QCS or those that were not managed by the convicted former HBoS employees Lynden Scourfield and/or Mark Dobson" would not be considered in scope for the Customer Review. I read this as saying that customers who were neither referred to QCS nor managed by Lynden Scourfield and Mark Dobson would not be considered in scope for the Customer Review.

Explaining the three cohorts

3.24 The Bank explained the three cohorts to me in this way.

Cohort 1: managed by Scourfield/Dobson and QCS

3.25 The Bank explained Cohort 1 to me as capturing those customers where there was the same connection between Lynden Scourfield and/or Mark Dobson and the QCS criminals as required for the existence of the criminal conspiracy evidenced at trial. It was in effect a subset of Cohort 2.

Cohort 2

3.26 Cohort 2, the Bank said, was because any contact with QCS was considered to be a potential indicator of detriment, regardless of the direct involvement of the criminal bankers. That was because of the findings in the trial against the principals of QCS.

3.27 The rationale of cohort 2 was that since QCS, David Mills and his associates were the perpetrators of the fraud, any Bank customer involved with them was a victim and ought to be within the Customer Review. That of course did not include the perpetrators themselves or those associated with them. Without QCS involvement, or the involvement of those associated with it, customers did not fall within the Customer Review unless they were within cohort 3, in other words, had complained.

Complaints and cohort 3

3.28 The Bank described the addition of cohort 3 as a safety net for customers to self-identify for inclusion in the Customer Review population. This was for those not captured in Cohorts 1 and 2, but who may have been exposed to the convicted bankers. Cohort 3 potentially extended the Customer Review to include customers without any QCS involvement if managed by Lynden Scourfield or Mark Dobson.

3.29 The intention of cohort 3 was that those customers could have their complaints reviewed to identify if any detriment had been suffered from these dealings. The Bank told me that cohort 3 was important since it had identified:

> "that there was no single "golden source" that definitively confirmed all connections referred to QCS or that were managed by the convicted ex HBOS employees over time."

3.30 The Bank divided those in cohort 3 into historic and new customers. Historic complaints were those which had been received before the public announcement of the Customer Review and which made reference to: (i) IAR; (ii) the conduct of Lynden Scourfield and/or Mark Dobson; or (iii) the involvement or conduct of QCS.

3.31 In respect of new complaints, the Bank said that it gave consideration to: (i) evidence that the customer was managed by IAR or other IA teams in HBOS; (ii) claims that the customer was affected by QCS' conduct; and (iii) claims that the customer was affected by Lynden Scourfield's or Mark Dobson's conduct during their time managing IAR.

Period covered

3.32 The Customer Review was to cover the period when Lynden Scourfield was based in IAR to the end of the period used in the indictment in the criminal trial, in other words between Q3 2000 and 30 September 2010. The Bank told me that it used this period since it considered that it was then that the conduct of Lynden Scourfield and Mark Dobson and/or QCS and/or David Mills potentially led to unfair treatment of IAR's customers.

3.33 As to customer complaints, the Bank generally excluded complaints about the conduct of HBOS employees after 19 January 2009, which was the date on which the Bank took over and IAR ceased to exist.

III REVIEW POPULATION: DIRECTORS

3.34 The Bank explained to me the rules it had for individuals to be admitted into the Customer Review. These were the directors of the businesses which fell within the Customer Review.

Directors

3.35 The Bank decided that all directors in office at the time a business was first referred into IAR would be eligible to participate in the Customer Review. Its rationale was that, as office holders, they were most likely to have had dealings with the convicted criminals.

3.36 The Bank's policy was that directors could self-identify for inclusion in the Customer Review population. If they had been exposed to Lynden Scourfield or Mark Dobson when their business was in IAR, they were invited to participate in the Customer Review. Where there was evidence that the individual was a director of a business at the time it was referred to IAR, and they had dealt with Lynden Scourfield or Mark Dobson, they were deemed eligible for inclusion in the Customer Review. As such, an involvement with QCS was not a pre-requisite.

3.37 The Bank took the view that applying its rules across all these businesses provided a list of directors which it considered would have faced unfair treatment as a result of the conduct of Lynden Scourfield or Mark Dobson and/or QCS and/or David Mills and his associates.

Excluded directors

3.38 Not all directors of businesses who came within the definition of the Customer Review population qualified for entry into the Customer Review. Rules 1 and 2 excluded certain directors associated with QCS and nominee company directors respectively.

3.39 Rule 3 excluded:

(i) directors who resigned before a business' entry into IAR; and

(ii) directors who started in office after its entry into IAR.

De facto directors

3.40 De facto directors are those occupying the position of director, but not appointed as such.[12] There is no single definitive test for de facto directorship. The essential question is "how was the company actually run?"[13]

3.41 In its methodology the Bank accepted that some individuals may appear in its records as directors but may not have been formally appointed. The methodology provided that, in such circumstances, the following points would be considered in determining whether such a person should be included in the Customer Review population:

[12] Companies Act 2006, section 250.
[13] *Smithton v Naggar* [2014] EWCA Civ 939; [2015] 1 WLR 189.

"(i) Is there evidence in the Bank's records that they were consistently referred to or treated as directors? (For example, the individual is referred to as a director in a credit report prepared by the Bank).

(ii) Is there consistent evidence that the individual(s) were involved in the running of the business such that they were effectively discharging the role of a director? (For example there is evidence of the individual making decisions on behalf of the business.)

(iii) Is there evidence of impact on the individual following interactions with QCS/IAR?"

3.42 However, it noted that "none of these conditions are considered sufficient in their own right to necessitate an individual being invited into the [Customer] Review or for them to be assessed for D&I". The circumstances pertaining to each individual had to be considered. The methodology stated that "where the pattern of facts indicates that an individual was treated commensurate to being a director and may have suffered D&I [distress and inconvenience], a decision will be taken on whether or not they will be assessed for D&I and an outcome will be communicated to them."

3.43 Assessors working on the Customer Review were responsible for highlighting individuals who could potentially fall into the category of de facto directors. It was for the QC Panel (described below) to decide whether or not the individuals in question were to be included in the Customer Review population. The population methodology provided that where an individual stated to the Customer Review that they were a de facto director, the Bank was to assess their case in the same way as individuals highlighted by the assessors as potential de facto directors.

3.44 In its methodology for assessing compensation for D&I, the Bank stated that:

"…consideration will also be given to circumstances where an individual was not formally appointed as a director but may have actually been acting as a director in the eyes of [the Bank] (i.e. a de facto director). In circumstances where it has been established that the individual was treated by [the Bank] as acting as such, he/she will be assessed on the same basis as if he/she was formally appointed."

3.45 In its submissions to my review, the Bank further explained that:

"The decision on whether a customer was or was not held to be a de facto director was based on the contemporaneous evidence. This was not confined to evidence on the Bank's file and any contemporaneous evidence provided by customers, relevant to the three questions set out in the methodology, was given due weight. As a point of factual interpretation, this is different to our assessment of D&I, where customers' submissions were taken at face value in the absence of contradictory contemporaneous evidence."

3.46 The Bank told me that in the Customer Review it accepted five de facto directors, but seven persons claiming to be a de facto (or shadow) director were rejected.

Exclusion of shareholders/creditors

3.47 Those who were not directors of businesses in the Customer Review were excluded from its population and thus from eligibility for compensation. That included shareholders of a business if they were not one of its directors. Creditors were also excluded.

Exclusion of those associated with QCS

3.48 Individuals and businesses were to be excluded from the Customer Review if they were established at trial to be associated with the criminals.

3.49 That policy produced a list of four key individuals (David Mills, Michael Bancroft, John Cartwright and Alison Mills) and of another 14 individuals associated with QCS. In addition there was a list of 16 businesses owned by David Mills and/or other related QCS individuals which were to be excluded from the Customer Review.

3.50 During the course of the Customer Review, the Bank also concluded that in two instances a director had acted in such close proximity to QCS that they were ineligible for D&I compensation. In those two cases, the Bank said, it had assessed claims for direct and consequential ("D&C") loss in the normal way and concluded that this also was not recoverable.

Directors removed as not in scope

3.51 The Bank told me that three directors were removed from the Customer Review population since they were not within its scope. In one instance the director was not a customer of HBOS. In the other two cases the Bank's initial assessment was that they did not satisfy the rules to fall within the review population.

IV FINDING THOSE WITHIN REVIEW POPULATION

3.52 Once the Bank had defined the Customer Review population, it told me that its design principle was to "cast our net as wide as possible". The Bank developed a detailed methodology for finding these customers.

Sources of information

3.53 The Bank explained to me that it used three broad categories of information to locate the businesses and individuals who met the definition for inclusion in the Customer Review.

3.54 First, there was the information from internal Bank sources. That included invoicing and accounting records and QCS bank account transactions; the peer credit review conducted in 2007; and an internal investigation by the Bank Support Unit in 2011. Secondly, there was information from external sources, including the skilled person's report, the Thames Valley Police, Companies House, trial transcripts and evidence. Thirdly, there were customer complaints and litigation threatened prior to the establishment of the Customer Review.

3.55 With respect to QCS invoices, the Bank told me that although these were frequently paid centrally via HBOS Accounts Payable, they could also be paid directly by IAR or by the

company with no involvement of HBOS. Thus, with one business in the Customer Review, the Bank said there was no evidence suggesting that the involvement of QCS was a result of a referral by HBOS. There were also examples in the Customer Review population where businesses were not managed in IAR but still had QCS involvement.

Complainants

3.56 During the course of the Customer Review, the Bank said, 82 individuals contacted it about HBOS Reading and requested their inclusion in the Customer Review.

3.57 20 of these 82 were received into cohort 3. Of the remaining 62, 19 were associated with businesses already included in the Customer Review; nine were former directors proactively invited under cohort 1 or 2; 10 were associated parties (not directors) and therefore not within the scope of the Customer Review; 18 were individuals who were not corporate banking customers; 16 were corporate banking customers who were not involved with IAR and had no QCS involvement; five were corporate banking customers involved with IAR, but not managed by Lynden Scourfield or Mark Dobson, nor involved with QCS; one was a corporate banking customer historically managed by Mark Dobson but not in IAR; and three were former Bank employees.

3.58 No involvement of QCS was found for any of those accepted into the Customer Review as part of the Cohort 3 approach. They were all effectively complaints about the conduct of Lynden Scourfield or Mark Dobson.

3.59 When not accepted into the Customer Review, the Bank told me that it handled complainants through the Bank's "business as usual" complaints procedure.

Identifying the Customer Review population

3.60 Prior to reviewing any files, the Bank told me that it used Companies House to identify all related companies (subsidiaries, holding companies etc.) and the corresponding directors of the customers it identified.

3.61 This gave 208 businesses and 680 directors (excluding nominee companies). In the first instance the Bank decided to contact those individuals who were active directors at the time a company was first referred to IAR.

3.62 There were therefore 219 individuals to contact. Five of these had indicated that they would pursue other remedies before invitations to participate in the Review had been sent. That left 214 individuals.

3.63 However, that number reduced since there were: (i) those who could not be traced; (ii) non-responders; (iii) those not in scope; and (iv) those choosing not to enter or to leave the Customer Review.

Tracing activities

3.64 The Bank told me that, in the event that its letters were not responded to, it engaged the services of two external "trace providers". The Bank has told me that it had three distinct levels of trace activity. With level 1, the initial tracing consisted of electronic and

physical search activities to locate the customer. This level of search was initiated 28 days after the final reminder letter. Level 2 involved a manual exercise undertaken on an individual basis, with the results typically becoming available after five weeks.

3.65 The Bank has told me that level 1 and 2 traces were conducted in parallel and if these trace activities did not result in a customer being successfully contacted, the tracing activity was escalated to level 3, which involved an in-depth investigation into the respective customer's whereabouts.

3.66 The Bank told me that in the event that any of these trace activities positively identified new contact details it recommenced the initial contact process and the customer then progressed through the Customer Review in the ordinary course.

3.67 In the event that these tracing activities were unsuccessful, the Bank told me that it made a final attempt to contact the customer by sending a letter by recorded delivery to the address it held.

3.68 If this letter was not responded to, the Bank deemed the customer: (i) as a "non-responder", whereby the tracing searches undertaken indicated that the address held on file or the newly-found address (obtained through the tracing searches undertaken) was correct; or (ii) as "not found", whereby the tracing searches were unable to confirm the correct address for the customer.

3.69 There were two cases where the Bank, having exhausted all tracing attempts, regarded the customer as not found.

Non-responders

3.70 There were 13 persons in this category. In these cases an address was confirmed but the Bank was unable to evoke a response from them. These directors were eventually removed from the Customer Review population.

Choosing to leave/not to enter Customer Review

3.71 There were five directors from two businesses who were in the Customer Review but chose to leave. All five reached a settlement with the Bank through negotiation or mediation.

3.72 There were two directors of the one business who chose not to enter the Customer Review, although they were within its scope. They also reached a settlement with the Bank through mediation.

The result: Customer Review population

3.73 Taking these four categories into account, the Bank's final population for the Customer Review consisted of 191 directors from 71 businesses.

3.74 The breakdown by cohort was as follows: cohort 1 – 21 businesses, 80 directors; cohort 2 – 30 businesses, 70 directors; and cohort 3 – 20 businesses, 41 directors.

V CONTACTING THOSE WITHIN THE SCOPE OF THE CUSTOMER REVIEW

3.75 The Bank's press release of 20 March 2017 recorded that it had written to the majority of customers within the scope of the Customer Review, but that other customers who had raised concerns that they may have been affected by the IAR fraud would be considered for inclusion as well.

The Bank's initial letters

3.76 If their initial letter was not responded to the Bank, in the first instance, sent three letters to the customer to the address held on the Bank's records after pre-determined periods of time. The first reminder letter was sent two weeks after the initial letter; the second was sent one week after the first reminder; and the final reminder letter was sent one month after the second reminder.

3.77 These initial letters informed customers of the establishment of the Customer Review, gave the name of their Bank contact during the Customer Review process and asked for their preferred contact details.

3.78 From 21 April 2017 customers received more detail of the Customer Review in letters headed "Review of HBOS Impaired Assets Office in Reading ('the Review') – Next Steps" ("the Next Steps letter").

The Next Steps letter

3.79 At the outset, the Next Steps letter expressed the Bank's commitment to providing fair, swift and appropriate compensation for the victims of the IAR fraud, reiterated the Bank's regret and apologised.

3.80 The letter went on to describe how the Customer Review would consider direct financial losses and other impacts including distress and inconvenience ("D&I").

> "As the scope and methodology of the Review are agreed by Professor Griggs, we will make an assessment of the impacts on you and your business of the conduct of those now convicted of criminal offences. This assessment will include consideration of any direct financial losses as well as knock-on impacts including the distress and inconvenience that has been caused. The assessment process will consider all of the information available to us from our own records. We also recognise that you may have your own records and information that you want us and Professor Griggs to be able to take into account…"

3.81 The letter added that the Bank expected the assessment process to take around four weeks. It said:

> "Once we have received your input we expect the assessment process to take around four weeks. When this work has been completed and has been approved or amended by Professor Griggs, we will communicate the outcome to you and we will give you time to consider whether you want to arrange a meeting with the Bank to discuss it. Professor Griggs will also be available to attend should you wish him to do so."

3.82 Under the heading "How can you provide information for the Review?", the letter said that a key part of the Customer Review was "to fully understand your point of view and experience in relation to your interaction with the Impaired Assets Office in Reading, and the impact of the criminal activities on you and your business."

3.83 The letter then invited recipients to provide information in the form of a questionnaire, to be returned within 28 days if possible. If the addressee preferred a meeting, it said, arrangements could be made for that. If the person did not want to provide any additional information, the Bank could make an assessment on the basis of information already held on file.

3.84 For the purposes of the Customer Review the Next Steps letter identified a relationship manager, along with the relationship manager's contact information.

3.85 The letter stated that it anticipated that recipients might want to take legal advice, and stated that the Bank would meet reasonable costs in this regard.

Customer questionnaire: introduction

3.86 While the Bank accepted information in whatever form customers wished, they were provided with a Customer Questionnaire to complete.

3.87 The questionnaire began with the Bank's commitment to providing fair, swift and appropriate compensation for the victims of the IAR fraud. It added that a key part of this was to understand the individual's point of view and experience in relation to interaction with IAR and the impact of the criminal activities on them and their business. If they held any documents or information which should be considered alongside the answers in the questionnaire, these could be submitted at the same time.

Customer questionnaire: the details

3.88 Section 1 of the questionnaire concerned guidance on its completion. Section 2 invited requests "for legal/professional fees to be paid" and for a face to face meeting to discuss the case.

3.89 In section 3, basic information was sought on the company and the individual completing the questionnaire. One question in this section concerned the title the individual held with the company or their relationship to the company "(e.g. Director)".

3.90 Section 4 requested further information about the company, its current status and its directors during its time in IAR. The section also asked whether there were other individuals the Bank should contact regarding the company.

3.91 There were then sections requesting details of: (a) interactions with IAR and those convicted in the criminal trial (who were individually named) (section 5); (b) interactions with QCS and those employed by it, what they did, and how these interactions could be described (section 6); and (c) details of the financial impact of the interactions with IAR and QCS, and of the personal impact (section 7).

3.92 Section 8 dealt with whether there had been a complaint to HBOS or the Bank, or legal action regarding IAR. There were then questions in section 9 about further information

which the customer would like to provide and whether they would like to meet Professor Griggs either at that point or in the future. Section 10 asked for confirmation about the customer's willingness to be included in the Customer Review.

VI FINANCIAL ASSISTANCE TO CUSTOMERS

3.93 The Bank's press release of 7 April 2017 announced, as mentioned earlier, that as part of the additional help to customers in the Customer Review it would make interim payments, cover reasonable fees for professional advice and write off debts to the Bank. Then in late June 2017 it announced ex gratia payments of £35,000 to each of those in the Customer Review.

Legal assistance

3.94 The 7 April 2017 press release had announced "reasonable fees for professional advice, […]to enable customers to access appropriate legal and financial advice." The Next Steps letter of 21 April 2017 referred to reasonable costs for legal assistance. Section 2 of the Questionnaire invited requests for legal/professional fees to be paid.

3.95 In practice, the Bank informed me, it funded legal support to customers (i) in preparing their submissions to the Customer Review; (ii) as regards "additional information" submissions (see below); and (iii) in obtaining advice on their settlement agreements prior to accepting an outcome.

3.96 For legal assistance the Bank told me that it paid an amount in excess of £4.6m ranging from less than £15,000 to some £335,000 for a single company. For one individual it paid in excess of £269,000.

3.97 In terms of numbers, 136 out of 191 customers obtained legal assistance. 59 customers appointed advisors after receiving their first outcome letter. The Bank expressed its view that the amount billed by lawyers in individual cases did not necessarily reflect their complexity.

3.98 The Bank told me that it paid over £0.5m to a claims management company which represented a small number of customers in the Review.

Financial advice

3.99 The Bank told me that there were 10 individuals across eight companies where it agreed to pay fees for financial advice. Financial advice cost approximately £80,000 in total. The Bank said that decisions to fund financial advice were based on the rationale provided by customers or their advisors.

Writing off customers' debts (mortgages)

3.100 As stated in its press release of 7 April 2017, the Bank decided that for those in the Customer Review it would write off and not pursue customers with remaining relevant business and personal debts owed to the Bank.

3.101 In all this this comprised 11 mortgages, one personal debt, one credit card debt and one business debt (including personal guarantees and commercial mortgages).

3.102 The mortgage debts ranged from less than £50,000 up to over £850,000. In eight of the mortgage cases there was no record of any recovery action having been taken, but in the other three cases recovery action had been commenced in relation to both the mortgage and personal guarantee. Recovery action had also been commenced with the personal debt (of some £30,000), the credit card debt (of some £12,000) and the business debt (of some £1.2 million, in relation to both the personal guarantees and commercial properties).

Interim payments

3.103 The Bank's Next Steps letter had offered interim payments on a case-by-case basis to assist victims in financial difficulty with their day-to-day living costs. Customers were not expected to prove that their financial hardship had been caused by involvement with the IAR.

3.104 The Bank told me that other than seeking to confirm the customer's income (where not provided), it accepted the customer's account of their needs. Occasionally, however, it sought a further explanation.

3.105 The Bank informed me that some £650,000 was paid as interim payments to 28 individuals in the Customer Review on an ex-gratia basis. The highest amount received by an individual was in excess of £121,000.

3.106 In addition some £580,000 was paid to 13 individuals as interim payments which were later offset against distress and inconvenience awards. In such cases the highest amount received by an individual was in excess of £202,000.

£35,000 ex gratia payment

3.107 In a press release on 30 June 2017 the Bank announced that all customers participating in the Customer Review were being offered an ex gratia payment of £35,000. This was on a "no admissions" basis. Payment would be made irrespective of whether or not customers would go on to accept any compensation offered. Payments were made retrospectively for those who had already accepted an offer. The Bank stated that the payment was to reflect the fact that the Customer Review was taking longer than expected.

3.108 A total of 181 out of the 191 individuals in the Customer Review received the £35,000 payment. Of those who did not receive a payment, nine had chosen to opt out of the Customer Review. The remaining case was a former director with whom contact was never established. A total of £6.3 million was paid.

CHAPTER 4 COMPENSATION: THE BANK'S METHODOLOGY

4.1 Once the Bank had established the Customer Review population, it had first to gather information about the companies and directors who fell within it. It then had to develop a methodology for calculating the compensation to be offered to customers. Customers were to have an input into the process, and the Bank needed to structure how this was to occur. There was also Professor Griggs' role in the assessments to be factored in. Once the Bank made an offer, with Professor Griggs' approval, it had to decide how challenges to that would be dealt with.

I GATHERING INFORMATION

4.2 The Bank explained to me the process of how it gathered information for the purposes of assessing cases in the Customer Review.

The Bank's approach

4.3 Case files were assembled by undertaking a series of searches of the documentation which had been collated and preserved by the Bank prior to the commencement of the Customer Review. That documentation had been assembled for the internal and external investigations leading to the criminal trial. Boxes of archived materials were searched. Requests were also made for specific information from, for example, former IAR staff.

4.4 Hard-copy files were augmented by searches of electronic files. The Bank told me that this included emails, laptop imaging and copies of four shared drives used by IA teams in Reading and Edinburgh, together with the materials shared with Thames Valley Police as part of their criminal investigation.

4.5 The Bank acknowledged the limitations to their information gathering. For example, it explained to me that because the IAR fraud occurred before retention of documents was mandatory, its electronic files were sometimes lacking structure and content. As well, its aim of providing swift outcomes to customers meant that it could not always be exhaustive in the searches it undertook.

4.6 The Bank expressed the view that, notwithstanding these limitations, it was confident that, when coupled with what customers provided, it had a sufficient level of information to reach fair and reasonable outcomes for customers.

Additional document searches

4.7 The Bank told me that it envisaged at the outset that the files built in accordance with its "file build" process would be sufficient and it expected that additional, electronic searches would be conducted on an exceptional basis.

4.8 However, it found it necessary with 39 of the 71 businesses in the Customer Review to conduct additional searches of electronic files. The reasons for this varied. However, the main reason was that the customer's account conflicted with that in the file and it was hoped that the further search might clarify matters.

II CASE ASSESSMENT: THE BANK'S APPROACH

4.9 The Bank developed a standardised system for calculating compensation in individual cases. This involved a template to be used by assessors to ensure accuracy and consistency in individual cases. Steps were also taken to check the individual casework of assessors.

The assessment template

4.10 The Bank developed a detailed assessment template, containing a large number of questions, to be completed by the assessors for each customer in the Customer Review.

4.11 The template was devised, the Bank said, to consider:

(i) the reasonableness of actions for a company which were taken or recommended by IAR and/or QCS, in the context of usual corporate turnaround activities; and

(ii) the level and nature of interaction an individual may have had with IAR and any resulting impact or detriment incurred.

4.12 Against the questions, whether in relation to the reasonableness of actions or the level and nature of interactions, assessors had to set out the reasons for their assessment and refer to the key documents they relied on. Missing or incomplete information had also to be noted.

4.13 According to the Bank, the need to produce expeditious outcomes meant adopting a simple "red flag" approach to assessment, rather than conducting a full forensic analysis. A high (or red flag) rating in response to any question was taken to indicate a higher likelihood of impact on or detriment to the customer. The Bank said that it accepted a degree of subjectivity in the assessors' responses to some questions.

Reasonableness of actions vis-a-vis a business

4.14 As regards (i) above, reasonableness of actions, the Bank explained that, where conduct did not at face value follow expectations, or could not be reasonably explained, further work was undertaken to determine whether the conduct was appropriate, and whether it led to losses which would not otherwise have happened.

4.15 In this regard the issue, the Bank said, was the basis upon which customers were referred to or entered into IAR. In the first instance the focus was to examine (a) the financial status of the company at the time of entry into IAR; (b) the appropriateness of the company's entry into IAR; (c) the company's treatment while in IAR and during turnaround activities involving QCS; and (d) the identification of a company's other creditors.

Referral to IAR

4.16 The Bank told me that, during the Customer Review, assessors evaluated the appropriateness of the transfer of a customer into IAR by giving particular consideration to a customer's financial status at the time of its entry and other relevant circumstances. Each customer was considered on a case-by-case basis rather than against any policy.

Level and nature of interaction with IAR and QCS

4.17 In terms of assessing the conduct of IAR and the convicted criminals in their dealings with companies, the Bank explained that its template was designed to assess the level of interaction an individual may have had with (a) IAR, or (b) QCS.

4.18 Interaction with IAR was considered by reference, in particular, to the frequency, nature and timeframe of its involvement in running the business. Direct involvement with Lynden Scourfield or Mark Dobson was also explored, and whether as a result there was any undue pressure exerted, including to work with QCS, and the effect of such pressure on the individual's decision making.

4.19 In considering interaction with QCS, the template sought to encompass all employees or consultants of QCS, whether convicted at trial or not, as well as all of David Mills' employees. The template aimed to capture the frequency, nature and timeframe of a customer's interactions with QCS individuals, together with any pressure which they brought to bear (including its effect).

4.20 The Bank told me that, under this part of the template regarding the level and nature of IAR and QCS interaction, "the principal head of loss considered was distress and inconvenience".

III CASE ASSESSMENT: THE MACHINERY

4.21 The Bank informed me that the Customer Review was managed through a special sub-committee of the Bank's Risk Committee and had cross-representation at a senior level. Day-to-day responsibility was assigned to a designated senior executive at the Bank. Monthly updates were provided to the Bank's executive board and the Bank's regulators. Operationally, the Bank's case review team consisted of assessors, internal legal advisors and compliance experts. There were conflict of interest checks to ensure that they had no connection to IAR, or any customer participating in the Customer Review.

Relationship managers

4.22 Customers invited to participate in the Customer Review were assigned a designated relationship manager who would be their primary contact at the Bank and guided the Customer through the Customer Review and attended to logistical matters (such as organising meetings and taking notes), but who would not form part of the team reviewing and assessing the customer's case.

Case assessors

4.23 For the purposes of the Customer Review, the Bank formed a team of what it described to me as experienced turnaround bankers, who had served in its Business Support Unit or the unit's predecessors. The Bank explained that these case assessors had a wide experience and expertise in dealing with financially distressed businesses and so were able to provide an expert opinion on the reasonableness of turnaround strategies and actions, and the fair treatment of customers in these circumstances.

4.24 The Bank told me that all case assessors were vetted for conflicts of interest and received training in the methodology that it had developed to determine compensation. Case assessors made decisions on the application of the methodology in individual cases without knowing what this meant in terms of particular amounts. It was the function of senior case assessors to collate this assessment with other information and to present a proposal to the Quality Control Panel for its agreement.

Compliance standards

4.25 Alongside the bankers, the Bank explained, were in-house lawyers and compliance officers.

4.26 As to its compliance officers, the Bank told me that they assessed cases under the FCA standards "Treating Customers Fairly" and "Customers in Financial Difficulty". In doing so it particularly focused on the degree of any "intrusion" (e.g. the instigation of independent business reviews; enforced board appointees); duration of engagement with Lynden Scourfield, Mark Dobson or QCS; degree of transparency and openness by IAR; "tone" of any discourse with company principals; existence of undue pressure; management of any conflicts of interest; and HBOS' response to any previous complaints.

Governance of outcomes

4.27 The Bank told me that it put in place several layers of governance so it would reach for each case fair and reasonable outcomes for customers.

4.28 First, at the case assessment level there was so-called "four eyes" checking of calculations, where a second review of each case file was conducted by a different assessor. Given the experience built up in assessing cases, the Bank abandoned four eyes checking on 1 August 2017, at the point when 55 of the 71 businesses had been assessed.

4.29 Second, the Bank conducted "case clinics", where initial findings and conclusions were presented by the various assessors and considered "in the round" for any detrimental impact on a customer.

4.30 Thirdly, assessors created a Quality Control ("QC") pack containing the analysis and the recommended outcome for each case.

4.31 That was considered by a QC Panel, the principal decision-making body made up of voting members from the business, compliance and legal parts of the Bank. The Bank told me that the Panel's task was to challenge the assessors where appropriate to reach a confirmed fair and reasonable outcome proposal for onward submission to Professor Griggs.

4.32 Fourthly, exceptional cases might be escalated to the Customer Review Steering Committee for ratification of outcomes, particularly where a proposed payment exceeded the delegated authority of the QC Panel.

IV COMPENSATION FOR D&I

4.33 A D&I payment was compensation payable to customers, calculated according to the Bank's own methodology. It fell outside ordinary legal principles applicable to the financial loss (both direct and consequential) which could be pursued through the courts.

4.34 To calculate D&I the Bank developed a matrix which enabled the application of set criteria in individual cases. The Bank stated that the matrix was designed to award compensation at up to twenty times what may be typically recoverable at law.

Rationale

4.35 The Bank told me that the D&I matrix was designed to provide an understanding of the engagement and interaction an individual had with Lynden Scourfield or Mark Dobson on the one hand, and with QCS on the other. Compensation flowed from this understanding.

4.36 The Bank said that the matrix was aimed at understanding how businesses were treated while in IAR, particularly whether actions taken during their relevant turnaround phase could be considered to have been reasonable (i.e. had they been taken by individuals other than the convicted criminals).

4.37 The Bank informed me that it had sought to identify whether the lack of integrity or honesty of Lynden Scourfield or Mark Dobson (when taking or recommending what could have been considered reasonable actions) may nevertheless have led to the unfair or unlawful treatment of customers, separately from any illegality identified as a result of the criminal prosecution.

Customer's account accepted

4.38 The default position was that in considering D&I the customer's account of events should be accepted unless there was express evidence to the contrary.

The D&I matrix

4.39 The D&I matrix had three categories for calculating compensation:

(i) category 1, which concerned direct involvement with Lynden Scourfield and/or Mark Dobson;

(ii) category 2, which concerned direct involvement of QCS; and

(iii) category 3, which concerned personal impacts.

4.40 Matrix scoring was based on the answers to the questions in the assessment template, together with the submissions customers provided.

4.41 In each category matters were then scored within the matrix: 0 = no involvement or impact; 1 = low involvement or impact; 2 = medium involvement, detriment or impact; and 3 = high involvement, detriment or impact. The Bank accepted that there was an element of judgment involved in the scoring.

4.42 Financial values were attached to these scores. A scalar was applied to differentiate between the amounts in categories 1 and 2 (x1.5) and those in category 3 (x3). The sum of the values made up the total D&I award.

Category 1 and introductions to QCS

4.43 The Bank informed me that, in mid-2017 after discussions with Professor Griggs, it decided that it was appropriate to assume that, where QCS were involved in a case, Lynden Scourfield and/or Mark Dobson were likely to have been involved, even if there was no evidence to support this.

4.44 Thus individuals scored a minimum of "1" for the matrix question "Decisions made on Lynden Scourfield and/or Mark Dobson advice and/or recommendation" even where there was no other interaction with those bankers.

4.45 Similarly, pressure on an individual to work with QCS was assumed where that organisation was introduced to the business. Hence individuals would also score a minimum of "1" for the matrix question "Undue pressure to work with QCS".

4.46 Under its consistency policy, the Bank applied these changes retrospectively. As a result, four directors who had already been assessed were offered additional compensation.

Introduction of "exceptional D&I" category

4.47 In July 2017, the Bank explained, it enhanced category 3 to recognise exceptional distress by introducing a new sub-category, "3B – Higher". All previous cases were re-evaluated against this new sub-category.

4.48 Exceptional personal impact was judged with regard to the following factors: (i) the individual had been publicly associated with the criminals; (ii) had the individual been persistently rebuffed in their pursuit of justice over many years; and/or (iii) the individual was subject to public disclosure of themselves or their company through the criminal trial.

4.49 Fourteen cases were awarded a 3B - Higher category award. As a result the Bank paid an additional £3.36 million in compensation.

Nil outcomes

4.50 "No redress" outcomes were issued to 36 individuals who scored a nil value on the D&I matrix, primarily because they were either not directors during the relevant period or the business was not managed in IAR.

V EXCEPTIONAL CASES

4.51 For a minority of cases, the Bank told me, it became evident that scoring against the D&I matrix alone did not reflect the unique and more serious characteristics of the detriment a customer had suffered. In these cases, it explained, customers provided additional information to demonstrate the existence of exceptional "aggravating factors".

4.52 The Bank said that the aggravating factors were specific to each case. There were no generic factors taken into account or criteria applied when assessing whether a case warranted an award outside the parameters of the matrix, although such cases were typically characterised by the customer's proximity to the fraudulent conspiracy and/or those convicted at trial, and were therefore vulnerable to influence and pressure. Overall, the Bank said, it attempted to capture the extreme and more serious nature of the circumstances of cases which the D&I matrix did not reflect.

4.53 The Bank gave me some examples of cases where it identified exceptional circumstances:

(i) particularly vulnerable customers being influenced or misled by actions of the criminals (e.g. HBOS over-promising on lending and specialist advice being available; being encouraged to provide management and logistical support for unrelated businesses that it transpired were connected with the fraud);

(ii) customers being encouraged, coerced or deceived into taking actions such as investing time, money and reputation into creating new entities that ultimately would not be viable given the IAR fraud;

(iii) timing of the appointment of administrators (e.g. with 24 hours' notice) and/or the appointment of QCS being premature when a business had recently commenced trading/injected more capital;

(iv) a recommendation (or what was perceived as a recommendation) for alternative finance from a financier later subject to adverse media criticism for charging at higher rates;

(v) having to deal with extreme behaviour by the convicted former HBOS employees when coping with distressing personal circumstances (e.g. serious illness of partner/bereavement);

(vi) being referenced in various online articles as having been an associate of the convicted individuals, in a way that had not been seen with any others.

4.54 In such cases either the Bank or Professor Griggs decided on additional compensation by way of an increase to the D&I matrix award.

VI COMPENSATION FOR D&C LOSS

4.55 The Bank told me that it assessed direct and consequential losses in accordance with ordinary legal principles.

4.56 In broad terms the Bank's methodology for considering direct and consequential loss to a business involved its legal assessors considering the business' financial status on entry into IAR and its treatment while there and during the turnaround activities of QCS.

4.57 As to direct losses to individuals, assessors were to consider whether there was a transfer of shares or in the ownership of a business while it was in IAR and any injections of funds during that time. An individual's shareholding and changes to it were also considered, together with any personal guarantees called upon.

4.58 Calculating the quantum of loss could draw on a range of matters such as the change of valuation of a business from its entry into IAR to its exit.

4.59 The methodology identified various types of potential loss including bank fees, default interest charges, interest charges on alternative borrowings, the costs associated with forced sales and the loss of opportunities.

Customer's evidence

4.60 The Bank said that the customer's evidence was considered. However, the Customer Review applied legal principles in evaluating it, whereas it took a customer's evidence at face value when assessing redress for D&I. If the customer did not have the evidence to support the claim for D&C loss, the methodology stated, the claim failed.

External advice

4.61 The Bank told me that in eight of the more complex cases it sought outside advice from EY on whether any D&C losses had been incurred. In all these cases, it continued, the external advisers reached the same conclusion that it had. I return to this in Chapter 11.

VII REFUND OF QCS FEES

4.62 The Bank decided to compensate companies in respect of fees paid to QCS, irrespective of whether a claim was made. That would be along with 8% simple interest per annum. This would be done even if the fees appeared to have been appropriate or were funded from increased borrowing not later repaid. The Bank's decisions in this regard were made on a case-by-case basis and in its discretion.

4.63 Compensation for QCS fees was paid: (i) to the business that incurred them, if it was still trading; (ii) to the business that incurred them, if it had been dissolved within six years and could be reinstated; or (iii) if the business had been dissolved more than six years previously and could not be reinstated, to its former shareholders at the point they were incurred. Fees could be refunded to shareholders who were not in the Customer Review.

4.64 Overall, the Bank offered £7.1 million and paid £5.6 million in respect of such payments. At the time of my review there were a small number of cases where businesses were in the process of being restored to the companies register so that refunds could be made.

VIII CONSISTENCY

4.65 The Bank explained to me that, in the early stages of the Customer Review, it sought consistency within and across individual case assessments by its four-eyes check, daily discussions among assessors and weekly forums for resolving and sharing technical queries. With experience, the need for these measures diminished and the frequency of knowledge-sharing forums was therefore reduced.

4.66 In the last quarter of 2017, after approximately half the Customer Review population had been assessed, formal consistency checking was introduced. It retrospectively re-considered all the outcomes communicated to customers. Upwards adjustments were

made to cases with similar fact patterns where appropriate. If an outcome was due to be lower than originally determined, the Bank maintained its original position.

4.67 When I asked Professor Griggs about consistency, he replied that there was a constant dialogue between the Bank and him to compare the circumstances of the various cases to ensure it was maintained. Periodically, he said, there were "look backs" as the Review developed and patterns, themes and recurring issues arose.

CHAPTER 5 INDEPENDENT REVIEWER: PROFESSOR GRIGGS

5.1 The Bank stated that its intention in appointing an independent reviewer for the Customer Review was to provide the assurance that it was delivering fair outcomes for customers.

5.2 The Bank told me that initially it considered appointing a large accounting or consultancy firm. However, feedback from external stakeholders had indicated that this would be unlikely to command confidence.

5.3 The Bank also gave consideration to appointing an independent legal expert. However, it concluded that since the Customer Review was not designed to replicate a legal process, it would be better to have an "SME champion", who would be supported by technical advice from professional firms.

I PROFESSOR GRIGGS AND HIS TEAM

5.4 Professor Griggs was approached about the role of independent reviewer in late February-early March 2017. The Bank investigated whether there were any conflicts of interest (either actual or perceived) as a result of his business and other interests.

5.5 After a series of meetings with the Bank, Professor Griggs was formally appointed with effect from 8 March 2017. As we saw earlier, his appointment was publicly announced on 20 March 2017.

5.6 The Bank told me that the FCA had confirmed that they were content with his appointment.

Assistance for Professor Griggs

5.7 To assist Professor Griggs in his task, he had the law firm Taylor Wessing LLP to provide legal advice. Taylor Wessing is an international law firm, with an office in London.

5.8 As well, he had the firms RSM (previously known as Baker Tilly) and Mercer & Hole (when RSM had a conflict) to provide advice on accounting issues. Beattie Communications Group acted for Professor Griggs on the public relations side.

5.9 Professor Griggs told me that he requested and was given a single point of contact in the Bank, to ensure an efficient flow of information.

5.10 The Bank provided Professor Griggs with an email address, @lloydsbanking.com. Emails sent to that address were forwarded to him. With time, he provided his personal details and those of his team so customers could make direct contact.

5.11 The Bank despatched the letters which Professor Griggs sent to customers, including his conclusions about the outcome of a case, together with its own letters.

Professor Griggs' overall view

5.12 In approaching his task, Professor Griggs informed me that he considered that one overarching factor he should take into account was the historical context of the events in question, namely, that in the early 2000s the SME commercial lending sector was more aggressive than today.

5.13 Overall, Professor Griggs told me that he considered that the Customer Review had delivered fair and reasonable outcomes to participants which avoided difficult and lengthy legal processes.

5.14 Notwithstanding that, he acknowledged that in some respects things could have been done differently. These are referred to below.

II PROFESSOR GRIGGS' ROLE

Professor Griggs' terms of reference

5.15 The press release of 20 March 2017 announcing Professor Griggs' appointment stated that his role was to agree the scope, methodology and individual case outcomes of the Customer Review in order to ensure fair outcomes, as well as to ensure that it was undertaken effectively.

5.16 Professor Griggs told me that he had three responsibilities.

5.17 First, he was to give his approval of the methodology for the review, to agree that it would operate effectively to provide fair customer outcomes.

5.18 In relation to this aspect of his role, he was to support and challenge the process as the Bank developed the methodology, to the extent he was able to without compromising his independence. He was also to approve any changes made to the methodology during the process.

5.19 Approval of the overall methodology was to include approval of each of the following elements: (i) the document gathering and Customer Review process; (ii) the factors assessed as part of the Customer Review (i.e., financial assessment and conduct and legal assessment); (iii) the treatment of customers in financial difficulty; (iv) the approach to customer participation in the Customer Review and the overall approach to communicating with customers; (v) the methodology for calculating the quantum of redress due under the Customer Review; and (vi) the process for communicating customer outcomes.

5.20 The second aspect of Professor Griggs' role was to oversee the client determinations made under the Customer Review. This included confirming that the Bank had:

(i) appropriately checked its data to ensure that all customers in scope had in fact been included in the review;

(ii) made its overall decision in accordance with the methodology;

(iii) taken into account all the relevant information in accordance with the methodology;

(iv) calculated any payment due in accordance with the agreed payment methodology;

(v) therefore reached a fair determination in accordance with the overall transparent approach; and

(vi) appropriately communicated the outcome and the explanation for it to the customer.

5.21 Professor Griggs' third job, he told me, was to approve the Bank's internal quality assurance process to ensure that the Customer Review was working effectively and any necessary enhancements to the methodology were made.

Areas excluded from Professor Griggs' oversight

5.22 Professor Griggs was to have no role in: (i) the Bank's decisions on interim payments; (ii) its decisions on professional advice; and (iii) its writing off of customers' remaining business and personal debts.

Informing the public and customers of the role

5.23 We saw that in the press release of 20 March 2017 Professor Griggs' role was described as: (i) agreeing the scope and methodology of the Customer Review; (ii) agreeing individual case outcomes to ensure fair outcomes; and (iii) ensuring that the Customer Review was undertaken effectively.

5.24 In the Next Steps letter, which the Bank sent out from 21 April 2017, it explained that it would send outcomes to customers after they had been "approved or amended" by Professor Griggs. There would be a chance to arrange a meeting with the Bank, which Professor Griggs could attend if that was what customers wanted.

5.25 Professor Griggs' own letter, accompanying this Next Steps letter, stated that since his appointment had been announced he had been working with the Bank to agree the scope and methodology of the Customer Review. He stated that he had been clear with the Bank that it must reach out to customers to see if they had further information relevant to their case. He added that he would be "personally involved in reviewing and approving" the Bank's outcome in each case "to ensure that the review is undertaken effectively and that you receive a fair outcome." The letter contained his address and other contact details.

Approving the Customer Review population

5.26 When I asked Professor Griggs how he satisfied himself that the Bank had appropriately identified the Customer Review's population, he told me that he took the view that it was solely a matter for the Bank to decide. After considering the rationale for the three cohorts which the Bank identified - customers referred by the convicted bankers to QCS, those with QCS involvement and those complaining about the convicted bankers - Professor Griggs felt that the Bank had cast a wide net and so had (to the extent that he was able to comment) captured all potential participants.

Approving the compensation methodology

5.27 As we have seen, under his terms of reference Professor Griggs had to approve the methodology for the Customer Review to agree that it would operate effectively to provide fair outcomes for customers.

5.28 He told me that, to satisfy himself that the Bank's methodology was capable of delivering fair and reasonable outcomes for customers, he firstly digested the comprehensive background material it had provided so he could understand the events at IAR. He then met with the Bank on several occasions to understand and assess the methodology, including how compensation would be calculated and the various factors taken into account, and his powers to challenge an outcome.

5.29 As a result, Professor Griggs told me, he concluded that the methodology was capable of delivering fair and reasonable outcomes for customers. In particular, he said, he had endorsed how the Bank's methodology took into account issues such as the length of time customers in the Customer Review spent with or were affected by those convicted at trial, the fees charged by QCS, the impact which those convicted had on individuals (including the emotional/personal impact) and/or on their businesses, and the length of time a business was in IAR.

Suggesting changes to Bank's methodology

5.30 I asked Professor Griggs to what extent there were changes in the methodology adopted by the Bank following his suggestions. He replied that there were none, but that he discussed certain best practices with the Bank. Examples of this, he said, were allowing customers extended time for submitting additional information when appropriate, providing detailed explanations at outcome meetings, and treating spouse directors sympathetically where their spouse was the main director.

III PROFESSOR GRIGGS' APPROACH

5.31 Professor Griggs told me about his own approach and that of his advisers in reviewing the Bank's decisions on compensation.

5.32 As explained earlier, my team and I were not able to explore fully the work undertaken by Professor Griggs, Taylor Wessing, RSM or Mercer & Hole.

Material available

5.33 In making his assessment of individual cases, Professor Griggs had access to the files and information which the Bank used in its own assessment.

5.34 In addition to the Bank files, he and his team would also receive the working papers the Bank used to carry out its own assessment, information from additional electronic searches when he requested them, and the written submissions of customers.

5.35 Professor Griggs did request further information when he felt it would be helpful to his assessment of a case. Professor Griggs asked for 11 additional searches with respect to seven businesses. He provided me with the details.

5.36 Professor Griggs commented that the Bank always provided any further information requested in a timely fashion.

5.37 The Bank told me that when customers corresponded directly with Professor Griggs, he normally shared the information with it so that cases could be assessed on an equal footing.

Reviewing cases with/without advisers

5.38 In a small number of cases Professor Griggs decided that he did not need any input from his advisers.

5.39 In the vast majority of cases, however, he told me that he asked his team at Taylor Wessing to review the case documentation and provide all necessary advice to him to assist him in reaching conclusions on what the Bank proposed as compensation.

5.40 If he required accounting advice, he would discuss what he required with Taylor Wessing, who would then instruct either RSM or Mercer & Hole to provide it.

Professor Griggs' methodology

5.41 Once the Bank completed an assessment, it prepared a briefing note to accompany the package of documents submitted to Professor Griggs. That set out the basis and rationale for the proposed outcome.

5.42 When I asked Professor Griggs, he said that neither he nor Taylor Wessing used standard work plans or templates. He read the complete case file on his own in one of the Bank's branches near his home and decided what support he needed from his advisers on a case. He said that he did not have his "own" methodology. He was independently reviewing cases in the context of the application of the Bank's methodology.

5.43 Professor Griggs generally sent his views to the Bank by email. He would either agree with the outcome; request an explanation; challenge the rationale for certain scores on the D&I matrix or the determinations of losses; or request a change to matrix scores and an associated increase in the amount to be offered. There might be a series of emails about a case.

Changes resulting from Professor Griggs' recommendations

5.44 During the course of the Customer Review, Professor Griggs said that he sought to make certain changes, such as suggesting amendments to the language of a few outcome letters to participants, introducing some flexibility into the procedure for meetings (i.e. not putting a limit on the format or number of those meetings where the customer wanted them) and, in some of the more complex cases, providing guidance to participants at outcome meetings as to the sorts of additional information that it would be useful to receive.

Approach of Professor Griggs' advisers

5.45 Professor Griggs informed me that Taylor Wessing typically reviewed the Bank's case file, instructed RSM or Mercer & Hole as applicable, provided advice as necessary to him, followed up on any queries with the Bank, and reviewed its outcome and provided their advice on it as necessary.

5.46 As to RSM and Mercer & Hole, they relied on the use of a small team of senior staff to interpret the requirements of each instruction rather than a checklist-driven approach. Unless there was a specific limitation to the instructions, the Bank's case file was read in full. The information obtained was supplemented by a detailed review of any records available at Companies House, covering items such as corporate structure, directors and shareholders, charges, statutory accounts, insolvency appointments, insolvency reports (administrators' proposals or other progress reports) and receipts and payments accounts.

IV OVERSEEING COMPENSATION

5.47 Under his terms of reference, Professor Griggs had a role in overseeing compensation awards. In approaching the task Professor Griggs told me that he was conscious that to his knowledge this was the first time that a major bank had established a scheme where an independent reviewer was appointed to act as a check and balance on case reviews.

Explanation to the Treasury Select Committee, June 2018

5.48 In response to a letter from Rt Hon Nicky Morgan MP, then chair of the House of Commons Treasury Select Committee, Professor Griggs wrote to her on 28 June 2018.[14]

5.49 He first explained to her that he had agreed with the Bank: (i) that the objective of the Customer Review was to achieve swift and fair compensation for customers impacted by the events at IAR in a way which would not subject them to a difficult or lengthy legal process; (ii) the ex gratia payments of £35,000; and (iii) that since the full story was unlikely to be in the Bank's records, it was important that customers were able to provide their own submissions to the Customer Review.

5.50 Professor Griggs then explained to the Rt Hon Nicky Morgan MP that his assessment of cases and that of the Bank took place separately and without reference to each other. D&C losses were considered using established legal principles on the basis of the information before him. In order to reach a conclusion on the extent of D&I, he had agreed with the Bank that these payments should be based heavily on the customer's own account of their experiences.

5.51 Professor Griggs informed the Rt Hon Nicky Morgan MP that there were a number of other cases where the Bank and he had both agreed to amend the amounts initially proposed. However, in a limited number of cases he had remained of a different view from the Bank as to the appropriate level of compensation. In every one of these cases the Bank had amended its offer to reflect his conclusion.

[14] These letters dated 26 June and 28 June 2018 appear on the Treasury Select Committee website under the headline "Committee presses for maximum transparency over "shocking" HBOS Reading crime" (https://www.parliament.uk/business/committees/committees-a-z/commons-select/treasury-committee/news-parliament-2017/hbos-reading-chairs-statement-17-19/).

Assessing and increasing awards

5.52 Professor Griggs told me that after consultation with his team he would reach a view on a particular case. He would then compare that to the proposed outcome the Bank had reached.

5.53 Professor Griggs told me that his assessment was never for a lower amount than the Bank's assessment.

5.54 I asked Professor Griggs about the basis on which he would recommend increases from the compensation that the Bank had determined. He explained that he would do so: (i) if he had a different view to the Bank as to the application of its methodology; and (ii) if although the outcome was in accordance with the methodology he considered that in order to achieve what he felt was a fair and reasonable outcome an increase was necessary.

5.55 He gave me two examples of a situation where he thought this appropriate. The first was where he felt that, when compared to another director within the same business, or perhaps to another individual in similar circumstances in a different case, the award to the individual in question should be increased.

5.56 A second situation was in cases where he felt that the Bank's methodology did not result in a figure which he felt reflected extreme distress or an extreme personal impact. There were 14 directors from 11 businesses where this occurred. In these cases he considered it appropriate to exercise his discretion to increase compensation in recognition of facts which adversely affected the person, but which strictly fell outside the parameters of the methodology.

Increased awards to reflect D&C losses

5.57 Professor Griggs told me that with four directors from three different businesses he reached the view that there was a plausible case for financial loss irrespective of a payment for D&I. He said that in those cases he sought and the Bank agreed to an increase in compensation for D&I. That reflected his view that the impact on participants was aggravated by the plausible legal case, based on what he believed to be fair and reasonable.

Spouse directors

5.58 Professor Griggs told me that as a result of his actions spouse directors were introduced as an informal change in the methodology. In such cases, he sought to ensure that the extent of his or her involvement was properly understood in order that it was reflected in the outcome. As he explained, he was conscious that the Bank's files might not evidence fully the involvement of, or impact on, a spouse director in interactions with the criminals, in particular where the spouse was a wife supporting a husband in the business while being at home. Professor Griggs said that he would speak to the spouse to understand their involvement in the business not only at the office but also at home. He gave weight to the spouses' explanation of their involvement in the business. In a case

where the business was jointly operated by the couple, Professor Griggs considered that in the absence of evidence that would demonstrate they were involved with the business to different extents, the spouse should be considered to have suffered the same or similar distress as their partner and therefore be offered similar compensation. Professor Griggs gave me several examples of occasions where spouse directors were considered sympathetically in the absence of contemporaneous evidence, and even if they did not have direct interactions with the criminals.

Disagreements with the Bank: consensus reached

5.59 If he disagreed with the Bank's reasoning or outcome, Professor Griggs told me, he would discuss it with the Bank, inform it in writing that he disagreed and why, and offer his view on how the outcome should be different. The Bank would consider his view and revert either to confirm its agreement with him or would set out why it was not prepared to change its view.

5.60 If the Bank's further reasoning for no change satisfied him, he would agree with its outcome.

5.61 Overall, Professor Griggs challenged 77 of the 285 outcomes the Bank proposed. With 25 of these 77 cases he agreed after discussion with the Bank that no change in the Bank's offer was needed.

5.62 In 52 of the 77 cases there was an increase for the customer. In 33 of the cases the Bank agreed with him that the offer should be increased. Professor Griggs said that in 16 cases, however, he overruled the Bank's offer and the customer received more than the Bank proposed.

5.63 Professor Griggs told me that in some cases he exercised his discretion to apply an increase because of the extreme distress or extreme personal impact suffered by the customer (as I have explained above), or because it reflected the need for a more sympathetic treatment of a spouse.

5.64 Overall Professor Griggs' challenges resulted in an additional £12.4 million being offered to customers.

Overruling the Bank's award

5.65 Professor Griggs informed me that he was given a right to overrule the Bank's compensation awards in certain circumstances. This was only exercised if after full discussion it was not possible to reach agreement with the Bank. He told me that this had undoubtedly given that right more value, as had the fact that it was used very sparingly. Professor Griggs said that the Bank had never overruled him on compensation to be awarded to customers. In addition to financial uplifts to customers' compensation, Professor Griggs told me that he also challenged the Bank on cases and issues which were, strictly speaking, outside his scope, but which customers requested to be addressed. These included requests to ease the non-disclosure exclusions in the offer letter, requests for letters of comfort from the Bank exonerating customers from any involvement in the

fraud, and raising with the Bank the unfairness of it only writing off debt of its own customers.

5.66 As I have explained above, Professor Griggs overruled the Bank's decision in 16 cases. Agreement could not be reached and he insisted on a discretionary uplift which went beyond what the methodology was capable of producing. Of those 16 cases, three were instances where the Bank had awarded nil compensation.

5.67 Professor Griggs also highlighted that he had been given access to senior management within the Bank to help break any deadlock with its main assessment team, or to get a second opinion as to its position on a particular matter.

5.68 According to Professor Griggs, the availability of his right to overrule the Bank, and that customers had been told in outcome meetings that he had the final word, were important features for the integrity of the Customer Review. That was particularly so in light of the perception by some participants that he was not fully independent from the Bank.

CHAPTER 6 CUSTOMER OUTCOMES

6.1 From its own files and what customers submitted, the Bank applied its methodology to calculate compensation offers for customers. It sent these out in offer letters. Customers could request meetings with the Bank at the outset of the process and with the Bank and Professor Griggs after they received an outcome letter. Additional information provided after that stage might result in an increased offer.

I CUSTOMER SUBMISSIONS AND MEETINGS

6.2 The Bank adopted a standard procedure for meeting customers before providing them with details of their compensation.

"Questionnaire" meetings

6.3 As we have seen, the Bank's Next Steps letter of 21 April 2017 invited recipients to provide information in the form of a questionnaire, but also offered a meeting if customers would prefer it. 46 customer meetings were held prior to individuals receiving their initial outcome.

6.4 The questionnaire meetings were typically fact finding meetings which gave customers an opportunity to provide their account. The Bank told me that they regarded these meetings as an opportunity to apologise face to face to customers for the actions of the convicted criminals and for them to share their story.

6.5 This, the Bank told me, was essential in allowing it to understand the distress the customer had experienced and added a more personal articulation to the customer's experiences which its file would not necessarily reflect. These meetings also gave the customer a better understanding of the Customer Review process and the role of Professor Griggs.

6.6 Professor Griggs considered that he should not be present for the questionnaire meetings to ensure that he remained independent. However, at that meeting the Bank would ask if a customer wanted to speak with Professor Griggs. Some took up that offer; others did not. Where a customer wanted to speak with Professor Griggs he would briefly call them on the telephone. The purpose was to check that the customer felt that the Bank had carried out the meeting properly and that there were no issues with that part of the process. Professor Griggs told me that he does not recall any customer saying that a questionnaire meeting with the Bank had not gone well.

Customer submissions

6.7 Customers could submit information along with or in substitution for the questionnaire. That was often done with the benefit of legal advice. Customers also made submissions of additional information after receiving an offer and after outcome meetings.

6.8 Professor Griggs told me that he was satisfied that customers were given sufficient opportunity to submit information for consideration in the assessment of their case. In his view they also had adequate opportunity to submit additional information.

6.9 He told me that he was also of the view that he considered that customers understood what information they were required to submit for participation in the Customer Review.

Non-disclosure of Bank-held information

6.10 The Bank adopted a policy of not disclosing to customers the information it held. It regarded this as a corollary of the non-legal, voluntary character of the Customer Review. As customers were told at the outcome meetings, the Customer Review was not designed to replicate a legal process. That also meant that offers of compensation were on a non-admissions basis.

6.11 Professor Griggs told me that the policy of non-disclosure meant that the Customer Review was able to assess outcomes quicker than would otherwise have been the case. He commented that when customers' advisers expressed dissatisfaction about the inability to make decisions on an outcome in the absence of disclosure:

> "this was in part because those advisers were approaching the Scheme through the lens of an adversarial process and therefore the issue of disclosure took on a greater significance than was appropriate given the parameters of the Scheme."

Non-disclosure of compensation methodology

6.12 The Bank also had a policy of not disclosing its methodology for calculating compensation, in particular its D&I matrix. That was for similar reasons as applied to the non-disclosure of information the Bank held.

6.13 I asked Professor Griggs for his views on whether the level of disclosure provided to customers in respect of compensation awards was sufficiently detailed to give them an understanding of the rationale for the amounts offered, and whether he was satisfied that it was appropriate not to disclose the Bank's methodology.

6.14 Professor Griggs' response was that it was a principle set by the Bank as part of the voluntary nature of the Customer Review, that he understood the Bank's rationale, but that ultimately that was its decision. His objective was to make sure that outcomes for participants were fair and consistent.

Cases leaving the Customer Review to pursue legal action etc.

6.15 In a number of cases, individuals included in the Customer Review decided to leave it and to pursue an alternative course. Under the Customer Review they were free to do this. There were five individuals who before receiving an offer left the Customer Review to seek redress by other means.

6.16 Four customers received a compensation offer within the Customer Review but declined to accept it.

6.17 The Bank in many cases agreed to enter standstill agreements with customers because of time limits to bringing legal proceedings. These ensured that participation in the Customer Review did not prejudice a customer's ability to choose to pursue alternative remedies should they be dissatisfied with what the Bank offered.

6.18 The Bank told me of its concern that customers might opt out of the Customer Review because they misunderstood aspects of how it would operate or because of a lack of confidence in the process. If it had evidence suggesting the customer was eligible for compensation, it informed customers of the indicative amount to ensure they were aware of this before making a decision to opt out formally.

II OUTCOME LETTERS

6.19 Once the Bank had considered a customer's case, it sent an outcome letter, setting out the amount of compensation (if any) it was offering, and inviting customers to an outcome meeting to discuss matters if they wished. Further outcome letters followed if the Bank reconsidered the case.

6.20 The Bank told me that these letters:

> "were written in alignment with our normal approach to responding to customer complaints, seeking to acknowledge the impact customers had experienced, apologising for this impact and providing a clear explanation of our review conclusions whilst generally demonstrating sensitivity."

Outcome letters: individuals

6.21 Although outcome letters followed a standard format, they varied with the nature of the case and also during the course of the Customer Review. Over time, the Bank told me, there were fuller explanations of the reasoning behind the Bank's proposed outcome, particularly in circumstances where it did not offer compensation, or refused to increase compensation following the customer's submission of additional information.

6.22 An outcome letter typically began with an expression of the Bank's regret about the customer's dealings with those responsible for criminal behaviour in connection with IAR, and "the length of time it has taken to reach an outcome since those events took place."

6.23 The letter then set out the amount of the Bank's offer of redress (if any) for D&I arising from the interactions with IAR. Later there was a general description of the nature of those interactions and their personal impact. Although the matrix was not disclosed, the description coincided broadly with the three categories in it used for determining any D&I payment: interactions with Lynden Scourfield or Mark Dobson, dealings with QCS, and any particular personal impact on the customer.

6.24 Reference was also made in the letter to a fact sheet enclosed on the tax treatment of the payment.

6.25 After setting out any D&I offer the letter stated that in relation to any claim for financial loss the Bank had assessed it "and can confirm that we do not consider that your claims satisfy the relevant legal tests." The reasoning was stated in broad terms, for example that the customer had not demonstrated, among other things, that the losses claimed were caused by the IAR fraud.

6.26 If compensation for QCS fees was payable, the letter would state an amount and explain the basis on which this was being done, namely that the Bank had identified the QCS fees charged but the company was dissolved so it had decided to offer to pay an equivalent amount to the former shareholders on a voluntary basis, together with compensatory interest from when the fees were paid. The tax treatment of these payments was spelt out.

6.27 The letters would also mention matters such as the set off of any interim payments against what was being offered. Customers were assured that the outcome had no bearing on their eligibility for their £35,000 ex-gratia payment.

6.28 Offers were stated to be made on a "no admissions" basis.

6.29 Customers were told that they must obtain their own independent legal advice before accepting the offer and entering the required settlement agreement. The Bank would meet reasonable costs for that.

6.30 There was a 28-day period to accept the offer or (if relevant) to provide additional information. If the customer believed that was not sufficient time they were told that their relationship manager should be informed.

Outcome letters: companies

6.31 The outcome of claims for compensation by companies in the Customer Review would be set out in a separate letter. These claims were often advanced by lawyers acting for customers.

6.32 The Bank rejected all such claims. The outcome letters would state that no redress was due to a company because the Bank had not identified any evidence of losses being incurred by it as a result of the IAR fraud. In reaching this conclusion, the Bank would explain, it had had regard to information provided to the Customer Review alongside information it held, including trading performance, trading potential, indebtedness and cash-flow, and the sequence of events leading to its administration and eventual dissolution. The letter would note that the company was already in financial difficulty before it became a customer of IAR, stating a reason such as poor trading results or being under-capitalised. The letter would also address, in outline, specific allegations raised.

Outcomes: Professor Griggs' letters

6.33 The Bank's outcome letters stated that the contents and the proposed redress sum had been reviewed and approved by Professor Griggs. It also stated that if the recipient wished to arrange a meeting with the Bank to discuss the contents, Professor Griggs could attend.

6.34 Enclosed with the Bank's outcome letters was a separate letter from Professor Griggs. This stated that he had reviewed the assessment, read the information on which it was based (from both the Bank and what had been submitted by the customer) and discussed the assessment with the Bank. In light of that he had approved the outcome and considered it and the amount offered was fair and reasonable. If there were questions

about the outcome, his letter added, the Bank had offered to have a meeting and he would be happy to attend.

III OUTCOME MEETINGS

6.35 All customers were offered a face-to-face meeting with the Bank and Professor Griggs following their receipt of an outcome letter. Professor Griggs told me that there were 64 such outcome meetings.

The Bank's purpose for outcome meetings

6.36 The Bank told me that it saw the outcome meetings as an important opportunity to ensure that the customers understood the rationale for their outcome and the next steps available to them.

6.37 As such the Bank said that it used the meetings to build on the detail that had previously been disclosed in the outcome letter. Its view was that the meetings helped customers better understand the outcome that had been communicated by setting out the history of the business prior to its transfer to IAR, as well as expanding on the actions and treatment the customer had experienced whilst in IAR, as evidenced in the file or taken from what the customer had told them.

6.38 While the Bank saw the meetings as an opportunity to explain outcomes, it did not intend them as a forum for negotiation and refused to engage in negotiations with customers or their representatives at the meetings.

Nature of outcome meetings

6.39 The majority of the outcome meetings were held in the Bank's premises in London, but in a number of cases its representatives travelled to the customer's preferred location. Prior to the meeting the relationship manager issued an agenda and would ask customers about any specific points they wished to raise.

6.40 Customers were able to bring their legal advisors to outcome meetings. The Bank paid for the reasonable costs of that as well as any associated expenses such as travel and accommodation.

6.41 The Bank was represented at the outcome meetings by one of its staff who attended regularly and by the relationship manager for the customer. The former was there to explain the purpose of the meeting, respond to customer queries and explain the outcome and possible next steps. The relationship manager was there as a note taker and the customer's main point of contact.

6.42 Professor Griggs was also in attendance at all outcome meetings. In 19 cases Professor Griggs spoke to customers without the Bank, either face to face or on the telephone. In most cases his legal advisers, Taylor Wessing, were present at the meetings.

Professor Griggs' role

6.43 The Bank conceived Professor Griggs' role as being to ensure the appropriate conduct of the outcome meetings, respond to customer questions where appropriate, and confirm that the case had been independently assessed with the outcome approved by him.

6.44 Professor Griggs told me that at outcome meetings he encouraged participants with lawyers to provide additional information in a way that was more personal and subjective as that was thought to be helpful for the consideration of their case. For example, in one case, he told me, he encouraged the customer to provide more information about the particular impact on him and his family, which then led to an increase in his award.

The meeting and the outcome script

6.45 The Bank said that it recognised the need to handle meetings with sensitivity since matters were likely to be very difficult and emotional for some customers. To this effect there was an explanation at the outset of a meeting that the customer was under no pressure to reach any agreement during the meeting itself, and that they would be given time after the meeting to consider how they wished to proceed. Customers were also told that the meeting could be suspended at any point should they want a break.

6.46 At the outcome meetings, the Bank's representative read an explanation of the history of the business' dealings with the Bank and with those convicted. The Bank told me that this enabled a better mutual understanding as to the proximity of a customer to the fraudulent conspiracy or those individuals convicted at trial.

6.47 The Bank told me that as the Customer Review progressed the format of outcome meetings developed. The script used became longer and more information about the process was provided. The change was instigated by Professor Griggs, who considered that it was important that the Bank provide more information. That was because it was not possible to answer questions about the basis of the decision-making in the matrix.

6.48 After the meeting, the Bank recorded its anticipated next steps, which it agreed with Professor Griggs. It was the responsibility of the relationship manager to ensure that the customer received a "next steps" communication within two working days after the meeting.

IV ADDITIONAL INFORMATION AND REVISED OFFERS

6.49 Customers were provided with an opportunity to submit additional information after their outcome had been communicated to them, to supplement what they had provided at earlier stages. Professor Griggs frequently requested that any new points raised by a customer be treated as additional information.

6.50 In practice, customers often provided additional information after they had received an outcome letter and attended an outcome meeting. The Bank paid for the reasonable costs associated with an initial submission of additional information.

6.51 Whenever additional information was received a further round of assessment activities was triggered in the Bank. The additional information was considered alongside all previous information from the case file by the assessors.

Revised offers after additional information

6.52 In total 69 customers provided additional information following the receipt of their initial offer. As a result, the Customer Review determined that in 38 cases there should be an increase in the D&I offered to a customer. That meant that additional compensation of £10 million was paid to customers.

Professor Griggs and additional information

6.53 In his letter to the Rt Hon Nicky Morgan MP of the Treasury Select Committee in mid-July 2018, Professor Griggs explained that some customers requested an outcome meeting with him and the Bank once they had their offers. Some customers then submitted additional information. Professor Griggs continued:

> "I consider that additional information with my team (and [the Bank] does the same), and whether it alters my conclusion as to the level of compensation that should be offered. If my conclusion as to the level of compensation which should be offered differs from that of [the Bank] (either before an outcome letter is sent by [the Bank] or after additional information is received), I will then discuss that and explain to [the Bank] why I consider that the offer should be different. In most cases, I reach agreement with [the Bank] as to the offer. In some cases, I have been unable to reach agreement with [the Bank] and in these cases my view is final. In every case where I have reached a different view from [the Bank] on the proposed offer, the offer has increased."

6.54 I asked Professor Griggs whether he thought there were examples where customers submitted additional information because they had not understood what was being asked of them prior to the outcome meeting. He did not think that was the case.

6.55 However, he added that because the methodology was not provided to the customers the discussion at outcome meetings would sometimes elicit a focus on particular aspects of a customer's story which he considered might be useful for him and the Bank to consider. He asked for that in the form of additional information.

6.56 In addition, he added, the Bank's description of events relating to their business at the time either reminded them of matters or resulted in their considering that they needed to provide context to those events or to provide additional information. Professor Griggs said that he always encouraged outcome meetings to be interactive.

6.57 Professor Griggs informed me that with 21 outcomes, relating to 17 directors, additional information led him to recommend an increase in compensation. With 16 outcomes relating to 11 directors Professor Griggs decided to increase the award as a result of the additional information, even though the Bank did not agree.

Meetings with an official of the Bank

6.58 In addition to the typical pattern for outcome meetings described above, a number of customers requested meetings directly with the Banks' accountable executive for the Customer Review. The Bank told me that these meetings were also attended by either the relationship manager or a member of the Bank's internal legal team.

6.59 I asked the Bank for information about the meetings with the Bank's accountable executive. The Bank responded that as regards compensation following the initial outcome letter, he held 15 meetings with six different directors. Four of those directors obtained an uplift in the D&I compensation payable following their submitting additional information. The SME Alliance attended with two of those directors. The Bank also informed me that compensation was increased post-outcome in one case following a telephone conversation with the Bank's accountable executive.

6.60 With each of these five directors (the four meetings in person and the telephone conversation), the Bank gave me an explanation as to why it had agreed to increase the compensation: for example, there was either exceptional distress or a personal impact which became evident from the additional information supplied.

V SETTLEMENT AGREEMENTS

6.61 Any individual or business accepting an offer (with the exception of shareholders receiving £2,000 or less as their portion of QCS fees) were required to enter into a settlement agreement with the Bank before doing so.

6.62 The Bank made it an express condition that all customers were required to take independent legal advice on the settlement agreement, for which it paid, prior to signature.

6.63 Outside of the narrow confidentiality requirements set out by the settlement agreement, the Bank told me, customers were free to speak to the police and other relevant authorities about concerns they had about IAR-related (and other) issues. I address this further in Chapter 14.

PART C STAKEHOLDER AND CUSTOMER VIEWS

CHAPTER 7 STAKEHOLDER SUBMISSIONS TO CRANSTON REVIEW

7.1. As I indicated in Chapter 1, I asked the SME Alliance and the APPG on Fair Business Banking for formal submissions to the Cranston Review. What I do in this chapter is to summarise their views on the Customer Review before turning in the following chapter to what the customers who saw me said about its performance.

I SME ALLIANCE

7.2. The SME Alliance Ltd was formed in September 2014 to support business owners who are victims of bank misconduct, including the IAR fraud. It takes the view that no review set up and run by Bank personnel can be considered "independent" where there is no obligation of transparency, no disclosure and no truly independent oversight.

Feedback on the Customer Review

7.3. Early in my review the director and co-founder of the SME Alliance, Mrs Nikki Turner, set out her "feedback" on the Customer Review under seven headings. The first, concerning eligibility requirements, focused on the exclusion of shareholders: since the Bank concluded that since every business would have failed, shareholders did not need to be compensated. The Bank, Mrs Turner said, had engineered a situation where unsecured creditors were also ignored, yet some would have gone to the wall because of the IAR fraud.

7.4. Under heading 2, Mrs Turner's document said that the Customer Review was reverse engineered to allow the Bank to pay D&I without paying direct and consequential loss. Moreover, the D&I payments were on a take it or leave it basis, with no discussion of the methodology or basis of calculation. She told me that some really devastating cases have been offered peanuts for D&I. Victims had had to wait for many years to get compensated. She added that the Bank knew that most of the victims did not have the ability, the energy, or the will to take legal proceedings.

7.5. Heading 3 concerned, amongst other things, the use of internal Bank documentation, not disclosed to customers. Mrs Turner said that it was used to paint a very bleak picture of a customer's business, yet some of the documentation would have been deposited in the Bank by the criminals and their staff.

7.6. There was a pressure on customers, heading 4, to accept settlements, since most of the victims were in dire straits 10 or 11 years after the Bank had closed their businesses.

7.7. Mrs Turner's heading 5 concerned the nature of the D&I offers. Those who made the most noise, she said, received the highest settlements. A better approach would have been a base amount everyone received as an apology, with D&I added on top.

7.8. "Forensic accountants" was Mrs Turner's heading 6. That concerned the statement in early press releases that the Bank was setting aside money for forensic accountants. However, the Bank subsequently refused to pay and would not wait for independent forensic accountant's reports. The promise to "assist victims in financial difficulty with

day to day living costs" had proved to be “like pulling teeth”. In some cases, she added, customers had been treated like “benefit cheats”.

7.9. Heading 7 in Mrs Turner’s feedback dealt with Bank expenditure for legal advice, which was ignored.

7.10. The worst thing about the Customer Review, Mrs Turner said, was that, with the publication of the Project Lord Turnbull report, the Bank should have compensated customers for the 11 years during which the IAR fraud had been concealed.

The Laidlaw/Tanchel opinion

7.11. In December 2018 the SME Alliance had obtained a legal opinion from Jonathan Laidlaw QC and Vivienne Tanchel of 2 Hare Court on the fairness of the Customer Review (“the Laidlaw/Tanchel opinion”). The SME Alliance gave me a copy of the opinion.

7.12. The Laidlaw/Tanchel opinion focussed on principles of natural justice. It concluded that the Customer Review was procedurally flawed and unlikely to provide just redress for the victims of the HBOS fraud. It took the view that the appointment of Professor Griggs by the Bank meant that he was not and was not seen to be independent. The failure to identify Professor Griggs’ accounting, insolvency and legal assistants meant that there could be no examination of their instructions, nor any challenge to their expertise or independence. The failure to disclose the documents relied upon by Professor Griggs meant customers did not know the case they had to meet and were unable to participate fully in the Customer Review.

7.13. The opinion added that the Customer Review’s terms of reference had been agreed without input from victims. The Customer Review methodology had not been updated to reflect the acceptance by the Bank that it commissioned the Project Lord Turnbull report. Customers had not been informed of the Project Lord Turnbull report, although regulators and the police had received extracts. The Bank had selected participants in the Customer Review and had not published its methodology for doing so.

7.14. Another criticism contained in the opinion was that the decision letters which the Bank sent to customers did not explain outcomes. Further, the Bank refused to fund experts (other than some legal representation) for customers, causing an inequality of arms. There was no appeal procedure from Professor Griggs.

7.15. For all of these reasons, the Laidlaw/ Tanchel opinion found that the Customer Review did not comply with fair process; nor did it have the transparency or oversight of the Dobbs Review, or of a skilled person’s report under section 166 of the Financial Services and Markets Act 2000.

The SME Alliance survey 2019

7.16. In late May 2019 the SME Alliance presented me with a small survey of 27 of its members about matters relevant to the Customer Review. They then provided a slightly updated version of the survey in June 2018. The survey identified those who had had dealings with Lynden Scourfield and Mark Dobson over the period 2002 to 2007, and

those who had dealings with other Bank staff who reported directly to those two bankers. Respondents were then invited to name those they dealt with at QCS. A number of questions followed about what happened to their business after the involvement of QCS and whether it was placed into administration or liquidated.

7.17. There were also questions about whether respondents had complained about their treatment and whether they had involved their MP. No respondent felt they had been dealt with fairly or reasonably in the Customer Review. Although a small number felt they had been dealt with politely in the Customer Review, most felt that their treatment had been unfair and unreasonable. Many indicated an impact of the IAR fraud on their families, and a significant number said that they themselves had contemplated suicide. None of the respondents were satisfied that the compensation offered in the Customer Review had taken into account the impact of the IAR fraud on their lives after 2007.

SME Alliance submission

7.18. In addition to this material, the SME Alliance made a formal submission to my review. The Customer Review began badly, the submission said, with the Bank denying that it knew of IAR fraud before the trial. If compensation had been awarded without taking that into account, it was even more unreasonable than thought. The submission quoted from a report the SME Alliance had produced in June 2018, which documented their concerns:

> "[The Customer] Review is a perfect example of the Bank being judge, jury and executioner of its own deeds. There is no transparency, no logical methodology and, rather than attempting to reach a fair and reasonable resolution for the victims to reflect what the Bank did or rather didn't do, it has now turned into a way to denigrate the victims based on historical documentation that was, in many cases, penned to conceal what was really happening in HBOS Reading. While [the Bank representatives] and Professor Griggs, are very polite and sympathetic to the victims, in truth, the orders from the anonymous "assessors" means the entire process of "outcome meetings" is both pointless and insulting. Pointless, because neither [the Bank representatives] can alter the offers and; insulting because the meetings are about the conduct of the victims (from the Bank's perspective) and not the conduct of the Bank."

7.19. The Customer Review, the submission continued, was for the most part focused on the conduct of the victims and not the criminal conduct of the Bank, which added to the suffering of the victims by denying what they knew to be true.

7.20. The submission was also critical of what it regarded as the lack of transparency in the Customer Review. The Bank could make allegations against the victims without disclosing the supporting documents. That did not comply with the Bank's obligation to treat customers fairly. Further, there was no appeal process available for anyone unhappy with the outcome; all the Bank did was to point out politely that the victims could reject the offers made and sue the Bank.

7.21. Regarding compensation, the SME Alliance said:

"We do not believe the compensation given to victims has been fair and reasonable and we are aware, in many if not most cases, losses (whether direct or consequential) have not been considered at all. Again, this is mostly because the Bank relied on undisclosed internal documentation to conclude there were few losses and very little chance the businesses would have been successful had they continued. The Bank has not had to substantiate its beliefs and even where victims have clear evidence of direct or consequential loss, prepared by legal and forensic experts, the Bank has mostly ignored the experts. We find it extraordinary Banks who had to be bailed out for billions of pounds from the public purse, and who continued to remunerate their senior executives with seven figure sums annually, have been quite so quick to denigrate their SME customers whose failure was as a result of fraudulent actions by the Banks."

7.22. Compensation in the Customer Review could not be compared with what a court would award because this was a unique, proven case of bankers and their colleagues defrauding customers in a systemic nature for personal gain. There is no precedent. In any event, a court would have fully considered D&C loss. Damages for this may well have been considerably more than what was awarded by the Customer Review. Given the background the Bank would not have wanted these cases to come to court. Comparisons which the SME Alliance understood the Bank to have made with damages awarded in the Piper Alpha disaster were unrealistic. In fact victims' losses flowed because their credit scores were trashed, their business reputations tarnished and their ability to source funds from mainstream lenders stymied.

7.23. The submission criticised the lack of consistency in the compensation offered. Awards had ranged from £100,000 to £5 million, with some genuine victims receiving a zero offer. The perception was that outside the Customer Review, the Alliance had been able to assist victims obtain better compensation (although still not the right compensation) than that offered under it.

7.24. The Alliance commented adversely on Professor Griggs as the independent reviewer. In its view he did not appear to have ultimate control over the Bank's decisions. While he was polite and seemed amenable to assisting the victims it seemed, from its perspective, that the Bank could overrule his views. The SME Alliance referred to a passage in the Walker Report[15] where it appeared that part of his role was to identify any perceived fault by victims in how they ran their businesses.

7.25. The awards in the Customer Review, the SME Alliance said, were not enough for people to rebuild their businesses, retire with security or, in some cases, repay the debts they had run up over the 10 years the Bank refused to acknowledge the fraud. Victims had no closure and many were, even now, struggling to survive after receiving awards.

7.26. Some things about the Customer Review, the SME Alliance thought, were well thought out, in particular the decision to award D&I to individuals as opposed to having to re-form companies dissolved post an administration process in order to consider losses. That

[15] Simon Walker CBE, Professor Christopher Hodges, Professor Robert Blackburn, *Review into the complaints and ADR landscape for the UK's SME market*, October 2018, 14. Professor Griggs has said the remark was taken out of context.

would have been long-winded, complicated and costly. But there was a lack of methodology and consistency in the awards for D&I.

7.27. A key point, the Alliance told me, was that no real consideration was given to the actual circumstances of the victims or the consequences of the 10 year gap between the discovery of the IAR fraud and the trial. The focus had been on the period of the fraud, and that following the trial, but not on the intervening time. There was no consideration of what these entrepreneurs may reasonably have felt they would have achieved in that 10 years. In that period victims had been left penniless, with no business and ability to earn a living, and in some cases the Banks had actively taken away other assets, including family homes.

II APPG ON FAIR BUSINESS BANKING

7.28. In response to my invitation for a formal submission, the All-Party Parliamentary Group on Fair Business Banking ("APPG") gave me access to the correspondence it had sent the Bank on the establishment of the Customer Review and during the period it operated. It also gave me its view now, looking back, as to how the Customer Review had performed.

Role of APPG

7.29. The APPG is one of the many cross-party groups comprised MPs and Members of the House of Lords. It is one of the largest, with 127 members from all sides of the two Houses of Parliament. When Parliament was dissolved on 5 November 2019 it was chaired by Mr Kevin Hollinrake MP.[16] It was originally formed in 2012 as the All-Party Parliamentary Group on Interest Rate Swap Mis-selling.[17] The APPG's remit was expanded after the 2015 general election to "Fair Business Banking".

7.30. The APPG told me that MPs had made frequent representations to it about cases which shared similar characteristics and which highlighted: (i) the imbalance of power that exists between businesses and the banks; (ii) the lack of satisfactory redress mechanisms and rights of action available to businesses; and (iii) the lack of satisfactory rights of action for owners of insolvent companies. It also informed me that it accepts cases from owners of businesses who have failed to obtain redress through the Financial Ombudsman Service or who have failed to persuade a regulator to pursue regulatory sanctions. It will also act in cases where businesses cannot persuade an insolvency practitioner appointed to take action (or satisfactory action) to recover losses. The APPG continued:

[16] Mr Hollinrake has been a Conservative MP. The Vice-Chairs have been Dr Lisa Cameron MP (Scottish National Party), Martin Whitfield MP (Labour), the Rt Hon. Sammy Wilson MP (Democratic Unionist Party), Stephen Kerr MP (Conservative), Luke Graham MP (Conservative), Lord Cromwell (Crossbench) and the Earl of Lindsay (Conservative). Heather Buchanan is the APPG's Director of Policy and Strategy. James Ventress is its Senior Policy Advisor.

[17] The APPG told me that following its work in this area the FCA established a review. The redress scheme which followed led to £2.1 billion being paid to businesses across the UK.

"We have yet to find an MP that does not have a constituent case that shares these characteristics. Our role is to support MPs in their casework whilst also identifying areas that require systemic reform. We therefore have a vast number of constituent case examples that inform our policy proposals, and which provide the APPG a wealth of knowledge of the problems that exist when businesses attempt to obtain access to justice after experiencing misconduct (or alleged misconduct) by a financial institution."

Early representations about Customer Review

7.31. The day after those involved in the IAR fraud were sentenced at Southwark Crown Court, the APPG's former chair, Mr George Kerevan MP, wrote on 3 February 2017 to an official of the Bank. The letter sought assurances, amongst other things, "that the victims of the fraud will receive proper compensation, as some are still enduring hardship as a result."

7.32. The Bank official responded on 7 February 2017 that the Bank would "take action to review the cases of all those who may have been affected and, where appropriate, to ensure that they are fairly recompensed." The letter went on to explain the appointment of an independent third party as set out in the press release issued that day.

7.33. Mr Kerevan MP replied the same day, noting the importance that any scheme be transparent and established in collaboration with Parliament and other stakeholders. Mr Kerevan MP criticised an RBS redress scheme on the basis that it "is poor when it comes to consequential losses." He highlighted the need to rebuild confidence and to demonstrate transparency."

"I would urge Lloyds to first sit down with the customers who were caught up in the HBOS Reading scam and involve them in designing the redress machinery. Again, both the APPG on Fair Business Banking and our colleagues in the APPG on Alternative Dispute Resolution, stand ready to work with yourselves and the victims to help identify an arrangement in which all parties have confidence."

7.34. In a letter to the FCA's Chief Executive, Mr Andrew Bailey, the following day, 8 February 2017, Mr Kerevan MP made three points as regards compensation payable under the Customer Review: (i) compensation be available to all companies who may have been affected by the events at IAR, not just those who gave evidence in court; (ii) the Bank considers its own culpability when evaluating what compensation is due; and (iii) building arbitration into the compensation scheme.

7.35. On 27 March 2017, Mr Kerevan MP wrote to another official of the Bank that while the Bank had consulted with some affected clients, it had proceeded on its own accord to appoint an independent adjudicator in advance of any consensus on a redress scheme. There was a very strong feeling among those affected that a Bank-appointed independent third party was not acceptable to the victims and certainly not one appointed by the Bank without consultation. Mr Kerevan MP commented specifically on the appointment of Professor Griggs:

"I know him and consider him both reputable and experienced. However his role is undermined by the fact he was appointed by the bank. To be frank, the redress system will have no credibility so long as the bank appoints the judge and sets the terms of redress."

7.36. Mr Kerevan MP suggested as a way "to get back on track" that there be a joint meeting at Parliament with the Bank, MPs from the APPG and key representatives of the IAR fraud victims, plus members of the Chartered Institute of Arbitrators with whom the APPG was working.

7.37. No such meeting was forthcoming. On 5 April 2017, Mr Kerevan MP wrote again to the Bank that its degree of engagement so far had been limited. A series of individual meetings with wronged customers telling them what the Bank was doing was not the premise of an open and constructive dialogue. The Bank appeared to be forging ahead in exactly the way that the APPG had noted to be the worst way forward. While he understood "that this method is designed to limit the bank's liability, it does not address the primary question of due process and fair and proper restitution for victims whose lives have been destroyed". Mr Kerevan MP added that the APPG's offer to act as a facilitator had been ignored. He reiterated his offer to facilitate such a meeting with the APPG and nominated representatives of the victims.

Representations during course of Customer Review

7.38. On 30 July 2017 the APPG's Director of Policy and Strategy, Heather Buchanan, emailed the Bank after a meeting between herself, Lord Cromwell (a vice-chair of the APPG) and representatives of the Bank. In it she stated that the Customer Review had no integrity. That problem could have been overcome by developing the system collaboratively. However, that opportunity had clearly passed, "and the Bank in and of itself quite simply does not have the perceived moral authority to set up its own system and conduct it without transparency, external, independent scrutiny and a system for appeal".

7.39. Ms Buchanan then listed the concerns the APPG held regarding the perceived independence and fairness of the Customer Review, and the "take it or leave it" nature of the offers. At the meeting, the email continued, she and Lord Cromwell had offered suggestions for improvement, including making the methodology used to calculate compensation clear to the victims, ensuring the full disclosure of forensic accountancy reports, the establishment of a credible appeals process, improvements to the clarity of reimbursements for costs and the need for consistency in eligibility for the scheme.

7.40. Responding to the email on 11 August 2017, an official of the Bank stated that in terms of transparency the Bank agreed that providing more information was a valuable improvement and enclosed "before and after" specimen letters showing how the Bank was evolving its approach. The Bank also continued to seek feedback directly from clients who have received outcomes to help improve the experience received.

7.41. The letter responded to the APPG's concerns regarding the lack of an appeals mechanism as follows:

"[C]ustomers have both the opportunity to meet with us and/or Griggs to discuss their outcome and to provide additional information where there are points that they do not believe have been properly considered; this is working well in practice. Whilst this is not an appeal process, for the reasons you have recorded, it does mean that customers have an opportunity to respond, challenge and understand their outcome."

7.42. On behalf of the APPG, Ms Buchanan sent further correspondence to the Bank in October and November 2017 with points raised by constituents. On 12 October 2017 she requested clarification whether the Bank was only offering compensation for D&I and not legal losses, and whether individuals were still able to pursue company losses if they received a D&I payment. A month later she emailed about the Customer Review, including about its scope, the extent to which the Bank disclosed documentation, and its processes and transparency. The Bank replied to this correspondence. It also updated the APPG on progress of the Customer Review. The APPG's records confirm that it remained concerned.

7.43. On 30 July 2018 Mr Hollinrake MP (by then the chair of the APPG) wrote to the Bank, providing a detailed overview of the APPG's concerns. The APPG told me that its concerns remained consistent throughout the duration of the Customer Review and that the letter demonstrated that the Bank had not acted on previous correspondence and meetings to improve its design.

7.44. Concerns raised included that businesses were not provided with access to forensic accounting documentation, that individuals were given "take it or leave it" offers with no discussion of the methodology nor the basis for their calculations, that the eligibility criteria were flawed, that there was no appeals mechanism and that the Bank was withholding payments for legal representation.

Parliamentary debate, December 2018

7.45. On 18 December 2018, the APPG secured a Westminster Hall debate entitled "HBOS Reading: Independent Review".[18] The debate was opened by Mr Hollinrake MP. In the course of his opening contribution, he stated that Bank had used the Customer Review "which is supposedly there to compensate the victims, to minimise payments and perpetuate the cover-up." The Customer Review had been a one-sided, partial process. Mr Hollinrake MP called for an opening up of all the cases that have been through the Customer Review by means of an examination through a completely impartial arbitration process which would fairly adjudicate and arbitrate the claims.

7.46. Quoting the Laidlaw/Tanchel opinion, discussed earlier, Mr Hollinrake MP characterised the Customer Review as flawed and having an appearance of partiality. Mr Hollinrake MP highlighted that on his information only four of the 76 cases had been dealt with by means of D&C loss, with all the rest having been dealt with through D&I. "[I]n other words", he added, "all those businesses were dud businesses. That is simply not

[18] House of Commons Debates, Westminster Hall, Hansard v.651 cc. 271WH-288WH

statistically possible." The Bank's offers were on a take it or leave it basis, which customers without resources had to take. Mr Hollinrake MP continued:

> "The levels of compensation should be determined by an independent third party, not by the bank itself, because there is no methodology. Nobody can contest the findings of Professor Griggs. There is no way of interrogating how he has arrived at a number…The fact is that the victims had no other option—no appeal process—other than going to court, which would have cost millions of pounds…This is in no way an independent process. Of course, everybody who goes to it is subject to a gagging order…"

7.47. As well as raising the cases of individual constituents, other MPs contributing to the debate made points about the opaqueness of the Customer Review process, that customers were powerless because the Bank refused to pay for forensic accounting, that the Customer Review was not properly compensating customers, that it was an internal scheme with complete control held by the Bank and that customers were pressurised to settle and to sign non-disclosure agreements.[19]

7.48. In replying to the debate, the Economic Secretary to the Treasury, John Glen MP acknowledged the concerns that MPs had raised about the Customer Review. Those concerns had been heard. Mr Glen MP announced that the Bank had agreed with the FCA that it would commission a post-completion review to quality-assure the methodology and the process of the Customer Review scheme (this became the Cranston Review). He would closely follow the progress of this quality assurance of the Customer Review.

APPG's submissions to the Cranston Review

7.49. The APPG put to me that it was clear from the correspondence with the Bank (which I outlined earlier) that at all stages in the Customer Review process it had consistently raised concerns from constituents. The key areas, it thought, centred around, firstly, that the Customer Review was designed solely by the Bank with no input from the FCA, other than to approve the appointment of Professor Griggs, and no input from the APPG, despite offers to facilitate meetings with the Chartered Institute of Arbitrators. Instead, all the Bank had done was to host a few meetings with customers to discuss the design of the Customer Review, and simply to tell customers what it would look like.

7.50. Secondly, the APPG said, it had made the point to the Bank that it was denying individuals access to forensic accountants reports and other documentation that has been used to form the basis of its decisions. That prevented their professional advisors from evaluating the true value of their claims and worsened an individual customer's bargaining position.

7.51. Thirdly, customers were often criticised with personal and irrelevant details which not only attacked their character but served to further undermine their bargaining position.

[19] Dr David Drew MP, Mr Colin Clark MP, Mr Edward Vaizey MP, Mr Martin Whitfield MP, Mr Jim Shannon MP, Ms Kirsty Blackman MP, Mr Jonathan Reynolds MP.

7.52. Fourthly, the APPG told me, it had constantly raised the concern that there was no appeals mechanism. Yet the Bank was fully aware that individuals, after being the victims of fraud, were in no position to challenge the Bank in court. The Banks offers were therefore "take it or leave it". There was no follow up meeting, and no discussion of the amount of compensation or the method of its calculation.

7.53. The final point the APPG made to me was that there seemed to be limited consistency in the compensation the Bank awarded. It appeared that individuals were paid compensation based on how much "noise" they could make. Additionally, some individuals appeared to be unfairly excluded since their contact was not with those convicted but with their deputies.

7.54. The APPG summed up by stating that its concerns were not addressed at any point during the course of the Customer Review.

CHAPTER 8 CUSTOMER INPUT TO CRANSTON REVIEW

8.1. This chapter outlines the views of customers about the Customer Review. As I have explained elsewhere in the report, I met 62 customers at interviews, mainly held in London, but also during visits outside the capital. A number of customers wrote to me, but for one reason or the other I did not see them. I spoke to a couple of customers on the telephone. Speaking to customers, as I explain in the following chapter, was central to how I went about fulfilling the Terms of Reference of assessing the Customer Review.

8.2. However, I emphasise at the outset of this chapter that, unlike the sample cases my team examined, the customers I met or otherwise heard from were not a scientifically selected sample. On the contrary, my approach was to offer to speak to everyone who had been involved in the Customer Review. I spoke to those customers who responded to my letter, as well as others (such as those who had not been allowed into the Customer Review) who heard of my review via other avenues, such as the website or press coverage. As such, even though 50 of those I saw or heard from were in the Customer Review, I cannot say whether they were representative of the some 190 individuals the Bank allowed into the review. It may be that it was because they were somewhat discontented that those I saw or heard from contacted me.

8.3. With that qualification, however, an overview of what customers told me had great value. Although for some it meant they had to relive difficult memories, for many, including those who found the experience painful, it provided them an opportunity to express their views about the Customer Review, which in many cases they felt they had been denied previously. For me and my team, their views complemented the information we derived from our examination of the sample cases. Importantly, they also provided insights into and highlighted issues which needed to be more at the forefront of our inquiry.

Outcome of Customer Review pre-determined

8.4. In a number of meetings, customers expressed the view that the outcome of the Customer Review was "preordained" or "predetermined", and that even before customers had made their submissions, the Bank had decided what it was going to pay and to whom.

8.5. Several customers thought it was suspicious that, as a result of the Customer Review, the Bank paid out almost exactly the £100 million it said that it had set aside at the start of the process:

> "Well they announced a big statement, saying "we're going to pay 100 million in compensation", and we're sitting there thinking, well that ain't gonna scratch the barrel. You know, this is crazy. And it just seems apparent that's been the modus operandi throughout, is to stick within that budget."

8.6. One customer thought that the Bank's focus on D&I rather than D&C loss was intended to ensure that the Bank could stay within its budget:

> "I think only just a matter of a few months ago did I realise it was only D&I. Which is perhaps how the bank was able to pluck a figure out of the air and say 'this is going to cost us one hundred million' with some sort of algorithm to help them, I have no idea."

8.7. Many customers felt that, although the Bank invited them to provide additional information once they had received their initial outcome offer, the Bank was unwilling to increase its offers regardless of what customers had to say. A number of customers framed this complaint in similar terms:

> "… we went back and tried to argue and submit more information, which was dismissed. He refused to take that into consideration, or discuss, or anything."

> "I put in my final submission and a very short period of time later I get a standard letter that says we've considered in great detail absolutely everything you've said and doesn't change our mind one jot."

> "… they wrote to me and said they considered the additional information, they now reassessed the estate in consideration of the additional information, and basically, there was no change on the offer, so it was all a complete waste of time."

Customer Review population

8.8. There were a number of those I saw who considered that they had been unfairly excluded from the Customer Review. In general terms this was a criticism that the Customer Review was too limited in its scope. This criticism took various forms. One concerned the limitation of the Customer Review to those who had come into contact with the criminals. Thus the lawyer for one customer told me:

> "[W]hile [X] didn't have the misfortune of meeting Scourfield in subsequent finance meetings, he still suffered financial loss as a result of what then happened."

8.9. Sometimes customers in this position made the point that they dealt with others who worked at IAR under the control of Lynden Scourfield or Mark Dobson. Some customers added that the person they dealt with at the Bank was named in the Project Lord Turnbull Report.

8.10. Conversely, there were those who did come into contact with the criminals but did not qualify for participation in the Customer Review because they were not directors at the relevant time. Thus one of those who came to see me told me that they and another person, X, had been heavily involved in running the business, but at the time were not directors.

> "[W]e're the ones that bore the brunt of the pain of that process. And the ones that were exposed to Alison Mills, and David Mills, and Mark Dobson, who were given unfettered access to all levels of the business. And so, the methodology just seems flawed in that context… [X] who was most involved, and most directly involved with Alison Mills, who was the one convicted, and David Mills, and Mark Dobson… I wasn't officially a director at the time. But I was very involved in the entire process…I was effectively [the company director's] right hand person involved with Alison Mills, with David Mills."

8.11. In this case the sense of injustice was compounded by three factors: first, detailed written evidence had been submitted supporting their case; secondly, directors of the company who did not have this exposure to the fraudsters were compensated; and thirdly, there

was never any compensation for the six months of wasted management time dealing with QCS.

8.12. Another customer had been involved in running the business with his son, but only his son was offered redress. As his lawyer explained to me:

> "this technicality of not being a director, or apparent technicality of not being a director at the relevant time, it appeared, owing to the tick box exercise, put him in a materially different position from his son. […] it was materially unfair."

8.13. The limitation to directors was particularly resented in situations where the business had been built up by a husband and wife but one of the spouses did not qualify for inclusion since they were never formally a director. One customer said his (ex-)wife did not receive an offer:

> "because they're saying she wasn't a director. […] We were both defrauded. We were originally 50/50 partners […]. How Lloyds can say, or Professor Griggs can say 'No. She's not had any distress.'"

8.14. In some cases, after further submissions about the spouse's active involvement in the business, both spouses were compensated equally, although initially the Bank's offer was lower for one. Thus one customer told me they wanted to provide further information:

> "about [X]'s involvement in the business. The only way we could do that is other people's evidence to say that she was involved. Then we had another meeting down in London and they didn't say yes or no. Then we got a letter to say they would increase [X]'s compensation to the same as mine."

8.15. This, like non-inclusion of spouses in the review, was particularly resented where the business had been founded by a husband and wife team. The discrepant treatment of these spouses was a matter of comment.

8.16. Then there were a number of persons who had initially been invited into the Customer Review, but were later told that they did not qualify. In some cases, customers interpreted the payment of £35,000 as an acceptance that they were definitely in the Customer Review, but they were then excluded.

8.17. There were also a number of cases where customers who believed that they were eligible for inclusion in the Customer Review were not contacted by the Bank, and were only invited to participate once they had made contact with the Bank and made themselves known. A number of those customers received significant redress offers as a result. One customer explained their concerns in the following terms:

> "had I not contacted Lloyds and pushed and frankly threatened them, I would not have been accepted into the review. Having been accepted into the review, they offered me a million pounds. It would be an extraordinary coincidence if I'm the only person that didn't meet the criteria to be contacted by Lloyds that was also a victim. And so I think in that aspect too, the whole approach to the review is fundamentally misconceived."

Financial losses not properly considered

8.18. A number of customers felt that the Bank had dismissed their claims for financial D&C losses without giving them due consideration, and that their claims were "not being taken seriously". Several customers complained that the Bank's (erroneous) starting point when considering their claims was that their businesses would have failed in any event. A lawyer who acted for a number of customers said:

> "at a basic, common-sense level it is improbable that each and every company was doomed to fail."

8.19. Other customers were unclear about the purpose of the redress payment offered by the Bank, with one customer in particular believing that it was intended to compensate them for their financial losses (and therefore did not compensate them for D&I suffered by them):

> "I think in retrospect it probably got somewhere near my financial losses. But what it never will do, and certainly it didn't at the time, is compensate me for what I was put through. […]
>
> I feel I got my liquidated damages but not my general damages. There's nothing there that compensated me for the damage, the psychological damage, the harm the behaviour of the bank and Quayside did to me and its consequential effect over many years."

Professor Griggs as independent reviewer

8.20. There were supportive comments about the role of Professor Griggs as the independent reviewer and of the assistance he provided. Thus one customer, who was encouraged by Professor Griggs to submit additional information and as a result received an increase in compensation, wrote to him that:

> "in this whole process, you [Professor Griggs] are the only person from the Review or Lloyds or Bank of Scotland to talk to me like a fellow human being."

8.21. But there were also critical comments about Professor Griggs as the independent reviewer. In some cases, the criticism was that he was put in the position where the appearance of his independence was compromised. One of the customers put it this way:

> "we were in a room with Professor Griggs, and Lloyds Banking Group, and Lloyds Banking Group's lawyers, and everybody else. It felt like they were one team combatting our claim, rather than an independent adviser operating."

8.22. Another customer expressed a similar view:

> "clearly the independence of Griggs was seriously questioned in our mind […] here we are independently meeting Griggs with Lloyds running the meeting, dictating the process and reading from a script."

8.23. A number of customers felt that Professor Griggs was not sufficiently engaged in the process, that he was dismissive or that he was not familiar with their cases. However, others described him as "genuine", "nice", "very accessible", and said that he gave them

tips as to how to frame their submissions so that he could get the Bank to increase their redress offers.

Outcome meetings

8.24. We saw that customers were offered outcome meetings with the Bank and Professor Griggs after they had received their offers of compensation (if any) in the outcome letters. Most, but not all, customers took the Bank up on this offer. However, many customers were disappointed with the Bank's handling of the outcome meetings. Their complaints fall into three categories.

8.25. First, they felt that the Bank made it clear from the outset of the meetings that its offers were non-negotiable and were presented as "take it or leave it" offers:

> "There's also this sort of veiled threat that we thought we were under. It's a take it or leave it offer. If you don't take it now, chances are you're going to lose it and on and on."

8.26. Some customers felt that they were put under pressure by the Bank to accept the outcome offer, and that there was no room for negotiation. Some customers were told that the Bank would not continue to fund their legal costs if they did not accept the Bank's initial outcome offer, and that put additional pressure on them to accept the Bank's offer.

8.27. Second, the Bank did not explain how it had arrived at the figure offered by way of redress. There was no explanation of the Bank's methodology, and it was unclear what information the Bank had taken into account when conducting the Customer Review:

> "they didn't tell us anything. They give us no indication of how it [the compensation] was got to or anything"

> "I might as well have been talking to the picture over there, because the feedback I got from them was nothing. There was no supportive statements or evidence."

8.28. A related criticism made by a number of customers was that the representatives of the Bank who attended the outcome meeting had not been involved in reviewing their submissions or assessing their cases.

8.29. In some cases, customers managed to discern particular aspects of the methodology from the questions asked by the Bank, but they were deeply critical of the methodology:

> "the fact that there was no explanation as to how they work out the figures, it just didn't make sense […] So it depends on the number of meetings with individuals, you know, how many times did your husband meet Lynden Scourfield, how many times did he meet David Mills, how many times did he meet Mike Bancroft? And it just seemed to be such a stupid way of working things out. I mean, you can't base what you're paying someone on the number of meetings they had with somebody."

> "It would appear that he was more interested in the way Dobson spoke to anyone […] That was the criteria of the whole meeting. What did he say to you? How many times did you speak to him? How rude was he to you? This was the criteria of this meeting which I found was ridiculous."

8.30. Third, at the outcome meetings the Bank's representative read from a script, and they felt that there was no deviation from that script or open discussion of what was being said.

> "we've all been at those courses, haven't we? Where basically you're sat down and the guy just literally reads your course notes out to you, and it was like that."

8.31. In addition to these criticisms (which were widespread), some customers also complained about the Bank's treatment of them at the outcome meetings, describing the Bank's representatives as "brutal" and "aggressive".

8.32. A number of customers were made to feel that the Bank considered their losses to be their own fault:

> "The undertone was very much like we were a disappointment to the whole proceedings, we were a bad smell."

> "He was really brutal. [He] all made out like we were in trouble, think it's our fault."

8.33. Another customer put it in the following way:

> "we still felt that we were hoodwinked again. We felt cheated and we shouldn't have felt like that. And it was because they didn't answer questions, because they wouldn't admit anything."

8.34. A number of customers felt that the Bank had not apologised sincerely for what had happened, and that the Bank continued to disbelieve their version of events even after the criminal trial.

Non-disclosure of documents

8.35. Several customers complained about the Bank's position on disclosure. The Bank refused all requests for disclosure, whether they were wide-ranging or limited to specific documents.

8.36. Customers had a number of reasons for requesting disclosure from the Bank. In some cases, they believed that the information they required was contained only in the Bank's records.

8.37. Some customers were concerned that the Bank's records were not reliable, because the fraudsters had created a significant part of the records:

> "if we had seen what he had seen from the bank, especially bearing in mind it had all been tainted in fraud, we may have had some good submissions to say about it."

8.38. Other customers were at a disadvantage simply because the companies in question were long since dissolved, or they no longer had access to the documents.

Settlement agreements

8.39. The situation was compounded by the settlement agreements which customers were required to sign. These agreements contained provisions which prevented former co-directors of a company from discussing their complaints with one another and, as I

explain below, were cause for further complaint. A number of customers complained that these terms were unfair.

Time limits imposed on customers

8.40. Some customers were impressed by the swiftness with which the Bank dealt with their cases. However, they were in the minority. A number of customers complained that the Bank had imposed unrealistic deadlines on them for the provision of information, and for their decision to either accept or reject their redress offers.

Conclusion

8.41. Very few customers I met or who contacted me had a positive experience of the Customer Review. As I said earlier, I must allow for the fact that I did not meet with or hear from every customer who participated in the Customer Review, and also perhaps that those who were dissatisfied were more likely to get in touch with me to voice their views. However, I did meet a large number. The vast majority were unhappy with the process and with the offer of redress made by the Bank. The same complaints were made by many customers, as is evident from this overview. Overall, customers made clear to me that they were dissatisfied with the Bank's handling of the Customer Review.

PART D ASSESSMENT OF BANK'S CUSTOMER REVIEW

CHAPTER 9 PRINCIPLES OF ASSESSMENT OF CRANSTON REVIEW

9.1. In this chapter I set out in greater detail than in Chapter 1 how I went about the task of assessment. It will be recalled that my Terms of Reference require me to consider, amongst other things, whether:

(i) the methodology and process developed for the Customer Review achieved the purpose of delivering fair and reasonable offers of compensation and was consistently applied in accordance with established principles of Treating Customers Fairly;

(ii) the judgements that were made on individual customer cases were fair and reasonable, including in relation to the assessment of direct and consequential losses;

(iii) the overall level of compensation to customers was fair and reasonable when compared to the damages likely to have been available through a court process;

(iv) Professor Griggs exercised appropriate levels of independent challenge over customer outcomes, ensured that offers to customers were reasonable and was able to properly perform his role; and

(v) The Customer Review methodology provided a reasonable basis on which to deliver fair outcomes and offer swift and generous compensation, taking into account various aspects of the Customer Review methodology and process, including the reasonableness of decisions in relation to professional advisor costs and whether the terms and conditions included within Settlement Agreements were fair and reasonable.

9.2. Part I explains how I interpreted the requirement of "fair and reasonable" which runs as a thread through these Terms of Reference.

9.3. Part II then turns to the requirement in my Terms of Reference that I sample cases. It will be recalled that they require me to assess the methodology of the Customer Review through a representative sampling of cases. The second part of the chapter explains how the sampling was undertaken and how my team set about the task of examining the sample cases.

9.4. Part III deals with the submissions I received from customers and the meetings I had with them. What customers said has been summarised earlier in Chapter 8. What the discussion in this chapter sets out are the details of how I received the submissions and conducted the interviews. As I have already explained, I regarded customer input as a crucial part of the assessment process.

I "FAIR" AND "REASONABLE"

9.5. Under the Terms of Reference, the standards of "fair" and "reasonable" regularly appear. Although there is no binding interpretation, let me explain how I have interpreted "fair" and "reasonable".

"Treating Customers Fairly"

9.6. A starting point is the standard of Treating Customers Fairly which the FCA imposes on financial services firms. The Bank told me that it took both the Treating Customers Fairly and Customers in Financial Difficulty standards as relevant in assessing customers in crisis in its Customer Review. Principle 6 of the FCA's Principles for Businesses provides that "a firm must pay due regard to the interests of its customers and treat them fairly".[20] All firms regulated by the FCA (including banks) are required to comply with the Principles for Businesses.[21] Whilst various rules and guidance in the FCA Handbook amplify Treating Customers Fairly with respect to the carrying on of specific financial services activities,[22] the Handbook does not contain generic guidance on the meaning of the term. The FCA has not been prescriptive as to the meaning of Treating Customers Fairly in determining what amounts to fair treatment contained in Principle 6.

9.7. However, the FCA has set out six outcomes that it expects firms to strive to achieve to ensure the fair treatment of customers. The Treating Customers Fairly outcomes are focused on the sale and after-sale of retail products and on the firms involved in the sale, provision and distribution of such products. They are therefore not readily applicable to the Customer Review, which, as I have explained, was a bespoke scheme for customer redress. However, they have informed my interpretation of what is "fair and reasonable".

9.8. Three of these outcomes (using the FCA numbering) are: Outcome 3, consumers are provided with clear information and are kept appropriately informed before, during and after the point of sale; Outcome 5, consumers are provided with products that perform as firms have led them to expect, and the associated service is of an acceptable standard and as they have been led to expect: and Outcome 6, consumers do not face unreasonable post-sale barriers imposed by firms to change product, switch provider, submit a claim or make a complaint.

9.9. Underlying the Treating Customers Fairly outcomes are types of conduct which are indicative of fair treatment of customers. I have used these to inform my assessment of the Customer Review.

9.10. Such conduct includes:

(i) Clear communication with customers and the provision of appropriate information (Outcome 3). The FCA considers[23] that Outcome 3 is linked to another one of its Principles for Businesses which requires a firm to "pay due regard to the information needs of its clients, and communicate information to them in a way which is clear, fair and not misleading" (Principle 7).[24]

[20] The FCA's Principles for Businesses ("PRIN"), 2.1.1R.
[21] PRIN, 3.1.1R.
[22] e.g., the Banking: Conduct of Business Sourcebook ("BCOBS"), 5.1.3AG in relation to retail banking and the Mortgage and Home Finance: Conduct of Business Sourcebook ("MCOB"), 4.2.1G.
[23] FCA Discussion Paper (DP 14/2), *Fairness of changes to mortgage contracts* (July 2014), paragraph 2.15.
[24] PRIN, 2.1.1R.

(ii) Honouring of representations and assurances given to a customer (Outcome 5). This means, for example, that the methodology and process designed for the Customer Review had to take into account the representations made and assurances given to customers and that the methodology had to be applied in a way that customers were led to believe it would operate.

(iii) Being reasonable about putting right things for which one is responsible and which have gone wrong (Outcome 6). I consider that this required, for example, that where, as part of the Customer Review methodology or process requirements were placed on customers, those requirements had to be appropriate in the circumstances and not unduly onerous.

"Fair" and "reasonable"

9.11. In my Terms of Reference, "fair" and "reasonable" are used in different contexts. For example, I am required to consider whether the Customer Review methodology and process achieved the purpose of delivering "fair and reasonable offers of compensation" for customers, whether the methodology provided a "reasonable basis on which to deliver fair outcomes" and whether terms included in settlement agreements were "fair and reasonable".

9.12. The meaning of the terms "fair" and "reasonable" depends on the context in which they are used. Let me begin with the natural and ordinary meaning of the terms before turning to how they have been interpreted in a number of different contexts.

Fair

9.13. "Fair" is a word which is commonly used and which, instinctively, most customers understand. However, it is difficult to define it precisely. With respect to conduct, actions, methods, and arguments the Oxford English Dictionary defines "fair" as "free from bias, fraud or injustice; equitable, legitimate, valid, sound."

9.14. In respect of remuneration, reward or compensation, the dictionary defines it as that which "adequately reflects the work done, service rendered, or injury received." When used in relation to conditions or circumstances, its meaning includes "not unduly favourable or adverse to anyone".

9.15. Fairness can relate to process as well as outcome. For example, a contract may be regarded as unfair because of the manner in which it was brought into existence or because of the effect of its terms.[25]

9.16. What is "fair" in any case will depend, of course, on the circumstances.[26] For example, what amounts to a fair offer of compensation will depend on a range of factors. These will include the level of harm or loss suffered by the customer, the nature and gravity of the conduct causing the harm and the level of compensation which may be awarded by a court in the particular circumstances.

[25] *Hart v O'Connor* [1985] 3 WLR 214, 224.
[26] *Manning v Ramjohn* [2011] UKPC 20, [39].

9.17. When judging what fairness required in the context of the Customer Review, the relevant circumstances include the nature of the Customer Review itself. It was a non-legal process intended to be speedier and at lower cost to customers than litigation. What is required to achieve fairness in this type of process will not be identical to what is required to achieve fairness in litigation.

9.18. Determining what is fair often involves the balancing of competing interests. For example, in relation to the fairness of contract terms, the legitimate need of one party to protect its interests must be weighed against the disadvantage caused to the other party as a result of the application of the terms.

9.19. As well as having regard to its dictionary meanings, I have also drawn upon statements made by judges and provisions of UK legislation as to what fairness may require and what may be regarded as unfair.

(i) Where a decision which may adversely affect a person is being taken, fairness may require that the person is given the opportunity to make representations either before the decision is taken, with a view to producing a favourable result, or after the decision is taken, with a view to procuring a modification. To enable effective representations to be made, fairness may also require that the person be informed of the gist of the case they have to meet.[27]

(ii) In the context of the relationship between a creditor and a non-commercial debtor, a sufficiently extreme inequality of knowledge and understanding is regarded as a "classic source" of unfairness.[28] The same might be said of other relationships where there is a significant disparity in the bargaining positions of the parties.

(iii) The Consumer Rights Act 2015 deals with the issue of fairness in the context of terms in a contract between traders and consumers.[29] The Act provides that a term is regarded as unfair if, contrary to the requirement of good faith, it causes a significant imbalance in the parties' rights and obligations under the contract to the detriment of the consumer. The Act requires that the fairness of a term is to be determined taking into account the nature of the subject matter of the contract and by reference to all the circumstances existing when the term was agreed, and to all of the other terms of the contract or of any other contract on which it depends.[30] The fairness test under the Consumer Rights Act 2015 has two key elements: (i) significant imbalance in the parties' rights and obligations; and (ii) good faith.[31] The "significant imbalance" element is consistent with the ordinary meaning of "fair" taken from the Oxford English Dictionary. Good faith has been described as a principle of "fair and open dealing"[32]. In the context of contractual relationships, the requirements of good faith have been said to include adherence

[27] *Doody v Secretary of State for the Home Department* [1993] 3 All ER 92, 106.
[28] *Plevin v Paragon Personal Finance Limited* [2014] UKSC 61; [2014] 1 WLR 4222, [18].
[29] A consumer is defined in section 2(3) of the Consumer Rights Act 2015 as an individual acting for purposes that are wholly or mainly outside that individual's trade, business, craft or profession.
[30] Consumer Rights Act 2015, sections 62(4) and (5).
[31] *Director General of Fair Trading v First National Bank plc* [2001] UKHL 52, [2002] 1 All ER 97, [36].
[32] *Interfoto Picture Library Ltd v Stiletto Visual Programmes Ltd* [1988] 1 All ER 348, 352.

to the spirit of a contract, faithfulness to an agreed common purpose and acting consistently with the justified expectations of the parties.[33] Although the Consumer Rights Act 2015 deals with fairness in a specific context, I consider that it provides useful guidance as to how the issue of fairness may be approached more generally.

(iv) In considering what is fair, I have also had regard to the indicators of fairness which I have drawn from the FCA's Treating Customers Fairly Outcomes. These include clear and adequate communication with customers and honouring assurances and representations made to customers. As to the assurances and representations made by the Bank, I have considered, in particular, the statements the Bank made about the Customer Review in its press releases dated 7 February 2017, 20 March 2017, 7 April 2017 and 26 April 2017.

Reasonable

9.20. As with "fair", "reasonable" is a word that is commonly used. It is also a familiar standard to lawyers. However, as with fairness, what it requires will vary with the circumstances.[34] The Oxford English Dictionary definition of "reasonable" includes "within the limits of what it would be rational or sensible to expect; not extravagant or excessive; moderate" and "in accordance with reason; not irrational, absurd, or ridiculous; just, legitimate; due, fitting".

9.21. Rationality is one aspect of the public law assessment of reasonableness (of actions taken by public bodies). In particular, when reviewing the actions of an administrative decision maker, the court reviews whether the decision maker has taken into account matters which it ought not to have taken into account or has failed to take into account matters which it ought to have taken into account.[35] In my view such considerations are relevant when assessing, for example, whether the decisions made by the Bank on individual cases in the Customer Review were reasonable.

9.22. Reasonableness, as with fairness, can relate to both process and outcome.

9.23. There are guidelines contained in the Unfair Contract Terms Act 1977 as to the assessment of "reasonableness" which applies to certain terms.[36] These are relevant in considering the reasonableness of the terms of the settlement agreements with customers. A factor that applies in the context of the Unfair Contract Terms Act 1977 which I consider to be particularly relevant in the context of the Customer Review is the relative bargaining strength of the parties.

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[33] *CPC Group Limited v Qatari Diar Real Estate Investment Company* [2010] EWHC 1535 (Ch), [246]
[34] *Ashworth Frazer Ltd v Gloucester City Council* [2001] UKHL 59; [2001] 1 WLR 2180, [67].
[35] *Associated Provincial Picture Houses Limited v Wednesbury Corporation* [1948] 1 KB 223, 233-234; *Braganza v BP Shipping Limited and another* [2015] UKSC 17,[24].
[36] Unfair Contract Terms Act 1977, Schedule 2.

II SAMPLE CASES

9.24. The Terms of Reference required me to undertake a detailed review of a number of cases on a representative sample basis. The Terms of Reference stated that this was to ensure that the methodology of the Customer Review was consistently applied and that outcomes were fair and reasonable.

9.25. Given the number of businesses and individuals within the Customer Review and my desire to complete the Cranston Review in a reasonable time frame, it would have been impractical to consider all cases in detail. Ensuring that a representative mix of cases was examined has meant that my team and I have been able to identify issues and deficiencies within the Customer Review, either in its methodology or in its application. These are dealt with in the following chapters. What I do here is to set out how we constructed our sample and how we then went about examining those cases which were part of it.

Sampling methodology

9.26. I asked my financial advisers, FTI, to develop a suitable sampling approach based on the overall population of individuals within the Customer Review. Following discussions with the Bank and Professor Griggs, my team and I identified 14 key characteristics on which to base my sample selection, being:

(1) Cases with the highest level of redress payment;

(2) Cases with the lowest quantum (non-nil) of redress payment;

(3) Five cases from the start of the Customer Review process;

(4) Five cases from the end of the Customer Review process;

(5) Cases with multiple rounds of additional information;

(6) Nil outcome cases;

(7) Cases where the settlement offer was rejected;

(8) Cases where Professor Griggs applied his override or uplift;

(9) Cases represented by the SME Alliance;

(10) Cases where Professor Griggs initially disagreed with the outcome proposed by the Bank;

(11) Cases increased or decreased as a result of the Bank's consistency checking procedures;

(12) Cases with large volumes of files;

(13) High profile cases which were included in the trial charge sheet for the criminal trial; and

(14) Customers that were not legally represented (prior to receiving the Bank's offer of redress).

9.27. These characteristics, whilst not intended to be exhaustive, allowed the selection of a diverse and representative sample of businesses which would in turn allow for a meaningful sample of directors across the entire Customer Review population.

9.28. At my request, the Bank then provided a database of all individual directors within the population with flags for each of the 14 categories identified above. My financial advisers then took the Bank database and constructed a so-called front end sampling model to generate a sample population for my team to review.

9.29. In order to limit sampling bias within the section of sample directors, the directors contained within each stated characteristic were assigned a random number via a random-number generator. These numbers were then sorted to provide a ranked list from highest to lowest. This ensured that random directors within each characteristic were sampled.

9.30. In addition to this, and to ensure that a manageable sample of directors was obtained, some directors were added to the sample population because they exhibited multiple sample characteristics. This was also intended to ensure that a number of the most complex and challenging cases were captured as part of my review.

Sample population

9.31. My initial sample population consisted of 20 distinct businesses and 26 unique directors. This represented 28% of the total number of businesses and 14% of the total number of directors covered by the Customer Review.

9.32. As the detailed sample-review work proceeded, by the end of July two issues with the original approach had become apparent:

(i) The same methodological issues were arising in many of the 25 meetings I had held by that point, and there were another 15 meetings scheduled. In my opinion, it was important to analyse which of these warranted further investigation and analysis; and

(ii) The financial and legal review of the files was taking longer than initially anticipated, such that I considered that the initial timetable for completing my review would be significantly exceeded (particularly when the additional issues just referred to had to be considered).

9.33. As such, I reconsidered the sampling approach with the assistance of my financial and legal advisers. We examined whether it could be possible to reduce the overall sample size without compromising the focused review of the issues identified during customer meetings, such that the overall integrity of the work would not be diminished.

9.34. As a starting point, my legal and financial teams advised me that any revised sample population would need to include, as a minimum, at least one individual director within each of the 14 categories originally identified (as set out earlier, and which were still considered to be valid categories).

9.35. Applying this approach enabled the initial sample population to be reduced from 20 businesses (and 26 unique directors) down to 15 businesses (with 20 unique directors).

9.36. I then reviewed the issues arising from customer meetings in order to decide whether any businesses (and specific methodological issues) warranted further investigation or analysis. This review identified eight additional businesses with specific issues which warranted further investigation. With the teams' help I also concluded that one of the cases identified merited inclusion in the sample population for a full review.

9.37. Taking all this into consideration we ended up with a revised sample population of 16 businesses and 21 unique directors for a full financial and legal review. That gave us a coverage of 23% and 11% respectively of the total population. Set out below is a table which summarises the number of directors selected within the revised sample population and the total population within each characteristic:[37]

Ref	Sampling Characteristic	Total No. Directors*	Total Population Size	% Sampled
1	Cases with highest level of redress payment	5	5	100%
2	Cases with lowest quantum (non-nil) of redress payment	1	16	6%
3	5 cases from start of review process	1	5	20%
4	5 cases end of review process	1	7	14%
5	Cases with multiple rounds of additional information (impacting and non-impacting)	5	18	28%
6	Nil outcome cases	1	33	3%
7	Cases where settlement offer was rejected	2	4	50%
8	Prof. Griggs override / uplift	7	17	41%
9	Cases represented by the SME Alliance	5	11	45%
10	Cases with initial settlement offer disagreement between Lloyds and Prof. Griggs	5	45	11%
11	Cases increased or decreased as a result of Lloyds consistency check	1	10	10%
12	Cases with large volumes of files	3	12	25%
13	High profile / included in trial charge sheet	6	16	38%
14	Customers that were not legally represented (prior to LBG offer of re-dress)	13	114	11%
		56	**313**	**18%**

9.38. After taking account of the additional eight businesses where focussed work was undertaken, my team and I have undertaken detailed work on, in total, 24 businesses, representing 31% of the total population.[38] The advice of my financial advisers, which I accept, is that this was a sufficient number of cases to examine.

Examining the sample cases

9.39. Once we had the sample cases, my team then had to devise a detailed work plan to examine the files associated with each case. How we did this, and the key areas covered, are as follows.

9.40. First, we conducted a full review of the contemporaneous records identified by the Bank's "file build" process, to ensure that: (1) all such documentation and information had been properly considered and, where relevant, appropriate conclusions had been drawn; (2) any inconsistencies in the information contained on the files had been properly investigated; and (3) any apparent gaps in the information contained on the files had been adequately followed up (through, for example, the undertaking of additional searches of the electronic document repository).

[37] It should be noted that directors may exhibit more than one of the characteristics and that there are businesses with more than one director (who may also exhibit different characteristics to each other, depending on the specific circumstances of the case).

[38] The percentage discrepancy is because two of the businesses considered for additional investigation were never included within the original Customer Review population.

9.41. Secondly, we reviewed and assessed the Customer Review documentation. This was the documentation created by either customers or the Bank during the course of the Customer Review. It included, amongst others, the Bank's detailed assessment template; the Quality Control pack (an internal Bank document which summarised the circumstances of the case and proposed outcome for the purpose of management challenge and approval); submissions provided by customers to the Bank (which could take the form of completed questionnaires, other written submissions or notes of "fact finding" meetings between the Bank and the customers); any correspondence between the Bank and the customer (and, where applicable, their lawyers) including outcome letters; and correspondence between the Bank and Professor Griggs.

9.42. Thirdly, we considered the submissions of customers provided directly to my Review, whether in writing or from meetings which I held with individual customers.

9.43. Fourthly, we critically assessed the D&I matrix and its application in each case and re-performed the calculation.

9.44. Coupled with that, fifthly, we critically analysed how the Bank assessed D&C loss, in particular by reference to the heads of loss claimed. I return to these matters in Chapters 12 and 13 below.

9.45. Sixthly, we considered the process the Bank adopted with each of the sample cases. That covered a range of matters such as the initial contact with the customer, the nature of the customer's input into the Customer Review and how it was addressed, the outcome letters and outcome meetings and the extent to which there was a variation in the initial offer and how that came about. These procedural matters are canvassed in the following chapter.

III STATEMENTS FROM BANK, PROFESSOR GRIGGS AND STAKEHOLDERS

9.46. As I explained in Chapter 1, in the early stages of the Cranston Review, my advisors and I held a number of fact-finding meetings with the Bank and, separately, with Professor Griggs and his legal team. However, I decided to request that both the Bank and Professor Griggs make formal contributions by way of written submissions. The Bank and Professor Griggs agreed, and I sent a written request to both detailing the topics I wanted them to cover.

9.47. The written submission from the Bank was received on 28 June 2019 and that from Professor Griggs on 4 July 2019. Following the initial submissions, follow-up requests (either in the way of clarifications on points in their initial submissions, or new points which subsequently arose) were sent to both the Bank and Professor Griggs. In the case of the Bank, there were a number of follow-up submissions as further points needed to be explored.

9.48. Additional submissions from the Bank were received on 1 August 2019, 10 September 2019, 16 September 2019, 3 October 2019 and 11 October 2019. The follow up submissions from Professor Griggs were received on 2 August 2019 and 29 August 2019. Both the Bank and Professor Griggs addressed the follow-up matters.

9.49. In addition to the written submissions, during the course of my review my financial advisers sent the Bank ad hoc and detailed queries in respect of specific issues arising on individual customer assessments and meetings. Again the Bank responded to the questions raised. As I have noted in chapter 1, both the Bank and Professor Griggs submitted comments and factual corrections in relation to the text of my draft report.

IV CUSTOMER SUBMISSIONS AND INTERVIEWS

9.50. From the outset it was my intention to make submissions from customers who had participated in the Customer Review central to my review. That was in addition to the input from stakeholders such as the SME Alliance and the APPG.

9.51. As we saw in Chapter 8, what customers told me has highlighted issues relevant to my Terms of Reference. One case was of sufficient interest that I subsequently included it within the sample population so that it could be thoroughly examined. As I explained earlier, the relevance of the issues raised in the submissions of customers was a major reason for having to postpone the date of publication of this report.

9.52. As regards written submissions, many customers gave me what they had prepared for the Customer Review itself and the associated correspondence and documents. However, I received 21 submissions specifically drafted in response to the letter I sent to all customers on 7 June 2019, where I included my Terms of Reference. There were 20 submissions from customers who did not subsequently have a meeting with me. The reasons for this varied: some customers did not want a meeting; some regarded their submission as sufficient; and in a few cases the customer resided abroad.

9.53. I had 49 meetings in the course of which I met 62 customers. They were held in the main at 3VB, as I have said in Chapter 8. The exceptions were when I travelled outside London to six meetings in Oxford, Milton Keynes, Norwich, and Bristol. At 22 meetings, lawyers representing the customer were present. On two occasions I spoke to customers over the phone. There were four meetings attended by the customer's lawyer, without the customer.

9.54. In all cases the atmosphere of the meetings was informal. They were loosely structured. I sought to remind customers near the outset that I was independent and not acting as an appellate body, and to cover issues such as the nature of their engagement with the Bank during the Customer Review and the role of Professor Griggs. On average the meetings lasted about an hour.

9.55. I was contacted by 11 of the 21 sample directors. Meetings were held with eight of them, either in person or with their representatives. I was also contacted by an additional four customers who were non-sample directors of a sample business. These meetings offered added value to the analysis of the files.

9.56. On 30 occasions I requested further information or documents from customers, typically informally at the meeting with them. After eight meetings with customers I requested further information from the Bank.

V CONCLUSION

9.57. In this chapter I have explained how the work on selecting and examining the sample cases was undertaken under the Terms of Reference. I have also summarised how I obtained input from the Bank, Professor Griggs, stakeholders and customers in the Customer Review.

9.58. Importantly, I have set out my approach to assessing whether what the Bank did was fair and/or reasonable. That has involved considering a number of factors which have varied depending on the aspect of the Customer Review that I was assessing, and then exercising a judgment as to their application in particular cases.

9.59. The factors include the clarity and adequacy of the Bank's communications, whether the Bank acted in good faith (in particular, whether it was open in its dealings with customers), the extent to which the Bank honoured representations and assurances it gave to customers, the level of harm or loss suffered by customers, what the likely outcome would have been if a customer's case had been considered by a court, whether customers had adequate opportunity to make representations, whether the Bank considered irrelevant matters or failed to consider relevant matters, and the relative bargaining positions of the Bank and its customers.

CHAPTER 10 BANK'S PROCEDURES AFFECTING CUSTOMERS

10.1. The Terms of Reference for my review require me to evaluate the Bank's approach in the Customer Review in relation to various procedural matters which directly affected customers. These matters are separate from the issue of compensation – dealt with in Chapters 12 and 13 below - although they have a bearing on it.

10.2. This chapter therefore addresses the Bank's approach to the following matters with respect to the Customer Review:

(1) communicating with customers, including the clarity of the process and the time provided for customers at each stage of the process;

(2) disclosure of the Bank's methodology and of its records;

(3) supporting customers, including the reasonableness of decisions in relation to professional advisor costs;

(4) the Bank's explanation of customers' outcomes in outcome letters and at outcome meetings, and the opportunity for customers to provide additional information for consideration by the Bank and Professor Griggs if they disagreed with their outcome at first instance; and

(5) Professor Griggs' role as independent reviewer.

10.3. The assessment draws on what the Bank told me in explanation of its approach to these various matters, the views of customers and the information which emerged from examining the sample cases. I should explain that although there is reference to the role of additional information in the process, I explore this in greater detail in Chapters 12 and 13.

10.4. The Terms of Reference also require me to assess the role of Professor Griggs. That is done in greater detail in the following chapters, but I say something in this chapter about his role as the independent reviewer and how this was explained to customers.

I COMMUNICATING WITH CUSTOMERS

10.5. During the course of the Customer Review, the Bank was in regular contact with customers, both individually and as a whole. That was by letter, and through meetings with individual customers, information mediated through the SME Alliance and the APPG, and in press releases.

Initial design of Customer Review

10.6. The Bank announced the establishment of the Customer Review on 7 February 2017. As I explained above, it wrote to a number of high-profile IAR-affected customers a few weeks later to elicit their views on how the Customer Review process might work. There were several meetings in early March 2017, which the Bank told me were helpful in designing the Customer Review, particularly in relation to the way in which customers would interact with it and the independent reviewer.

10.7. Both the APPG and the SME Alliance told me that, had the Bank consulted more seriously on the scope and methodology of the Customer Review at the outset, some of the later criticism could have been avoided.

10.8. At the time, the Bank's view seems to have been that any more consultation than it undertook would have delayed matters, and it was vital to start making compensation offers as early as possible.

10.9. With hindsight, that view can be seen as misguided. The Bank told me that it now accepted that consulting more broadly up front with a wider group of stakeholders might have reduced some of the criticisms levelled at the Customer Review.

Clarity of communications with customers

10.10. Any communication from the Bank had to be accurate, readily understandable and not such as to distort the reality of the position as known by the Bank. The initial communications from the Bank were clear. The Bank's press releases about the Customer Review always attracted substantial media coverage. Its early letters to customers were straightforward and welcoming. It appointed relationship managers for each customer to be a point of contact and source of information.

10.11. A basic error at the outset, however, was the failure to publish the terms of reference for the Customer Review.

10.12. A constant theme of what customers told me, and in the submissions of the SME Alliance and the APPG on Fair Business Banking, was that the Bank did not explain matters, in particular the scope of the review population and the methodology for calculating compensation. There was also some confusion about the role of Professor Griggs and his power to overrule the Bank's awards.

10.13. To customers there also seemed to be contradictions in the Bank's messages. For example, the Bank had said that it would fund financial advice, but then in the main refused customer applications to employ a forensic accountant. The Bank had said that it would be compensating those impacted by the IAR fraud, but then confined awards to the directors of business customers that had been in IAR. The Bank apologised to customers for the IAR fraud, and expressed sympathy, but conveyed the message at outcome meetings that the failure of their business was the customers' own fault. The Bank and Professor Griggs encouraged additional information at outcome meetings, but then seemed to ignore it. These views of customers I return to at various points below.

10.14. At this point I simply need to record the Bank's acknowledgment that, with hindsight, customers might have benefitted from a website that contained information on the Customer Review process. The Bank told me that it could have been a useful way to explain aspects of the Customer Review in greater detail and reduce the risk of customer confusion. The Bank said that the website could have included more detailed information explaining how the Customer Review operated, including guidance on legal claims, customer submissions and the disclosure of documents. It could also have been used to increase understanding as to the role of Professor Griggs. All this is undoubtedly correct.

10.15. There were a small number of customers whom the Bank failed to contact but who were later included in the Customer Review after hearing about it from third parties or in the media. A few expressed surprise since some still banked with one of the Lloyds Banking Group entities. The explanation may be that they fell into Cohort 3 in the methodology for defining the review population and therefore needed to complain to be included. However, this was never fully explained. I return to the separate issue of the steps the Bank took to trace customers in the following chapter.

The customer questionnaire

10.16. As we saw in Chapter 3, following the initial communications customers were sent, by post, a detailed questionnaire which they were encouraged to complete for the Bank to assess their case in the Customer Review. Completion of the questionnaire was not mandatory, and customers were able to provide additional written submissions and information via other means, notably in meetings with the Bank or through written submissions with the assistance of a lawyer they had engaged.

10.17. In my view the questionnaire produced by the Bank was reasonably clear, relatively straightforward to follow and explained the reasons why certain information was being requested. Moreover, the Bank made clear that information could be submitted by other means best suited to the individual customer.

10.18. The use of hard-copy questionnaires suffers from the inherent drawback of implicitly guiding individuals as to the length of their submission (by virtue of the size of the available space), not only in absolute terms but also relative to other questions (i.e. a larger text box for one question as compared to another may imply a higher degree of importance or an expectation of greater detail being provided for that question over another). The boxes on the questionnaires were very small (no more than a couple of centimetres deep in each case). The Bank attempted to mitigate this risk by allowing electronic completion of the questionnaire (this was used by 111 of 136 customers) and alternative free-form submissions.

10.19. However, given the limited disclosure of the detail of the Bank's methodology, and the basis on which distress and inconvenience ("D&I") awards (and direct and consequential ("D&C") compensation) were to be made and assessed, further guidance to customers as to the level of detail, and the extent of reliance that would be placed on supporting evidence, would almost certainly have proved beneficial to them. This, in my view, reduced the overall effectiveness of the questionnaire as a tool for ensuring that the information customers were invited to provide was sufficiently detailed to allow them to achieve the highest redress possible, as a result of the information provided in the questionnaire itself.

Timeframes in the Customer Review

10.20. The Bank established an ambitious timeframe for the completion of the Customer Review process. As explained earlier the Bank envisaged that each customer's participation in the Customer Review would be completed within less than four months.

In fact the process of making awards took far longer than anticipated. For example, customers generally took longer to submit information than was envisaged, with an average period of nearly four months to receive customers' initial submissions. The last outcome letter was issued on 1 April 2019 and the Customer Review was formally concluded on 7 May 2019 on the announcement of my appointment.

10.21. Nonetheless, some customers who saw me felt that the Bank's timescales were too tight, and that they had felt under pressure to submit information and to make a decision regarding their outcomes.

10.22. One particular concern raised with me was that the Bank did not reassure customers that their outcome offer would remain open beyond the 28-day time limit if they wished to put in additional information. Having looked at the Bank's written communications with several customers, I think the Bank made clear that, if the customer wished to submit additional information, they would be permitted more time.

10.23. As to the general criticism that the Bank put pressure on customers to progress rapidly through the Customer Review process, I am not persuaded that this was the case overall, although it may have been the perception that customers had in particular cases. In a number of cases, the Bank agreed to permit customers significant extensions of time to make their submissions, provide additional information or consider their outcome offers. In one sample case, the Bank agreed to numerous extensions to the period for consideration of the outcome offer, totalling almost ten months. In another sample case, the period for consideration of the outcome offer was extended by eleven months.

10.24. With hindsight, the Bank accepted that its original timeframe was unachievable given that most customers required considerably longer than it had anticipated. It acknowledged that more careful consideration could have been given to what was publicly stated at the outset of the Customer Review.

£35,000 customer payments for delay

10.25. It will be recalled that the longer than anticipated time the Customer Review was taking was the reason the Bank made the £35,000 payment in late June 2017. It was on an ex gratia basis to all those in the Customer Review. The Bank is to be commended for making those payments, which were not deductible from any compensation paid.

II THE POLICY OF NON-DISCLOSURE

10.26. A constant theme of customers' and stakeholders' complaints was that the Bank never explained the methodology of the Customer Review, why customers were included and how compensation was calculated. In particular, there was criticism of the policy the Bank adopted of not disclosing documents it had in its possession, which customers needed in order to advance their case.

Non-disclosure of Bank's methodology

10.27. A recurrent theme in the meetings I had with customers was that the methodology, terms of reference, criteria for inclusion and documents on which the Bank relied in its

decisions on compensation were not communicated to them. I have given the flavour of this criticism in Chapter 8. Stakeholders such as the SME Alliance and the APPG regularly raised the lack of transparency of the scope and methodology of the Customer Review.

10.28. In response to the specific criticisms in the Laidlaw/Tanchel opinion about the failure to disclose the scope and methodology of the Customer Review, the Bank said that detailed explanations of the Review methodology had been provided to the APPG, Treasury Select Committee and FCA. I am unable to agree with this. Neither the APPG nor the Treasury Select Committee were provided with details of the methodology for determining the Customer Review population or D&I compensation.

10.29. In one of its methodology documents, the Bank said this about disclosing the methodology for calculating compensation:

> "[The Bank] will not disclose the methodology, the contents of the file build or how the outcome has been calculated. This is in keeping with its desire to communicate fair outcomes without incurring unreasonable delays as part of a process that is designed to be as straightforward as possible."

10.30. The Customer Review was a without prejudice, non-legal scheme for providing redress to those impacted by the IAR fraud. The Bank had the laudable aim of compensating those impacted by the IAR fraud as swiftly as it could. It had the legitimate reason of seeking to avoid lengthy arguments over the application of its methodology which would no doubt have occurred once it was disclosed.

10.31. Nonetheless, it seems to me that the information needs of customers included at least some explanation by the Bank of: (a) the basis on which their claims for compensation would be assessed; and (b) the outcome of the assessment of their case explained in sufficient detail to enable them to understand the reasoning, and to challenge it if necessary. Just how far this should have gone in practice is best left for the discussion in Chapters 12 and 13.

Non-disclosure of Bank's records

10.32. In the course of the Customer Review, the Bank took the approach that disclosure of documentation to customers was not appropriate. In response to a specific concern raised in the Laidlaw/Tanchel opinion that the Customer Review should have complied with the common rules of procedure and fairness concerning disclosure, as are applied by the courts and other factfinding tribunals, the Bank explained as follows:

> "The Review was set up as a voluntary compensation scheme, overseen by an independent reviewer, to help customers receive fair, swift and appropriate compensation […].
>
> Whilst disclosure of documents is a feature of a litigation process, it is not required in a voluntary compensation scheme such as the Review. The [Bank] considers that it provided to Professor Griggs all information that it identified as relevant to each case in order to ensure fair determinations and for him to take account as appropriate."

10.33. The Bank further explained to me that it considered that the Customer Review process protected against any disadvantage to the customer arising from the position on disclosure:

> "It was recognised that in addition to the advantages of the Review process in terms of the payments considered, and the time to receive compensation, there were also potential risks with the approach adopted. The [Bank] sought to mitigate these risks by design and/or by enhancements in the process throughout the Review. For example whilst the Review did not provide for document disclosure to customers, the Independent Reviewer (and his advisors) were given access to all relevant documents relied upon by the Review."

10.34. The Bank's decision not to provide disclosure was one of the most common complaints that customers voiced to me during my review. The concerns fell generally into three categories:

(i) The Customer Review process should have allowed for full disclosure, akin to legal proceedings. The failure to do so, whilst at the same time requiring the customer to disclose all evidence upon which the customer wished to rely, created an unfair imbalance between the parties.

(ii) The Bank refused to provide disclosure of specific documents (even company documents that were not internal to the Bank) requested by the customer to assist the customer with his or her submissions.

(iii) In those cases where the Bank had provided the customer with a measure of explanation for its conclusions, and the customer considered that the Bank had reached an incorrect factual conclusion, the Bank refused to disclose the specific pieces of evidence that it had relied upon in reaching that conclusion.

10.35. As to the first category, I understand the Bank's view that the fact that the Customer Review was not designed to replicate a legal process is important. Litigation is a combative process, and the disclosure rules are designed specifically for that process, to ensure equality of arms, and to ensure that the court has before it the best evidence available (oral as well as documentary). Disclosure within the legal process is often lengthy, gives rise to significant disputes, and is extremely costly. For a process such as the Customer Review, which was designed to be non-combative, speedier, less risky and at lower cost to the customer, I consider that the Bank adopted a reasonable approach in not providing the same levels of disclosure found in legal proceedings.

10.36. That said, and as the Bank recognised, departing from the legal standard of full disclosure does mean that it was necessary to ensure that safeguards were put in place to counter the imbalance that inevitably results from a one-sided disclosure process.

10.37. The question of whether, and if so how much, disclosure is reasonably required to deliver fair outcomes will depend upon the particular nature of the non-legal process. The closer the evidential requirements of the decision-maker are to legal standards, the greater the need to be transparent about the evidence available to the decision-maker. It will therefore depend upon what is being expected of the customer to make good a claim, how

full the documentation available to the reviewer and decision-maker is, and what access the customer will have to evidence from other sources.

10.38. I have reached the view that in the context of the Customer Review, the Bank's approach to disclosure did not provide a reasonable basis on which to deliver fair outcomes for customers. As I explore further in Chapter 12, this most significantly impacted the Bank's assessment of D&C loss, where the Bank took the view that it was for the customer to prove its case, to full legal standards, on the documentary evidence. The Bank's approach to D&C loss was not tempered to take into account the disadvantages faced by customers in advancing such a claim, such as obtaining company documentation from a company that the customer was no longer involved with, or speaking to matters that took place over a decade ago. Nor did the Bank's approach take into account that its own evidence gathering process was more limited than it would have been in a litigation process.

10.39. This was compounded by the fact that the principle of non-disclosure was applied inflexibly. Even targeted and well-founded requests for the disclosure of specific, non-confidential items were rejected without proper consideration. This also devalued the opportunity to provide additional information, since it was impossible for the customer to identify the basis for the Bank's conclusion, where any factual error lay, or, consequently, what additional information would assist to correct it. I consider the impact of the Bank's position in relation to the sample cases, and the impact on fair outcomes which resulted, in Chapter 12.

10.40. I also consider that the Bank failed to put in place adequate safeguards to counter this:

(1) The fact that the Bank conversely took an extremely lenient approach to evidence in the course of its D&I assessment did not balance out the unfairness caused in respect of the D&C loss assessment.

(2) In my view, Professor Griggs' role as independent reviewer was not a sufficient safeguard. In the sample cases I saw very few examples of Professor Griggs challenging the Bank's conclusions of fact or raising questions over a lack of underpinning documentary evidence. In the few instances where Professor Griggs did challenge the Bank, he was met with resistance.[39]

10.41. In summary, whilst a non-legal process does not inherently require full disclosure in order to provide a reasonable basis for fair outcomes and swift and generous compensation, the appropriate level of disclosure will in each case depend upon the nature of the process. The Bank's methodology in the Customer Review must be considered in light of its nature and operation. Whilst I make no findings as to what levels of disclosure would have sufficed, I have reached the conclusion that in the specific

[39] In response to this Professor Griggs tells me that he challenged factual conclusions reached by the Bank in a number of ways. First, he requested several additional searches of the Bank's electronic records. Second, he suggested to a number of participants in the Customer Review that they provide additional information about their experience. In some instances, that information led to increases in compensation to that originally offered by the Bank. Finally, Professor Griggs, on multiple occasions, applied an uplift to D&I redress after reviewing the same case file as that reviewed by the Bank.

context of the Customer Review, and in particular where the Bank was imposing stringent requirements on customer claims to D&C loss, the Bank's decision to refuse any disclosure requests resulted in a process that did not provide a reasonable basis for fair outcomes and swift and generous compensation. The result has been that in some cases customer outcomes have not been fair and reasonable, or in line with the stated objects of the Customer Review.

III SUPPORTING CUSTOMERS

10.42. As I explained in Chapter 3, the Bank announced on 7 April 2017 that it would provide additional support for customers in the Customer Review. This took various forms.

Legal fees

10.43. A notable aspect of additional support was for legal fees. The Bank told me that reasonable, pre-approved payments were made to legal advisors where they were requested by customers in order to assist them prepare submissions to the Bank as part of their participation in the Customer Review. The Bank said that customers were invited to select their own legal advisors, or they could be introduced to legal advisors by the Bank.

10.44. During our work on the sample population, we found that legal fees were requested in 11 of the 16 sample cases. Legal fees totalling £1.5 million were paid to various legal advisors across the sample businesses. The lowest legal fee claim paid was £5,000 and the highest, £270,000. The average quantum of legal fees paid for each sample company was £77,000.

10.45. As I have explained, early in my review the APPG arranged two meetings so that I could talk to lawyers who had acted for customers in the Customer Review. I also spoke to a number of the lawyers who accompanied customers seeing me about their experience of the Customer Review.

10.46. The focus of these conversations was on the Bank's handling of cases. That was not unexpected when lawyers were primarily concerned about their clients' cases. In as much as they commented on the Bank's payments to them, there was some criticism of the need for pre-approval and about the cut-off which operated for the work reimbursed after a final outcome letter. Since I did not see all the lawyers who represented customers in the Customer Review, it is not possible to reach definite conclusions about these matters.

10.47. The Bank is to be commended for deciding at the outset to fund legal assistance to customers in the Customer Review. What it paid to lawyers overall was a substantial sum. Nevertheless, in particular cases a customer might have benefited from some additional help. Equally, some payments to lawyers and claims managers were generous. My impression is that there would have been a benefit for both the Bank and customers if its policy for making payments had been clearer from the outset.

Financial advice

10.48. The 7 April 2017 press release had said that the Bank would reimburse customers

reasonable fees for professional advice whilst in the Customer Review "to enable customers to access appropriate legal and financial advice". A number of customers whom I met complained that their requests for help with fees for financial advice were refused by the Bank.

10.49. Accordingly I asked the Bank to provide me with the details of all the cases in which financial advisers' fees were approved. The information provided by the Bank shows that the Bank reimbursed fees for financial advice for 10 individual customers, and that the total amount paid by the Bank was approximately £80,000. The Bank explained that these were "case by case decisions based on the rationale provided by the customer and/or their advisors."

10.50. I then asked the Bank to explain its rationale for agreeing to pay the fees in those ten cases, and for refusing to pay such fees in other cases. In its response, the Bank sought to draw a distinction between fees for financial advisers and fees for forensic accountants.

10.51. As to financial advisers, the Bank noted that "the proposed scope of this type of work (and costs) were generally considered by the [Bank] to be reasonable and aligned to what we expected customers would require to participate in the Customer Review". By contrast, with requests about forensic accountants, the Bank "did not generally consider this to be a reasonable request in circumstances where neither the [Bank] nor the Independent Reviewer had identified the existence of recoverable losses or had not had the customer's input to make that assessment". The Bank told me that requests from customers were not in order to identify and present their recoverable losses but were instead just to quantify losses that had either been determined as not recoverable or where evidence was not yet provided as to their connection (if any) to the IAR fraud.

10.52. As a preliminary point, I find this stance difficult to reconcile with the Bank's statement on 7 April 2017, which seemed to place no restrictions on the types of professional adviser, legal or financial, from whom customers could obtain support paid for by the Bank in preparing their input for the Customer Review. Secondly, Professor Griggs' recollection is that the Bank's position from the outset was that it would not pay for forensic accountant services on behalf of participants, that is whether the Bank funded forensic accountants was not dependent on the Bank's or Professor Griggs' view as to the existence of recoverable losses, nor whether either had received customer input.

10.53. Further, it is clear that the Bank adopted a different approach to assessing requests for fees for legal advisers and financial advisers. With legal fees no regard was had to the merits of customers' claims before their fees were approved, whereas with requests for fees of forensic accountants the Bank says that it imposed a threshold requirement of recoverable losses. The imposition of this threshold requirement was not reasonable: the purpose of obtaining input from a forensic accountant would inevitably be to enable a customer to identify and present their recoverable losses.

10.54. Furthermore, the fact that the Customer Review had not "identified the existence of recoverable losses" put the conclusion before the inquiry. Customers who may have had recoverable losses would have been hampered in providing the evidence of such losses

by their lack of financial advice. In Chapter 12 below, I explain that in some of the sample cases my financial advisers considered that customers had a credible claim for financial loss as a result of the IAR fraud. What I find most notable about the information provided by the Bank is that none of those customers is on the list of those who received assistance with fees for financial advisers or forensic accountants.

10.55. It is particularly concerning that in two of those sample cases, the customers obtained financial advice at their own expense, and at significant cost. In one case, the customer's solicitor requested the Bank's pre-agreement to those fees, and the Bank refused stating that whilst it was willing to meet all reasonable costs for financial and legal advice, "we do not currently believe that the engagement of a forensic accountant is necessary for your client to participate in the review."

10.56. In another sample case, the request was likewise refused, but the customer was unable to afford the financial advice without the Bank's support. They prepared their submissions without the assistance of a forensic accountant.

10.57. To make matters worse, it transpired that, in two of these cases, the Bank obtained external financial assistance from the well-known firm of accountants, EY. I address this in Chapter 11.

10.58. The same issue arose in several other cases: customers submitted requests for fees for financial advisers and forensic accounting and were refused. The Bank simply stated that it did not consider the requests reasonable. I cannot rule out the potential influence of these refusals on the outcomes of these cases and the possibility that some of these customers' claims for financial losses were wrongly rejected by the Bank.

10.59. In conclusion, I consider that the Bank's refusal to fund such fees was not reasonable, particularly in circumstances where, as I have explained earlier, it obtained outside financial advice from EY in respect of a number of these claims. On the one hand the Bank was refusing customers' requests for such advice on the grounds that it was unnecessary, but on the other obtaining that advice for its own purposes. It is moreover unfortunate that, as I explain further in Chapter 12, the Bank subsequently rejected all claims for D&C loss for lack of evidence.

Writing off customers' debts

10.60. The full statement in the press release dated 7 April 2017 was that the Bank would:

> "[w]rite off customers' remaining relevant business and personal debts currently owed to [the Bank], where they were victims of the criminal conduct, and not pursue them for any repayment."

10.61. Earlier I set out the details of what the Bank did in this regard. In total, it wrote off 18 customers' debts amounting to more than £6.3 million.

10.62. The policy does not appear to be reflected in the Bank's methodology. As the press release explained it, the decision to write off such debts appears to have been taken "to provide additional help to those impacted customers" (i.e. the victims of the IAR fraud).

10.63. In my view the Bank's intention was laudable, and it provided significant relief to some customers. The difficulty was that the policy in effect discriminated against customers who had refinanced their debts with other lenders, or who had repaid their debts to the Bank, for example by selling off assets.

10.64. For example, in one sample case a director was forced to draw down on his pension fund in order to pay down his mortgage and reduce his monthly mortgage payments. Another director was forced to sell his home and downsize.

10.65. In another sample case, this issue came to the attention of Professor Griggs. He raised it with the Bank in an email in January 2018:

> "Where the connection has outstanding debt with [the Bank] in many cases you have written that off as well. You have not done the same where [the business] is not a customer of [the Bank] which while I understand the difficulty of doing that could give the perception that [the Bank] customers are getting a better deal than connections who bank and have debt elsewhere …"

10.66. Professor Griggs pointed out that the director in that case was at risk of being evicted because of arrears on a mortgage with another bank, whereas if the mortgage had been with the Bank it would have been written off. Nevertheless, it appears that the Bank did not change its approach and continued to provide this assistance only to customers whose indebtedness remained with the Bank.

10.67. I agree with Professor Griggs: the Bank's approach favoured customers whose indebtedness was with the Bank, but those customers who had refinanced elsewhere or sold off assets were left in a worse position. Customers in the same position with debts to the Bank were treated inconsistently. The Bank has not justified the unequal treatment. In the circumstances, the Bank's approach was not reasonable.

Interim payments

10.68. Another way the Bank sought "to provide additional help" to victims of the fraud, announced on 7 April 2017, was by providing "interim payments on a case-by-case basis to assist victims in financial difficulty with day to day living costs".

10.69. Such payments were made in response to a request from a customer, and each request was assessed on a case-by-case basis. When making a request, customers were required to submit information about their expenses and their financial situation. The Bank explained its approach to me in the following terms:

> "Whilst an explanation was requested in relation to a customer's shortfall in covering their day to day living costs, customers were not expected to prove that their financial hardship had been caused by their involvement with HBOS IAR. Other than seeking to confirm any income of which the customer was in receipt (where not provided) the Group did not seek to challenge the amounts claimed, but rather accepted the customer's account of the expenditure they were facing. Occasionally, further explanation was sought where, for example, amounts claimed had extraordinarily increased from a previous claim made."

10.70. Interim payments, to be offset against future redress payments, were also made in respect of expenses which were not "within the usual categories of day to day living costs".

10.71. A few customers complained about the Bank's approach to interim payments. Some believed strongly that it was mean spirited and too demanding of justification.

10.72. In my view, it was reasonable of the Bank to require some evidence that a customer was in need of assistance with day-to-day living expenses. The Bank did not require extensive information: it told me that all it required was confirmation of income.

10.73. There were 28 occasions when customers received interim payments. As I said, I received very few complaints. Overall, the system seemed to work well. The Bank is to be commended for adopting the system of making interim payments.

IV OUTCOME LETTERS AND MEETINGS

10.74. Chapters 12 and 13 are concerned with the substantive outcomes for customers. My concern here is with process.

10.75. Outcome letters were short, and did not contain much explanation. The level of information provided in outcome meetings appears to have been more variable. In both cases the Bank appears to have made efforts to include more information in the later stages of the Customer Review. Professor Griggs encouraged this.

10.76. Let me focus on the transcripts for the outcome meetings in the sample cases and the lack of substantive explanations for rejecting the customer's case for D&C losses. It will be recalled that many customers spoke of their unhappy experience at outcome meetings, where the attitude of the Bank was dismissive or worse, giving the impression that it regarded them as failures, with the IAR fraud being irrelevant and the Bank taking no responsibility.

10.77. First, the scripts contained generic matters such as how the Customer Review came about, Professor Griggs' role as independent reviewer, the tax treatment of D&I redress payments, and that, because the review was a voluntary process designed to facilitate compensation on a no admissions basis, the Bank was: "unable to share the methodology but can confirm that it takes into account interactions with [IAR and QCS] and the impacts of those interactions."

10.78. I asked my financial advisers to assess the discussion in the scripts about the customer's business. Their view was that explanations were at a high level so did not reflect the full complexity of a business' history. On the whole they found that the scripts reflected the business histories which they had found in the files but also reflected the fact that, as I have explained earlier, the Bank's files were not necessarily complete or accurate.

10.79. In one sample case the factual inaccuracies generated a further letter from the customer's solicitor explaining how the Bank had fallen into error. The upshot was that the customer received a short letter stating that the additional information had been considered and the outcome remained unchanged. Unsurprisingly, the impression left with the customer was that the Bank had simply ignored the further submission.

10.80. In another sample case it became clear that the customer's dissatisfaction with the Bank's conclusion in respect of D&C loss was, in part, a result of his inability to access documents on the Bank's file. The Bank had refused his solicitors' earlier request for disclosure of such material under its policy of non-disclosure. The material was neither confidential nor privileged, but would have greatly assisted the customer's understanding of the Bank's conclusion.

10.81. Even after they had received outcome payments, customers still lacked an understanding of what they represented. One non-sample customer commented that the sum that he had been awarded probably just about reflected his specific damages (i.e. specifically identifiable financial loss) but did not address his general damages arising out of D&I. As the only redress he received (in common with other customers) was a payment under the D&I redress scheme, he had no idea what the redress award represented, or that his claim for D&C loss had been rejected.

10.82. Based upon the sample cases that we have reviewed, and my meetings with customers, I am unable to accept the Bank's submission that it provided sufficient details to customers to explain why D&C loss was not recoverable. On the contrary, the lack of transparency in communications around the analysis and methodology appears to have been one of the most significant deficiencies of the Customer Review.

10.83. In view of the general lack of detail surrounding the Bank's decision-making which was communicated to customers, I am also unable to accept the Bank's contention that its explanations allowed customers the opportunity to respond with additional information that might strengthen their D&C claim, including by providing supporting evidence. The lack of transparency as to how the Bank was treating customers' submissions and evidence, and its refusal to disclose the evidence upon which it had reached its conclusions, disabled them from being able to supply effective additional information to strengthen their claim. I have not seen any explanations, whether by way of outcome letters, outcome meetings or otherwise, that would have assisted.

10.84. Further customer submissions following the outcome meeting generally attempted to challenge logical fallacies that the customer perceived in the outcome, and factual inaccuracies stated by the Bank or Professor Griggs at the meeting. Simply contradicting or undermining the Bank's or Professor Grigg's reasoning was not sufficient to change the outcome. That was because the process was not designed to be a negotiation, and only new contemporaneous documentary evidence as to D&C loss could lead to that part of the Customer Review being revisited.

10.85. In my view, outcome meetings did not provide sufficient information to enable customers to understand what additional information might assist to further a D&C loss claim. Accordingly, the process did not provide a real or practical opportunity to change the outcome of the Bank's original D&C loss assessment.

10.86. However, as we see in Chapter 13, customers were frequently able to achieve an increase to the redress offered by expanding on the detail of their suffering since this went to D&I. In a number of cases, customers confirmed that they received specific

guidance from Professor Griggs as to how best to do this. He recognised that this was the only realistic way to improve the Bank's financial offer under its approach. In my view, that leads conveniently to a discussion of his role.

V INDEPENDENT REVIEWER: PROFESSOR GRIGGS

10.87. The Bank took the welcome step of appointing what it described as an independent reviewer to oversee the process of the Customer Review. In this part of the chapter, I offer an assessment of this at a procedural level. The following chapters contain an analysis of what happened with the substantive decision-making on customers' cases and the role in that of Professor Griggs as the independent reviewer.

Role of "independent reviewer"

10.88. In announcing the Customer Review in its first press release of 7 February 2017, the Bank announced that in consultation with the FCA it would appoint "an independent third party as part of the review" and the Bank would agree with them "the scope, methodology and individual case outcomes of the review."

10.89. When Professor Griggs' appointment as the "independent reviewer" was announced on 20 March 2017, those words were repeated but with the addition that his agreeing the scope, methodology and individual case outcomes of the Customer Review was "to ensure fair outcomes and that the review is undertaken effectively." In Chapter 5, I explain how these requirements were spelt out in Professor Griggs' terms of reference, although (mistakenly in my view) these were not made public.

10.90. As I explain there, and despite what had been said, Professor Griggs did not approve the scope of the Customer Review, taking the view that it was the Bank's decision. After meetings and presentations he concluded that the methodology would deliver fair and reasonable outcomes.

10.91. Further detail about Professor Griggs' role in compensation decisions was given to customers. Thus in the Bank's Next Steps letter and Professor Griggs' accompanying letter, which the Bank sent out from 21 April 2017, it was said that customers' outcomes would be "approved or amended" by him, that he was involved in agreeing the scope and methodology of the Customer Review, and that he would be "personally involved in reviewing and approving" outcomes "to ensure that the review is undertaken effectively and that you receive a fair outcome." His outcome letters stated that he had reviewed and approved the Bank's offer. The "review and approve" terminology was repeated in outcome meeting scripts.

Requirements for an "independent reviewer"

10.92. The description "independent" in the notion of an "independent reviewer" gives a strong indication of what is required on the part of anyone performing the role. Independence is an attitude of mind, evidenced by a willingness to challenge and to take difficult decisions. Impartiality, even-handedness, an absence of bias and open-mindedness seem to be essential requirements. Independence of mind may derive from

character, but it might also come from training and experience. It is a prerequisite of some occupations, such as the judiciary.

10.93. The appearance of independence is as important as the substance: an independent reviewer must not only act independently but appear to do so. Confidence in a person appointed as an independent reviewer is undermined if the process for performing their functions gives rise to any suggestion that their independence is compromised. That is the unfortunate reality, however independent they may be in practice.

10.94. Finally, procedures are essential in ensuring independence in practice, as well as the appearance of independence. Checking to ensure that there are no conflicts of interest is the first step. Separateness is crucial. It contributes to the appearance of independence. If a reviewer is closely associated physically with those being reviewed, the public are more likely to regard their interests as aligned. That is likely to be the case whatever the reality. Moreover, separateness can also assist the practice of independence in reinforcing impartiality and even-handedness.

Professor Griggs as independent reviewer

10.95. As I have indicated, my concern here is the procedural side of Professor Griggs acting as the independent reviewer. In Chapters 12 and 13 I explain that Professor Griggs did act independently, and, as a result of the steps he took, some customers received increases, sometimes substantial increases, over what the Bank offered. In a number of cases he overruled the Bank.

10.96. Procedurally, however, he was placed in an impossible position and it is not surprising that customers questioned his independence. His appearance of independence was undermined by the way the process was structured: for example, he began with a Bank email address, albeit later his direct contact details were made available; his letters to customers accompanied the Bank's letters in the same envelope and did not explain the details of his reasoning; he met customers, in the main, on Bank premises, not on neutral ground; and his power to overrule the Bank was in my judgment never properly spelt out in writing, at least until his June 2018 letter to the Treasury Select Committee.

VI CONCLUSIONS

10.97. The Bank adopted a number of commendable features in the Customer Review. Its early communications to customers were sympathetic and clear. It also appointed a relationship manager for each customer. Overall it was generous in its funding of legal assistance and with its system of interim relief payments and debt relief. The payment of £35,000 for the unanticipated delay in processing compensation awards was a welcome gesture. The appointment of Professor Griggs as independent reviewer was a valuable innovation.

10.98. However, there are other aspects of the Bank's procedures which fell short in providing a reasonable basis to deliver fair outcomes. Early clarity in its messages was undermined by its failure to explain more fully through the publication of terms of reference or otherwise how it and Professor Griggs were to perform their task of providing fair

compensation to IAR customers. Its general refusal to fund forensic accounting advice was contrary to the message it had given at the outset, as well as unreasonable, not least because in some complex cases it sought outside advice itself. The policy of debt relief was laudable but did not consider customers who had repaid or refinanced their debts. Although it had legitimate reasons for refusing to disclose full details of its methodology and the documents it had in its possession about customers' businesses, the blanket policy was unfair for the reasons I have explained. The Bank's outcome letters and meetings failed to afford a proper explanation to customers as to why D&C losses were not compensated, or that customers were being compensated for D&I and how the case for enhancing this was best presented. Finally, despite his efforts to assist customers, Professor Griggs was placed in a position where his appearance of independence was compromised and confidence in his position as independent reviewer undermined.

CHAPTER 11 BANK'S PROCEDURES: SCOPE OF CUSTOMER REVIEW AND ASSESSMENT OF CASES

11.1. Chapters 12 and 13 consider in detail how the Bank assessed compensation for those in the Customer Review. Before turning to that, I need to address some preliminary points.

11.2. Parts I and II of this chapter concern how the Bank defined the population of those eligible for the Customer Review, and therefore eligible for compensation. That requires a consideration of why the Bank defined the cohorts for the Customer Review in the way that it did and limited individual compensation awards, in the main, to directors of the IAR business customers.

11.3. The chapter turns in part III to the steps which led up to the decision whether to award compensation to those within the Customer Review population and how much that would be. The discussion in this regard goes to the requirement in my Terms of Reference to review the Bank's approach to "building a case file".

11.4. Finally, the chapter discusses some other steps the Bank took in the course of assessing compensation in the Customer Review, including the formal measures taken to ensure consistency in the treatment of customers.

I CUSTOMER REVIEW POPULATION: BUSINESSES

11.5. As we saw in Chapter 3, the Bank's methodology divided the Customer Review population into three cohorts: cohort 1, customers managed by Lynden Scourfield and/or Mark Dobson who were referred to QCS; cohort 2, customer cases involved with or managed by QCS, or which had any other involvement with QCS or convicted QCS individuals, regardless of the proximity of Lynden Scourfield and/or Mark Dobson; and cohort 3, customers who complained about the conduct of Lynden Scourfield, Mark Dobson, or QCS as it related to IAR.

Cohort 1

11.6. The Bank justified limiting the Customer Review to those managed by Lynden Scourfield and/or Mark Dobson at IAR and/or those referred to QCS by pointing, first, to the pattern of criminality established at trial. The allegations at trial were not that these two bankers were corrupt generally or acted fraudulently outside their QCS involvement, but were based on their receiving inducements from individuals at QCS, and then either introducing IAR customers to QCS or requiring that IAR customers employ QCS to advise on turnaround strategies. Cohort 1 was intended to capture customers who were affected by that fact pattern.

11.7. The Bank worked on the basis that individuals in the HBOS management structure, other than Lynden Scourfield and Mark Dobson (including individuals either reporting directly to these two or superior to them), were innocent of criminal behaviour. It told me that it received allegations (as I did) from customers of wider fraud and criminal activity outside IAR or by other employees at IAR. The Bank explained that it engaged outside law firms

to assess these allegations, but they found no suggestion of wider misconduct. Allegations of wider wrongdoing are outside my Terms of Reference.

Cohort 2

11.8. It will be recalled from Chapter 3 that the rationale of cohort 2 was that any contact with QCS was considered to be a potential indicator of detriment, regardless of the direct involvement of Lynden Scourfield or Mark Dobson. However, I should note that the Bank told me that in cohort 2 cases where Lynden Scourfield and Mark Dobson were not involved it in fact saw no evidence of wrongdoing or detriment caused by the customers' relationship managers.

11.9. Nevertheless, any involvement with QCS was sufficient for a customer to fall within cohort 2. By contrast, customers who were managed by Lynden Scourfield and/or Mark Dobson, but had no involvement with QCS, did not fall within the scope of the Customer Review unless they were within cohort 3, in other words, unless they had complained. The Bank told me that it had conducted a "desktop review" of 30 companies that had been identified as having been managed by Lynden Scourfield and Mark Dobson at IAR but not referred to QCS. None of these companies (or related individuals) had complained. The Bank concluded, from the fact that they had not complained, that there was no criminality or customer detriment in these cases, and therefore that there was no need to widen the Customer Review population.

11.10. I consider that the failure to include customers who were managed by Lynden Scourfield and/or Mark Dobson, but had no involvement with QCS, was an inconsistency in the population methodology that caused customers to be excluded from the Customer Review when: (i) they may have been affected by the fraudsters, and (ii) they could have been compensated under the distress and inconvenience ("D&I") matrix. Let me explain.

11.11. Lynden Scourfield and Mark Dobson were convicted along with the QCS offenders. If the Bank considered that there was potential for customers to have been affected by the QCS offenders acting without Lynden Scourfield and Mark Dobson (cohort 2), there also existed the potential for customers to be affected by Lynden Scourfield and/or Mark Dobson acting without the QCS offenders. The fact that no such customers complained to the Bank does not mean that there was in fact no criminality or customer detriment in their cases.

Complaints and cohort 3

11.12. Cohort 3 is the broadest of the three cohorts. It could include customers who had contact with any of the convicted individuals (i.e. it could bypass the restrictions on cohorts 1 and 2) if the customer complained. Based on our review of a number of sample cases, it seems to my team and me that there was no further vetting of cohort 3 customers to ascertain whether or not they were in fact impacted by the IAR fraud.

11.13. The difficulty is that cohort 3 would appear to favour customers who shouted loudest, regardless of whether they had any connection to the criminal fact pattern established at the trial. Customers entering the Customer Review population in this way received the

ex gratia payment of £35,000, and very likely would have received additional redress under the D&I matrix, even though their cases did not necessarily match the criminal fact pattern.

11.14. Conversely, because entry to cohort 3 turned on a complaint, some customers who may have been entitled to redress under the D&I matrix may have been ignorant of the Customer Review, meaning they did not complain.

11.15. There was one customer in that category who approached me; he only became aware of the Customer Review after my appointment. I referred him to the Bank. It made him an offer on an exceptional basis, not as part of the Customer Review (which had finished) but applying the same principles. That was a welcome step by the Bank.

11.16. There was one limitation on cohort 3; the Bank generally excluded customers whose complaints alleged misconduct occurring after 19 January 2009, once HBOS had been acquired by Lloyds Banking Group, because they came under a separate risk framework. The Bank told me that it received complaints from two businesses with no QCS involvement after that date. The Bank in agreement with Professor Griggs decided that they were outside the Customer Review. The two cases were treated as conduct complaints within the Bank's ordinary complaint handling procedures. That seemed a sensible approach.

II CUSTOMER REVIEW POPULATION: DIRECTORS

11.17. When the Customer Review was established the Bank stated in its early press releases that it was seeking to compensate those "who may have been affected by criminal activities linked to IAR", "victims of the IAR fraud" and those "impacted" by the IAR fraud. As far as those individuals were concerned, however, the methodology confined awards to the directors of IAR business customers.

11.18. In this part of the chapter I consider four categories, de facto directors (and those in a similar position) who were not included in the Customer Review population, shareholders and creditors, directors of companies in IAR who were excluded, and customers who left the Customer Review.

De facto directors

Bank's methodology

11.19. Earlier I explained that, in the Bank's methodology, it considered for entry into the Customer Review a small number of de facto directors where HBOS (through IAR) had treated certain employees of a business as if they were a director, or where the employees had assumed the responsibilities of an appointed director.

11.20. To identify de facto directors, the Bank examined its records for evidence that individuals were consistently treated or referred to as a director, for example in one of its credit reports, or that they were making decisions on behalf of the business. It addressed the issue case by case. When I asked the Bank about this process, it clarified that

contemporaneous evidence provided by customers was also given due weight. This was not explained to customers.

Assessment of Bank's approach

11.21. A feature of the Bank's approach to de facto directors was that it placed significant weight on how HBOS regarded the individual at the time. Although the population methodology referred to both how HBOS regarded the customer and to evidence of the customer's involvement in the running of the business, the methodology for D&I payments appears to have placed greater focus on the first of these factors. Whilst a relevant factor for identifying a de facto director is whether third parties considered the individual to be a director, that question is only part of the overall, objective assessment a court would undertake. The effect was to elevate HBOS' contemporaneous view of the individual's role to a central requirement for inclusion in the Customer Review. A test like this is difficult to apply in practice, and it was further exacerbated by the Bank's focus on the (limited) contemporaneous documentary evidence.

11.22. Absent contemporaneous evidence, the Bank did not give weight to the customer's submissions on their involvement in the running of the business. I consider that the Bank ought to have had a more balanced regard to the totality of the evidence available, including customer submissions.

11.23. I had submissions from five individuals who told me that their claims to be included in the Customer Review as a de facto director or equivalent had been rejected. I asked the Bank about them. The Bank explained that, in respect of four of the five cases, there was no evidence to support a finding that the individual was a de facto director. It explained that in the fifth case, the individual had not in fact made a claim that they should be considered as a de facto director.

11.24. All this I find unsatisfactory. In summary the Bank placed significant weight on HBOS' treatment of the individual at the time in assessing whether an individual qualified as a de facto director, failed to explain the evidential requirements to customers and failed to give weight to customer submissions in the absence of contemporaneous evidence in support of the customer's claim.

Shareholders/creditors

11.25. Shareholders and creditors were excluded from the review population.

11.26. The methodology did consider some issues related to shareholders. For example, the methodology had questions requiring consideration of whether there was any share transfer from a director or injection of funds by a director. However, there was no question which would have identified shareholder losses that would have been avoided but for the fraud.

11.27. As for creditors, by the nature of the fraud the largest (and most secured) creditor by the time of the businesses' collapse would have been the Bank itself. However, there may have been other creditor losses of relevance. The D&C methodology did provide for the possibility of the Bank considering certain claims on a case by case basis, but in practice

it did not do so. As this concerns specifically D&C loss, further discussion of the point is best left to Chapter 12.

Excluded directors

11.28. There were a number of directors who, although their business was in IAR and would otherwise have been within one of the cohorts, were excluded from the Customer Review population.

Directors appointed post-entry into IAR

11.29. I asked the Bank why it considered it reasonable to exclude directors who started in office after their business was transferred into IAR. It gave two reasons: (i) directors in office at the time of entry were most likely to have been at risk of detriment from the introduction of QCS; and (ii) there were many reasons for subsequent changes to directorships, including the frequent appointment as directors of those associated with QCS whose inclusion would not have been appropriate.

11.30. However, the Bank added, it did consider on a case-by-case basis whether to admit directors into the Customer Review who had been appointed after the transfer of a business to IAR. One way it did this was that it asked those in the Customer Review to identify anyone else who may have interacted with Lynden Scourfield or Mark Dobson and to identify any directors appointed during the period in IAR.

Directors associated with QCS

11.31. In two instances a director acting in close proximity to QCS was ineligible for a D&I payment. I asked the Bank to explain the situation. I also had a meeting with one of the individuals concerned, and he provided me with his submissions to the Bank. To my knowledge there have been no adverse findings against the two individuals in any legal proceedings. Neither case emerged as a sample case so I have not been able to undertake a full assessment of the case files. Without that, and indeed further inquiry which, given the nature of my review, I am in no position to undertake, I am not able to reach a conclusion on the matter.

11.32. In my view, the Bank's decision to exclude from the Customer Review those who were closely associated with the fraudsters and who appeared to benefit from their activities seems reasonable. As I have just indicated, I am not in a position to comment on whether the Bank drew the line in the right place in particular cases.

Customers who left the Customer Review

11.33. A small number of customers chose to leave the Customer Review, and to seek to resolve their complaints through other processes (for example, through negotiation with the Bank or mediation). Those alternative dispute resolution processes, and the outcomes achieved by customers through those processes, are not within the scope of my review which, by the Terms of Reference, is limited to the methodology, process and outcomes of the Customer Review. Furthermore, such processes (in particular mediation) usually

proceed on the basis of strict confidentiality. It would be inappropriate for me to comment on such confidential matters.

III GATHERING DOCUMENTATION AND CUSTOMER INPUT

11.34. Once the Bank had defined those who fell within the Customer Review, it had to collect information about and from customers. What follows is an assessment of the formal procedures they designed to obtain documentary information on customers, to find the individual directors within the Customer Review and to obtain customer input.

Sources of information

11.35. As I explained earlier, the Bank drew its information from internal Bank sources, from external sources such as the skilled person's report, the police, Companies House, and the trial and from customer complaints and threatened litigation prior to the Customer Review's establishment.

11.36. I was concerned that the Bank should explain why information about which customers were referred to QCS, or were managed by Lynden Scourfield and Mark Dobson, was not readily ascertainable from its records. It responded that its IT systems contained no data field that either captured customers managed by Lynden Scourfield or Mark Dobson or referred to QCS. HBOS' previous systems had not been designed to record all parties associated with a business customer or to maintain a full history of matters: for example, they could state the current but not any previous relationship manager. Further, records may have been deleted or destroyed under record-retention policies. There had also been changes in the structure of the Bank and certain IT systems could have been decommissioned post-merger.

11.37. With respect to QCS invoices, the Bank told me that although these were frequently paid centrally via HBOS Accounts Payable, they could also be paid directly by IAR or by the company with no involvement of HBOS. Thus, there was no evidence for one company in the Customer Review suggesting that the initial involvement of QCS was a result of a referral by HBOS, and there were examples in the Customer Review population of companies which were not managed in IAR but still had QCS involvement.

11.38. My financial advisers have advised me that these explanations are reasonable.

Bank's contemporaneous records

11.39. The first point under the phase 1 heading of my Terms of Reference requires me to assess the Bank's "approach to building a case file". This followed from the criticism of customers that the documents available to the Customer Review, including to Professor Griggs, were inaccurate or incomplete.

11.40. In particular there was a concern that, since some of the Bank's material was produced by individuals involved in or complicit in the IAR fraud, it could not be regarded as reliable. There could be no confidence, the argument ran, that the documents available to the Bank and Professor Griggs were a true record of what occurred.

Extent of Bank's searches

11.41. The Bank has told me that the hard-copy contemporaneous records used to form the basis of the Bank's assessment were selectively augmented by searches of the electronic records, of which there were around 15 million. During my financial advisers' work on the sample cases, it was noted that there was a significant amount of contemporaneous e-mail correspondence included within the hard-copy files, which appears to suggest that there was a limited need for searching the database for additional electronic records. There could be no certainty that further relevant electronic correspondence would not have been located if those searches had been undertaken.

11.42. My financial advisers are of the view (which I accept) that, whilst it was not ideal that there were potentially relevant additional electronic records available, the Bank's stance was understandable in the context of seeking the swift assessment and delivery of outcomes to customers, which was the stated aim of the Bank for the Customer Review.

Alteration/falsification of documents

11.43. As part of their work on the sample cases, my financial advisers found no evidence of the contemporaneous files having been altered or falsified in order to conceal evidence of fraudulent conduct by either of the convicted criminals (or other Bank employees). However, they pointed out to me that the nature of the work which they undertook for the purposes of the Cranston Review was different in nature to an audit or forensic review of the information. As such it may not have identified instances of documents being deliberately altered or falsified.

11.44. A director in one of the sample cases claimed in his submissions to me that he was specifically instructed by the fraudsters to send particular emails in order to create a paper trail to support the perpetuation of the fraud in the contemporaneous documentation, by giving the appearance that he instigated certain actions that one of the fraudsters in fact recommended. A director in one of the non-sample cases gave a similar account: he was instructed to write cheques by the fraudsters, but that was not obvious from the Bank's records. Evidence of such activity, by its very nature, would not be shown in the Bank's files. Consequently, although I am unable to draw definitive conclusions on this point, it may well be that some Bank records did not tell the full story.

Completeness of documents

11.45. My financial advisers reviewed all of the contemporaneous records contained within the Bank's files for the sample cases to find whether (for the Bank's assessment) there had been any apparent gaps in the information contained on the files, and if so, whether the Bank had adequately followed up and investigated them.

11.46. During the review of the 16 sample cases, two cases were identified with apparent gaps in the contemporaneous records. In both of those cases I asked for, and received, an explanation from the Bank. No material information gaps were identified during the detailed review of the other 14 sample cases.

11.47. In the first case, a gap in the records relating to a distinct period of time following the business' referral out of IAR was identified. This issue was also noted by a Bank assessor during the Customer Review. The Bank told me that additional searches had been undertaken on the Recommind database (the Bank's electronic document repository containing in excess of 15 million electronic records). These searches were in respect of individual items of correspondence which had been referenced in customer submissions but had not been located on the hard copy files. The searches undertaken had not addressed the absence of records for the time period identified.

11.48. I therefore requested the Bank to undertake a further search of the electronic database, based on defined search parameters as advised by my financial and legal advisers. The Bank undertook this further search and gave me the results (through uploading the relevant documents on the secure online system used by the Bank to share documents with my team). The search resulted in a further 827 potentially relevant documents being identified. Following a review of all 827 documents by my financial advisers, they considered 65 of the documents to have been relevant to the sample case in the Customer Review. That said, the documents in question would not have, in the opinion of my advisers, materially altered the Bank's assessment of the case or the settlement offer that was made to the customers (based on the application of the Bank's methodology).

11.49. In the second case my financial advisers noted that the contemporaneous files were significantly lacking relevant documentation (when compared to other sample cases), for example there were few internal credit papers/applications, limited facility documentation (and related correspondence), and minimal levels of both internal and external correspondence. Again, this was noted by the Bank assessor in the Customer Review.

11.50. In this case, the Bank advised me that they had undertaken further searches of the Bank's records in the course of the Customer Review, including:

(1) A search of the Bank's hard-copy archive indices, utilising both company names and the names of the individual directors. This search identified no additional relevant hard-copy information; and

(2) A search of the electronic database, using both relevant company names and individual directors' names, for the period that the business was managed within IAR.

11.51. The Bank told me that the electronic search identified 102 relevant documents (after removing duplicates), which were included in the Bank's assessment of the case (and were included in the files that were provided to my review).

11.52. Given the length of time that has passed since the criminal activity occurred (which in this particular case was between 11 and 14 years), it is unsurprising that not all relevant records from the time could be readily identified (or even known to still exist) for each of the customers. However, in this second case my financial advisers and I consider that the Bank took all reasonable steps to seek to identify Bank records that were relevant to the Customer Review.

Finding and tracing customers

11.53. Earlier I described what the Bank told me about its efforts to contact customers and what it did when there was no response. If a customer ceased to reply to communications during the Customer Review, the Bank told me that they would have made reasonable efforts in order to re-establish contact with the respective customer.

11.54. The Bank engaged the services of two external "trace providers", who, my financial experts advised me, are known as reputable firms and experienced at providing tracing services.

11.55. There were genuine non-responders. In respect of one of our sample cases where contact was made with some of the directors, there were two directors who did not respond to correspondence, although they had been successfully located and indeed had signed for the final recorded-delivery letter. We identified another case where the Bank was unable to locate an address for a director through tracing, but asked for and obtained contact details from another director. It then contacted the first director.

11.56. I asked the Bank for details of the two cases where the Bank, having exhausted all tracing attempts, regarded the customer as not found. Regarding one of these, all attempts failed. With the other, there was no record of the business being a former customer. However, individuals associated with the business were mentioned along with others in correspondence from a law firm in 2011. Further inquiries were made, including at Companies House and the law firm, but to no avail.

11.57. There has been a significant passing of time since the end of the relevant period considered by the Customer Review, which inevitably resulted in a lack of readily available and accurate contact information in relation to a number of customers who were identified as being eligible for inclusion in the Customer Review. Notwithstanding this, I consider the steps taken by the Bank to be reasonable insofar as ensuring that the contact details of those affected customers who did not respond (or ceased to respond) were proactively sought in order to include the customer in the Customer Review.

IV BANK'S ASSESSMENT METHODOLOGY: FURTHER ASPECTS

11.58. This part of the chapter covers some miscellaneous issues not dealt with elsewhere relating to the Bank's assessment of customers' cases.

Internal bank machinery

11.59. In Chapter 4, I described the formal procedures the Bank put in place to carry out the Customer Review. This included the establishment of case-review teams, comprised of case assessors, and of various layers above that, including the QC Panel.

11.60. My financial advisers are of the opinion (which I accept) that the assessment process established by the Bank provided the necessary framework and suitable checks and balances which would ensure that customers' outcomes would be determined by suitably experienced and qualified personnel. In their view the procedures were such that decisions could be appropriately challenged by senior and experienced Bank personnel

prior to being considered by Professor Griggs. In the sample cases that my team reviewed, it was noted that the Bank's processes had been followed as intended. However, it is clear that they nonetheless failed to address any of the issues that I identify in Chapters 12 and 13.

Referrals of customers to IAR

HBOS policy on moving customers to Impaired Assets ("IA")

11.61. The relevant policies regarding transferring customers out of the "good book" bank into IA was explained in a Bank employee's witness statement provided in September 2010 as part of Thames Valley Police's then ongoing investigation.

11.62. In summary, there were two operating models in use at the relevant time; a "high value" model (used by the Corporate Banking division), and a "mid value" model (used by the Business Banking division). The distinction between the two was based primarily on the nature and size of the customer and the level of exposure held by the Bank.

11.63. In the "high value" model, the day-to-day banking relationship remained with the existing relationship manager (i.e. within the "good book" bank) but credit decisions were dealt with by the high-risk credit sanctioning hierarchy. In practice, and this is confirmed in a number of the sample cases which fell into this category, this meant that, following classification as high risk, IA staff had ongoing monitoring roles in relation to these businesses, but not necessarily day-to-day (or even frequent) interactions with customers.

11.64. In the "mid value" model, the relationship with the customer was handled exclusively by the IA team, including all day-to-day banking activities. Again, a number of the cases within my sample fell into this category.

11.65. In practice, a customer should have been moved to IA if there were concerns as to its financial viability (through, for example, continuing to incur losses, or experiencing cash-flow pressures, significant delays in paying creditors, or other creditor pressure), or because existing banking arrangements were being breached, for example, requiring additional lending to meet forecast liabilities, exceeding agreed overdraft limits (without prior Bank approval) or breaching covenants contained within facility agreements.

Referrals to IAR

11.66. IAR covered the broadly defined London and South Region. Customers who met the criteria for referral to IA (as described above), and whose banking relationship was managed out of the London and South Region, would have been referred to IAR (as opposed to one of the Bank's other regional IA teams).

11.67. The Bank advised me that during the Customer Review, the individual case assessors evaluated the appropriateness of the transfer into IAR by giving particular consideration to the financial status of the company at the time of its entry to IAR (along with other relevant circumstances). The assessment made by the Bank was not specifically considered against any formal policy that may have been in place at the time, although

the considerations applied by the case assessors were in line with the factors set out above.

11.68. In relation to the 16 sample cases, in each case my financial advisers concluded that it had been appropriate to transfer the customer to IAR, based on these criteria. Although they draw no specific conclusion from it, in a number of cases it was not clear exactly when the transfer to IAR occurred, since it was not clear from the Bank's documentation. Further, in a number of cases, the transfer of the customer to IAR had not been clearly communicated and so the customer, at least initially, would have been unaware that the relationship had transferred to IAR.

External advice: referral to EY

11.69. As I mentioned in Chapter 4, the Bank obtained expert input from EY LLP (formerly Ernst & Young) in relation to eight Customer Review files (the "EY reports"). Five of these concerned sample cases that formed part of my review. These reports had not originally been provided to me by the Bank as part of its disclosure of sample case files. Upon my request, however, the Bank readily provided copies of the five EY reports for the five sample cases.

11.70. When I pressed for an explanation of this, the Bank said that the EY reports were obtained to provide assurance over the decisions being reached through the Bank's assessment work, but that the work which resulted in them was undertaken independently from the Customer Review, did not form part of the Customer Review methodology, and did not form part of the information that case assessors relied upon in assessing the cases in the Customer Review. The Bank further explained to me that, for the same reasons, Professor Griggs was not provided with copies of the EY reports.

11.71. Having reviewed the EY reports, I am surprised by the Bank's contentions. In particular, EY make clear in them that their work was undertaken for the specific purpose of assisting the Bank in assessing whether the customers concerned had potentially suffered losses. Moreover, it is said in the EY reports that EY would meet with the Bank's assessors to discuss their findings and compare and debate any differences (although several of the final reports record that they did not in fact do so). It appears that in some cases EY was provided with at least parts of the customers' submissions to the Customer Review. In others, EY informs me that they were asked to perform their assessment even before the Bank had received some or all of the customer's submissions. I also note that although the provision of the final versions of the EY reports was delayed until after the conclusion of the Customer Review, in respect of the five EY reports which covered sample cases, EY's draft report followed receipt of the initial customer submissions and preceded the Bank's initial outcome letter. EY have also clarified to me that whilst they were asked to provide final versions of their reports in April 2019 for archiving purposes, no further assessment work was in fact conducted after April 2018, making clear that the substantive work took place during the Bank's review of the customers concerned.

11.72. In the circumstances, it appears to me that the EY reports were material to the Bank's review of each case. In those circumstances, the Bank's explanation for not disclosing

them to Professor Griggs (and to me) is not convincing. The EY reports ought to have been disclosed to him, because they were plainly pertinent to his work as the independent reviewer.

11.73. As to the EY reports themselves, my financial advisers comment that: (i) no firm conclusions are drawn and analysis is limited and largely based on factual information provided by the Bank. Indeed, EY have confirmed to me that in some cases they noted the limited information on the files provided, but were told by the Bank that that was all it had on its files. This necessarily limited EY's analysis; (ii) no counter-factual scenarios (setting out the position which would have existed but for the involvement of the criminals) have been prepared to assess the potential financial loss. In this regard, EY have told me that they were not asked to consider any counter-factual scenarios; (iii) the valuation analysis (where applicable) is high level; and (iv) there appears to be no consideration of broader financial losses, such as loss of earnings. On this point, EY have explained to me that the Bank did not ask them to consider or take into account the possibility of any such broader loss.

11.74. I make the following observations:

(1) The Bank's decision to instruct EY to undertake the reports indicates that the Bank perceived those cases might have merit, and recognised its potential exposure.

(2) Whilst EY indicate that they have had access to, and taken into consideration, the Customer Review compensation methodology, in most cases the EY reports reflect what is in my judgment an adversarial stance (which I have identified in Chapter 12 in the Bank's own approach), in particular in relation to the assessment of D&C loss.

(3) In some cases, the Bank's conclusions in its Customer Review closely resemble the findings in the EY reports. This supports the inference that the Bank took the EY reports into account in its Customer Review for these cases.

(4) In some of these cases, the customer had expressly sought funding for expert financial assistance. In each such case, the request was refused, and in one case the Bank specifically stated that it did not consider it necessary for the customer to have such assistance to put forward his claim. In circumstances where the Bank obtained outside assistance in order to assess the case for D&C loss, to refuse the same assistance to these customers seems unfair.

11.75. In summary, I am disappointed by the late disclosure of the EY reports and not convinced by the Bank's contention that they were unrelated to the Customer Review. They seem to me to have been relevant to it. They relate to cases in which it appears that the Bank considered that the customer's claim might have merit. The Bank's approach in relation to these cases reinforces my view (set out in Chapter 12) that the Bank resisted recognising D&C loss. As a result, it took an adversarial approach which was out of keeping with the professed basis and aims of the Customer Review and which resulted in unfairness to customers.

Consistency methodology

11.76. In Chapter 4 I touched on the Bank's formal consistency methodology.

11.77. The Bank told me that the objective of the consistency checking process was to ensure that the Bank's methodology had been consistently and correctly applied, therefore ensuring that all outcomes issued or to be issued (at that point in time) were fair and consistent.

11.78. The Bank has informed me that certain situations gave rise to an increased redress offer being awarded to a customer as a result of the consistency checking process. The Bank provided me with specific examples of these situations:

(1) Provision of new and impacting information from a director in cases where a co-director's claim had been previously assessed and communicated;

(2) The Bank gained greater experience of practically applying its methodology as the Customer Review progressed and this also incorporated feedback received from Professor Griggs;

(3) Where the Bank's assessors needed to exercise a degree of judgement in assessing customer outcomes, the Bank sought to ensure that any subjectivity in these assessments were mitigated across the wider review population.

11.79. The Bank has told me that, where the consistency check suggested the customer's redress award should have been lower, the Bank maintained the original outcome.

11.80. Changes to customer outcomes resulting from the consistency checking process were formally documented in the Customer Review materials prepared by the Bank (and, for the sample cases, shared with my team) and were agreed by Professor Griggs.

11.81. My financial advisers are of the view (which I accept) that the Bank's consistency checking process was a useful and appropriate operational process which helped to ensure consistent outcomes across the Customer Review population. In terms of tangible impacts, I am told that the Bank's consistency checking process resulted in an increase to redress offers in the Customer Review totalling £390k across 11 customers. Despite this, for other reasons the D&I matrix nonetheless had the potential to produce anomalous results. I address this in Chapter 13.

V CONCLUSIONS

11.82. For the purposes of the Customer Review the Bank adopted internal procedures and a structure for carrying out the assessment of individual cases. It was hampered by the length of time which had elapsed since the IAR fraud had occurred and the destruction of records under the type of retention policies typically in operation in any institution. That did not mean that the Bank's procedures were perfect. For example, there were occasional unexpected gaps in its records of the whereabouts of customers.

11.83. However, I consider for the reasons given in this chapter that the Bank took all reasonable steps to seek to identify records relevant to the Customer Review, engaged reputable "trace providers" to find customers when there were difficulties, and took fair

and reasonable steps to ensure that the contact details of those affected customers who did not respond (or ceased to respond) were proactively sought.

11.84. As I have explained, my financial advisers did not find any evidence of the contemporaneous files having been altered or falsified. However, because the nature of the work which they undertook for the purposes of my review was different from an audit or a forensic review of the information, they may not have identified instances of documents being deliberately altered or falsified.

11.85. As regards the Customer Review population, the Bank's methodology defined three cohorts turning on the nature of the contact with the convicted bankers and QCS. It is possible to identify inconsistencies and drawbacks in the boundaries set for the cohorts. Some of these are highlighted above. However, cohort 3 enabled customers to avoid the constraints of cohorts 1 and 2. Although it had the disadvantage of being complaint driven – one needed to know about the Customer Review – it was relatively open ended. Overall, I take the view that the Bank's definitions for the three cohorts were reasonable and fair.

11.86. However, I consider it a deficiency in the definition of the Customer Review population that, with individuals, the focus was on directors. The Bank chose directors since, as it explained to me, they were likely to have had dealings as officer holders with the convicted criminals. That was a sensible starting point, but it should not have been the end of the inquiry. After all, the Bank's stated intention was to compensate those affected by the IAR fraud.

11.87. The Bank extended the Customer Review to de facto directors, but did not extend its attention to others running the business. The approach to identifying de facto directors had the deficiencies which I have already identified. Against the broad reach of the Customer Review as announced – to compensate those impacted by the IAR fraud - the methodology to identify impacted customers involved in running a business did not apply in these respects to produce fair and reasonable results.

CHAPTER 12 ASSESSMENT OF DIRECT AND CONSEQUENTIAL LOSS

12.1. In this chapter I examine direct and consequential loss ("D&C loss"). These are the losses which a court might award, for example, in respect of damage caused to a business and its shareholders through the fraud of a third person, or damage caused to the principal of a business as a result of the fraud, such as loss of income or earning ability through damage to his or her reputation.

12.2. The Bank did not make a single redress payment for D&C loss across the entire Customer Review, whether to a business or an individual.

12.3. However, in a small but significant number of sample cases which my team reviewed, the customers put forward credible claims for D&C loss. I am not in a position to say whether any non-sample cases also had credible claims for D&C loss, but that possibility cannot be ruled out.

12.4. None of this means that if these cases came to court the claim would be successful. There are many factors which bear on the outcome of cases once they reach court. Lawyers speak of litigation risk, the risks that a witness' account is not convincing under cross-examination, the risk that other evidence such as expert evidence is not as strong as was thought, and so on.

12.5. Except in one respect where another view is possible, there was nothing wrong in the Bank's understanding of the law. However, I have reached the conclusion that the Bank's D&C methodology, in both structure and application, was balanced against recognising or awarding such loss. To use the language of my Terms of Reference, it did not provide a reasonable basis on which to deliver fair outcomes and offer swift and reasonable compensation for D&C losses to those in the Customer Review.

12.6. I explain in greater detail below how I have reached that conclusion. In summary, the Bank's approach to the assessment of the sample cases demonstrated in many cases a flawed consideration of the proper counterfactual scenario. The process also employed an overly strict evidential threshold, beyond that which would have applied had these claims been pursued in court proceedings and not appropriate within the context of the Customer Review. Just as significantly, I have not identified any occasion on which the strict evidential requirements that the Bank applied were ever properly or clearly communicated to the customer.

12.7. As a result, there were, in my view, unacceptable barriers to claims for D&C loss. I am not surprised that every such claim was rejected. Using again the language of my Terms of Reference, that meant that the judgements the Bank made on individual customer cases were not fair and reasonable in relation to the assessment of D&C losses. Further, the Bank's approach to the "heads of loss" that it considered, together with its approach to and basis for establishing loss and ensuring consistency in assessments, did not provide a reasonable basis on which to deliver fair outcomes and offer swift and reasonable compensation.

12.8. This chapter proceeds with a brief account of what the law says about D&C loss (Part I). It then examines how the Bank explained the law to its assessors in the methodology. Save in one respect, this was essentially correct (Part II). The bulk of the chapter (Part III) is an assessment of this methodology and its application in the sample cases. Then there are two shorter parts, one where I address the relationship between the Bank and Professor Griggs (Part IV), the other where I recall the bearing some of the analysis in Chapters 10 and 11 has on D&C loss (Part V).

I DIRECT AND CONSEQUENTIAL LOSS: LEGAL PRINCIPLES

12.9. For completeness, this part sets out in summary form the law relating to D&C loss.

12.10. Normal (or direct) loss and consequential loss are distinguished as follows:

> "There is a very important distinction to be drawn between (i) an injury that carries with it a normal or usual loss, and (ii) the later consequential losses that are actually suffered from the injury. These two types of damages are often described as "normal" losses and "consequential" losses. They are, respectively, the usual or generalised consequences of an injury and the actual consequences. The normal loss is that loss which every claimant in a like situation will be expected to suffer; the "particular" or "actual" consequential loss is that loss which is related to the circumstances of the particular claimant." [40]

12.11. Within the category of consequential losses, there is a further distinction to be made between:

> "the negative loss of gains that the claimant would have made had the wrong not been committed and the positive expenses to which he is put by reason of the commission of the wrong".[41]

12.12. From the Bank's methodology, which I summarise below, it is evident that the Bank envisaged that any claims made by customers affected by the IAR fraud would most likely be framed as claims for fraudulent misrepresentation. Therefore, the Bank's methodology for assessing claims for consequential loss was intended to reflect the proper measure of damages for fraud.

12.13. That is important since in non-fraud cases consequential losses are recoverable if they are not too remote. However, in cases of fraud the position is more favourable to the claimant:

> "In fraud, the defendant has been guilty of a deliberate wrong by inducing the plaintiff to act to his detriment. The object of damages is to compensate the plaintiff for all the loss he has suffered, so far, again, as money can do it. In contract, the damages are limited to what may reasonably be supposed to have been in the contemplation of the parties. In fraud, they are not so limited. The defendant is bound to make reparation for all the actual damages directly flowing from the fraudulent inducement. … All such

[40] *McGregor on Damages*, 20th ed (2018), paragraph 3-008.
[41] *McGregor*, paragraph 3-008.

damages can be recovered: and it does not lie in the mouth of the fraudulent person to say that they could not reasonably have been foreseen."[42]

12.14. In analysing the position if there had been no fraud (the non-fraudulent counterfactual), a distinction is also to be drawn between the hypothetical behaviour of the parties (here, the Bank and the customer) and the hypothetical behaviour of third parties (such as, for example, other potential investors or finance providers, landlords, or suppliers and end customers):

> "In contrast with past facts and the hypothetical behaviour of the claimant and defendant, the hypothetical behaviour of third parties is to be determined on a loss of a chance basis (unless the parties concede otherwise). This means that the claimant does not have to show that on the balance of probabilities (i.e. to a more than 50 per cent likelihood) the third party would have behaved so as to confer a benefit or prevent a loss, it is enough if the claimant can prove that there is a 'substantial' chance, which may well be less than 50 per cent, that the third party would have behaved in this way. The claimant can then recover the fraction of the hypothetical loss that corresponds with the chance that the third party would have acted in such a way as to make it come about."[43]

II DIRECT AND CONSEQUENTIAL LOSS IN THE CUSTOMER REVIEW

12.15. The Bank's approach to assessing D&C loss was set out in two governing methodology documents, the Financial/Technical Assessment, and the Consequential Loss Assessment. I refer to these two documents together as the D&C methodology.

12.16. Each of these documents identified Design Principles which underpinned the approach to, respectively, direct financial loss and consequential loss. These are explained further below.

12.17. The Financial/Technical Assessment explained that the assessment of direct financial loss was to take place at each of the individual (i.e. director) level and business/company level, which the D&C methodology referred to as the entity (i.e. business) level. It contained a series of questions for each of the entity-level analysis (which I will call the "business-level" analysis) and the individual-level analysis, the purpose of which was to guide the Bank's assessment of financial losses.

Business-level analysis

12.18. The Financial/Technical Assessment identified as the design principle for the business-level analysis that D&C redress for a business should take into account "red flag" assessment criteria. Red flags were generated when a business had had involvement with the convicted former employees of the Bank and/or either QCS or David Mills.

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[42] *Doyle v Olby* [1969] 2 QB 158, 166-167, Lord Denning MR

[43] *Kramer, The Law of Contract Damages*, 2nd ed (2017),13-79. The principles concerning loss of a chance do not differ as between contract and tort (see *McGregor*, Chapter 10).

12.19. The questions that the Bank considered when assessing D&C loss at business level related to:

(1) The financial status of the business at the time of entry into IAR;

(2) The appropriateness of the business' entry into IAR;

(3) The treatment of the business while in IAR and during turnaround activities involving QCS; and

(4) The identification of any other creditors of the businesses.

12.20. The business assessment was designed to capture statistic and specific information including:

(1) The change of the valuation of the business from entry into IAR to exit;

(2) QCS/RPC invoices;

(3) Directors appointed or removed;

(4) New loans or products purchased;

(5) Transfer of ownership; value of assets transferred; nature of transfer;

(6) Value of funds injected;

(7) IAR fees;

(8) Value of any gifts and entertainment provided; and

(9) Value of other creditors' interests in the business.

12.21. The process for assessing D&C losses at business level involved various stages and different assessors. A factual Assessment Template was to be completed by the Bank's assessor, and a legal assessor would then conduct a financial assessment to assess whether D&C loss had been incurred (based on the information provided). The legal assessor was then able to:

> "advise the [Customer] Review on the Customer's claims. The Legal Assessor's proposed Financial Assessment is considered and challenged by QC Panel in arriving at the final assessment outcome. The Programme Legal Lead advises QC Panel on the soundness of the overall case outcome."

12.22. The Financial/Technical Assessment noted that:

> "Should the [Bank's] Assessors or Legal Assessors feel that they would like to obtain further information before concluding their review, they can make a request to the Case Clinic and, if appropriate, the QC Panel. Requests will be considered on a case by case basis and in line with the Review's principles."

12.23. My understanding is that the Bank's assessors were provided with the Bank's files to undertake their review. The quote at paragraph 12.22 above appears to reflect that those files were compiled using primarily the Bank's hard copy documents, but with the ability

for specific additional searches (electronic or hard copy) to be carried out. The mechanism in paragraph 12.22 would appear to provide for this.

Individual-level analysis

12.24. The individual-level analysis identified the following questions that the Bank considered to be of particular relevance to the financial assessment of individuals:

(1) Whether there was any transfer of shares/ownership of the business during the time that it was managed by IAR, including, specifically, information regarding the individual's shareholding value and dates in the business;

(2) Whether there were any injections of funds by the directors during the business' time in IAR, any personal guarantees that were in place for the relevant individual, in what amount, and whether or not they were called upon.

D&C claims raised in customer's submissions

12.25. The document suggested that where a customer made a specific claim for D&C loss:

"the Legal Assessor should provide a comment for each claim, including whether there is any new or additional information contained within the submission and whether the Legal Assessor agrees with the allegation. The Legal Assessor should also provide document references in support of his/her conclusion."

Consequential loss assessments

12.26. The Design Principles set out in the Consequential Loss Assessments document stated that:

"Claims for Consequential Loss will be assessed by the Legal assessors by reference to established legal principles including in the tort of deceit (fraudulent misrepresentation)", and that the assessment will "take account of the BSU Assessor's finding and any Customer input."

12.27. The introduction to the body of the document further elucidated that:

"In most instances it is expected that the proactive and voluntary assessment of Direct Loss with the addition of 8% Compensatory Interest and the write-off of any relevant business and/or personal indebtedness to LBG will avoid the need for a Customer to advance a Consequential Loss claim."

12.28. However, the Bank recognised that:

"a court would usually have the benefit of each party providing disclosure of relevant documents, the exchange of statements dealing with factual and expert witness evidence, and an ability to test that evidence through cross-examination. The same is not available in the Review."

12.29. I consider this to be a key point, which I return to in the analysis below. These matters underpin the overarching description of the Customer Review in the methodology document as being:

"a voluntary process and has been designed to be as simple as possible to provide fair, swift and appropriate redress to Customers. It is not designed or intended to replicate a legal process. Decisions on Consequential Loss will be made on the evidence available, applying the relevant legal principles and within the overall framework of the Review."

12.30. The document proceeded to summarise the principles applicable to assessing loss in cases of deceit. The key points noted are that:

(1) The aim of damages is to put the injured party into the position they would have been in but for the improper conduct or tortious act.

(2) In fraud cases the measure is more generous, and reasonable foreseeability is not required (only a sufficient causal connection).

(3) The requirements of deceit are summarised, including the requirement to identify a fraudulent representation, knowledge and/or intention, reliance and detriment.

(4) The burden of proof concerning these elements is on the claimant (i.e. the customer).

12.31. The document further noted that where a claim is not advanced in the tort of deceit, "it must still satisfy, to [the Bank] and Independent Reviewer's satisfaction, the legal tests to the claim being advanced."

12.32. The document also implicitly acknowledged the need to evaluate a potential counterfactual (i.e. the scenario of what would have happened but for the fraud):

"It is likely that those Customers in the Review that are now insolvent or dissolved will assert that their businesses would have turned around and been profitable but for the alleged improper actions of those convicted in the criminal trial. In the light of this, the assessment will include in its considerations:

- The Customer's financial position prior to the alleged improper conduct;
- The specific factors that led to the Customer being in a distressed financial position; and
- The probability of the Customer being able to trade profitably but for the alleged improper conduct."

12.33. The document noted that claims for out of pocket expenses would be easier to establish than, for example, loss of profits claims, which are inherently more speculative, and set out that:

"Where appropriate, a probabilistic approach (applying a percentage discount to allow for the fact that the transaction may have been less profitable than anticipated or to reflect the uncertainty of the outcome more generally) may be considered."

12.34. This approach was appropriate. Loss of a chance is the correct legal analysis to apply where the outcome in question involves the actions of third parties.

12.35. The methodology also addressed mitigation of loss, noting that:

"While it may be possible to identify cases where Customers appear to have failed to discharge their duty to mitigate, we would only expect this line of argument to be adopted on an exceptional basis dependent upon the detailed facts of the case."

12.36. This also seems appropriate and sensible. I would add that we did not come across any files in the sample cases in which the Bank asserted a failure to mitigate.

12.37. The Bank also identified an (apparently non-exhaustive) list of "Broad categories of consequential loss" that it was anticipated might be claimed. These were as follows:

(1) Bank fees, default interest and charges;

(2) Interest charges on alternative borrowings;

(3) Forced sale of assets/machinery/property;

(4) Loss of opportunity;

(5) Loss of profits;

(6) Loss of business value;

(7) Claims arising out of business failure/insolvency;

(8) Claims for losses incurred by shareholders, directors and third parties;

(9) Loss of management time;

(10) Claims for distress, inconvenience, hardship, pressure and impact on personal life;

(11) Damage to reputation;

(12) Professional fees and costs in dealing with the consequences of the IAR fraud;

(13) Costs incurred in seeking compensation. Distress, inconvenience etc. are included in this list, although these are separately dealt with under the Bank's D&I methodology: see Chapter 13.

12.38. The D&C methodology required claims for consequential loss to be "sufficiently evidenced" and provided the reviewer with further guidance in respect of the categories, including the following:

(1) In respect of forced asset sales:

"it will need to be determined whether the enforcement of security and/or the deterioration of the business was caused by the fraudulent actions of those convicted."

(2) For loss of opportunity, the D&C methodology recognised that:

"This type of claim is often difficult to evidence as it requires detail of the opportunities that the Customer would likely have pursued but for the wrongful conduct which makes them speculative in nature. Where claims are not supported by satisfactory evidence they will not succeed."

(3) In respect of loss of profits, the D&C methodology noted that this was highly fact-dependent, such that little guidance could be given.

(4) In respect of loss of business value:

"the Customer will have to show that the fraudulent actions of those convicted had a direct effect on its performance. As regards to supporting documentation, the Customer should provide [the Bank] with information to demonstrate the overall financial health of the business during the relevant period, for example annual accounts or valuation reports. If there was already a general downward trend LBG would need to be provided with cogent evidence that the business would have been turned around or value retained but for the fraudulent activity."

(5) Claims for losses incurred by shareholders, directors and third parties were generally excluded on the basis that:

"Individuals will only have standing to bring claims on their own behalf. A claim by an individual for diminution in the market value of shares held by the Individual will not be recoverable as such losses would merely be reflecting of the company's losses."

Importantly, the methodology went on to recognise that:

"However, depending upon the nature of the relationship between the Individual and the Group there may be cases where the Individual has standing to bring claims for personal loss against the Group (e.g. in their capacity as guarantor).

Where the relevant Entity is dissolved and cannot be restored consideration will be given to such matters on a case by case basis."

(6) Loss of management time would face a "high threshold":

"the successful recovery of damages for wasted management time through the courts is rare. In particular the impacted party would need to be able to provide clear evidence of the time spent dealing with the alleged fraud (e.g. time sheets or similar), together with cogent evidence that such divergence of time caused a significant disruption to the business."

(7) Claims for damage to reputation were essentially dismissed as being "only recoverable in tort in the context of defamation", which would require "cogent evidence" and be restricted to "comments […] made publicly by the former HBoS employees convicted at trial".

12.39. As I have already said, in my view the Bank's summary of the applicable legal principles in its D&C methodology documentation was an accurate description of the losses recoverable in cases of fraud and reflects the legal principles propounded in case-law. The one exception to this was the Bank's treatment of claims for loss of income or earning ability through damage to reputation, which was narrow in approach.

12.40. Whilst damages for loss of reputation per se may be the domain of defamation, damages for financial loss flowing from loss of reputation are not necessarily so restricted.

Pecuniary loss is recoverable, subject to a causal link being established.[44] There is no requirement that the representation is the immediate cause of the loss claim, so long as there is an unbroken chain of causation. There is therefore no reason in principle why a claimant cannot claim for loss of earnings resulting from damage to reputation provided the damage to reputation was caused by the fraudulent representation. As explained by Lord Nicholls in *Malik v BCCI SA (in liquidation)*[45]:

> "I agree that the cause of action known to the law in respect of injury to reputation is the tort of defamation. With certain exceptions this tort provides a remedy, where the necessary ingredients are present, whether or not the injury to a person's reputation causes financial loss. No proof of actual damage is necessary, and damages are at large. If, as a result of the injury to his reputation the plaintiff does in fact suffer financial loss, this may be recoverable in a defamation action as 'special damage'.
>
> All this is commonplace. It by no means follows, however, that financial loss which may be recoverable as special damage in a defamation action is irrecoverable as damages for breach of contract. If a breach of contract gives rise to financial loss which on ordinary principles would be recoverable as damages for breach of contract, those damages do not cease to be recoverable because they might also be recoverable in a defamation action. There can be no justification for artificially excising from the damages recoverable for breach of contract that part of the financial loss which might or might not be the subject of a successful claim in defamation. Hallett J. summarised the position in *Foaminol Laboratories Ltd. v. British Artid Plastics Ltd*. [1941] 2 All E.R. 393, 399-400:
>
> '… a claim for mere loss of reputation is the proper subject of an action for defamation, and cannot ordinarily be sustained by means of any other form of action... However ... if pecuniary loss can be established, the mere fact that the pecuniary loss is brought about by the loss of reputation caused by a breach of contract is not sufficient to preclude the plaintiffs from recovering in respect of that pecuniary loss.'"[46]

12.41. There is no reason why the same would not apply to a tortious claim in deceit. Ultimately, the claim is for pecuniary loss (and not for the damage to reputation per se). The question is simply one of causation, although I accept there is no authority directly on the point.

12.42. Finally, the D&C methodology provided that if the loss had already been accounted for as direct loss it would be excluded, and that any consequential loss should be off-set against any compensatory interest award that had already been made in respect of direct loss. Both of these matters are concerned with preventing double recovery and seem sensible.

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[44] *Halsburys Laws* Vol 76, para 790; See also *McGregor*, paragraph 49-007. See also *McGregor*, paragraph 49-041, addressing damages recoverable, including for loss of earnings, in a case where physical injury resulted from deceit.

[45] [1998] AC 20.

[46] [1998] AC 20 at page 40.

III BANK'S APPLICATION OF THE D&C METHODOLOGY

12.43. In Chapter 9 I set out how my team and I examined the sample cases. Perhaps a brief reminder will assist. First, my financial advisers looked at the Bank's assessment of any claims for D&C loss in the sample cases, including the Bank's analysis and conclusions as to likely counterfactuals, and its consideration of any counterfactuals put forward by the customer. They also undertook their own analysis as to what they considered to be the most reasonable counterfactual. Their conclusions in relation to these financial and factual analyses were then passed to me and my legal team, together with the customer file. The file was then assessed according to legal principles, based upon the financial analysis received from the financial team, and bearing in mind the Bank's stated D&C methodology. The analysis which follows is the product of our examination of the Bank's approach to D&C loss in the sample cases.

12.44. In this section I have structured my commentary on the Bank's approach as follows:

a) The Bank's emphasis on the voluntary, non-legal nature of the process;

b) Burden of proof;

c) The D&C evidential threshold;

d) Causation and counterfactual: valuation of the business;

e) Other consequences of the IAR fraud;

f) Writing off customer debts with the Bank; and

g) Outcome meetings, and the role of additional information in the assessment of D&C loss.

(a) The Bank's emphasis on the voluntary, non-legal nature of the process

12.45. It was a key tenet of the Customer Review that the process was not set up to replicate a litigation process or a statutory decision-making process. I have already set out above how this was expressly stated in the D&C methodology documents themselves. The point was also emphasised in the Bank's submissions to me, as it was to customers at the time.

12.46. Customers who participated in the Customer Review were sent a letter which explained that the Bank wanted to understand the customer's point of view and experience in relation to their interaction with IAR, and the impact of the criminal activities on the customer and their business. To this end, the letter invited the customer to complete a questionnaire, or attend a meeting, or both, and provide any of the customer's own records and information that the customer wanted the Customer Review to take into account.

12.47. However, the Bank's methodology reveals that it had a different approach to assessment of D&C loss, which was to be assessed by "established legal tests and principles", compared to its approach to D&I loss, which was "a bespoke approach" to be applied in "considering personal impacts in the form of distress and inconvenience."

12.48. It seems to me that this approach to the assessment of D&C loss introduced a "legal" element to the Customer Review process which was at odds with the Bank's position on its other aspects.

Disclosure

12.49. The voluntary and non-legal nature of the Customer Review also featured in the Bank's approach to disclosure. As the Bank explained in its submission to me (and referred to in Chapter 10): "Whilst disclosure of documents is a feature of a litigation process, it is not required in a voluntary compensation scheme such as the Review." The Bank considered that the provision of all information to Professor Griggs provided adequate safeguards to the customer, because Professor Griggs, as the independent reviewer, was able to challenge the Bank's interpretation of the evidence and its conclusions. However, Professor Griggs himself disagreed with this.

12.50. This was also the justification given by the Bank in declining customer requests for disclosure (whether general, or of specific documents), as discussed in Chapter 10. Thus in one of the sample cases, the customer's solicitors sought disclosure of company documentation that the customer himself had provided to HBOS during earlier proceedings, and/or which would have been available to the customer at the time of the relevant events in question, and much of which would have been the customer's own work product and documentation. The customer's solicitors clarified that the request excluded the Bank's internal documentation, and was to enable the customer to provide a more helpful and accurate narrative of events for the Customer Review process.

12.51. The Bank declined the request, emphasising that the Bank was simply "seeking input [from the customers] to the review process to ensure we have all the information available in making our assessment…"

12.52. In another sample case, the customer's solicitors sought disclosure of a specific document which: (a) had been sent by the Bank to the customer's former co-director while the business was in IAR, and (b) had been referred to by the Bank in the customer's outcome letter and in the outcome meeting as a reason for the Bank rejecting his claim for D&C loss. Again, the Bank declined the request**,** and refused to permit the two former co-directors to discuss the matter:

> "As you are aware, [former co-director] has now entered into a settlement agreement with the Group regarding the events at the HBOS Impaired Assets Office Reading … We would draw your attention to clauses 2.2 and 2.3 of this settlement agreement, which would preclude [former co-director] from entering into the discussions you appear to be proposing.
>
> … the disclosure of documents by the Group is not something that is being offered by the Review. We reiterate that Professor Griggs has been provided with all relevant documents in support of his role as Independent Reviewer and will have taken these into account in his decision to confirm and approve the outcomes for your clients … as being fair and reasonable."

Perceived discouragement of legal submissions from customers

12.53. The Bank also emphasised the non-legal nature of the Customer Review in terms of the nature and content of customer input. That was also the case where a customer was legally represented. In one sample case, the customer submissions specifically stated that:

> "At the request of the Bank no legal argument has been raised in this Written Submission, as the Bank has made clear that is not what the Review Scheme is about."

12.54. In another sample case, the solicitors' covering email to the customer submissions explained that:

> "As you know, we have not treated the process as being litigious; indeed in many respects quite the contrary, it has been more investigative. There are no pleadings to work out from; no discovery and no disclosure – indeed the Bank has declined to make disclosure – all of which in a litigation process would precede the production of Witness statements. […] Accordingly with regard to all of the above, what our client and ourselves have been able to produce has been necessarily hampered compared to what would be expected in traditional litigation or mediation processes. For this reason we are describing our clients' central submission as a Narrative. However, this is the process which at this point both the Bank and our clients have willingly entered into. The Bank made clear at the outset that [...] our clients are being viewed as Victims by the Bank for the purposes of this process (e.g. as opposed to as Claimants). […T]he purpose of this process is to endeavour to seek an amicable and agreed solution and settlement if at all possible; and we and our clients have engaged in the process most seriously and accordingly. We of course believe the Bank likewise. And that courtesy is appreciated."

(b) Burden of proof

12.55. Despite the non-legal nature of the Customer Review, the D&C methodology made clear that the burden of proof in respect of any claim to D&C loss was on the customer. The reference in the D&C methodology to the requirements of a claim in deceit (see paragraphs 12.26 and 12.30 above) also stated that the Bank expected the customer to prove not only the fact and causation of the loss, but also the legal elements needed to advance the preceding claim of wrongdoing.

12.56. I find this difficult to understand in circumstances where customers were being discouraged from submitting legal submissions, and where the general fact of the fraud was acknowledged. I can understand requiring the customer to establish, to a sufficient degree, that the customer has in fact suffered loss, and that that loss was caused by the fraud. However, it seems inconsistent with the acknowledgment of the IAR fraud, and the non-legal nature of the Customer Review, to require customers to formulate and prove their case as if in legal proceedings.

(c) D&C evidential threshold

High evidential standard, and failure to communicate expectations to customers

12.57. As I have noted above, the Bank's methodology documents emphasised that the Customer Review would not consider the same material that a court would consider, given that the review was not designed to replicate a legal process. Thus:

> "Decisions on Consequential Loss will be made on the evidence available, applying the relevant legal principles and within the overall framework of the Review."

12.58. As I have also identified above, the D&C methodology documents provided the assessor with guidance as to the level of evidential proof which would be required for certain types of claim to be successful (the "D&C evidential threshold").

12.59. However, there was a notable difference between the approach adopted by the Bank in respect of D&C loss, and its approach in respect of D&I loss. This has been explained in the Bank's statement to me in the following terms:

> "While the Review applies established legal principles to the assessment of direct and consequential losses, it takes customer evidence at face value when assessing redress for distress and inconvenience, absent evidence to the contrary. This assessment was designed to provide an understanding of the engagement and interaction the individual had with convicted former HBOS employees within IAR and/or QCS."

12.60. In his submission to me, Professor Griggs set out this reflection:

> "One issue that arose often in outcome meetings was the concept that the word of participants would be accepted where there was no evidence to the contrary. In relation to compensation for distress and inconvenience, the Scheme required that these payments should be heavily based on the customer's own account of their experiences. In determining that distress and inconvenience compensation, inter alia, the default position was that the participant's account of events should be believed unless there was express evidence to the contrary and impacted participants should not need to prove causation, as a court would require. The position in relation to allegations of direct or consequential loss was different, in that the Scheme required clear evidence of that. Occasionally in outcome meetings, this led to confusion by participants. This was an issue which could have been explained on an 'information page' on LBG's website."

12.61. This approach that the Bank adopted to the assessment of evidence in relation to claims for D&C loss gives me cause for concern.

12.62. First, none of this was communicated to customers. Vague references to "legal principles" being applied, whilst emphasising repeatedly the non-legal nature of the Customer Review, were insufficient to explain the test that the Bank in fact applied, or what the Bank in fact expected to see from the customer in support of a claim for D&C loss. This is all the more important because customers perceived that they were being dissuaded from framing their submissions as anything more than information that they considered the Bank

should take into account when reviewing the customer's file. The unsurprising result was, precisely as Professor Griggs identified, confusion on the part of customers.

12.63. Second, the application of legal principle is in any event a different matter from the evidential standard and requirements being applied. If legal principles are to be applied by way of a non-legal process, it is imperative that the manner in which the non-legal process differs from a legal process will not operate to the detriment of the customer. This was particularly important because the Customer Review was presented as a customer-focused process designed to compensate victims of an acknowledged large-scale fraud, and the Bank was taking on the role of judge.

12.64. Third, given the stance taken by the Bank on disclosure, it seems to me that it would have been near impossible for the customers to meet many of the evidential requirements even had they been properly communicated to them. For example, to prove business loss, the D&C methodology indicated that the customer would need to provide contemporaneous documentary evidence of the business' financial records, prove that the specific fraudulent conduct of the convicted individuals in relation to the file negatively impacted the business, and to what extent. Customers generally had no access to that documentation (for example, because the relevant company had been dissolved, or the individual was removed as a director), no access to the Bank's documentation showing what the fraudulent individuals had done behind the scenes, and no access to financial expertise (because in almost all cases the Bank refused to fund such advice, as explained in Chapter 10). The matters in question had occurred over a decade previously. In those circumstances, it would have been nigh on impossible for customers to satisfy the standard set by the Bank. Similar observations may be made about the references in the D&C methodology to time-sheets (for loss of management time), proof of missed opportunities, and proof of specific causality regarding forced asset sales.

12.65. Fourth, customers were not shown the evidence upon which the Bank was rejecting their contentions, so remained unable to challenge it properly. Where requests for this material were made, they were refused. Not only was the Bank setting a higher evidential bar than with court proceedings, but it did so in a way that the responsive party had no idea of the case it had to meet. This seems inimical to a fair and reasonable approach.

12.66. In short, the evidential standard applied by the Bank in respect of claims for D&C loss was, in the circumstances of the Customer Review, a high one – and, indeed, a higher one than would have applied in court proceedings. The unfairness of that high threshold was exacerbated by the Bank's general approach to the evidence, as explained below.

Over-reliance upon the documentary record

12.67. In litigation, witness evidence forms an important part of the totality of the evidence considered by the court or tribunal. For reasons I explain further below, in fraud cases in particular, it will likely perform a central role. In the courtroom, witness evidence will be tested through cross-examination against: (a) documentary evidence; (b) circumstantial evidence; (c) what other witnesses have to say, and (d) the credibility of the witness. It will then be accorded a weight depending upon the outcome of that exercise.

12.68. For understandable reasons, the Customer Review did not provide for cross-examination of the customer's evidence. Properly, the Bank recognised that the absence of cross-examination was likely to disadvantage the customer. The Bank's solution, as it told me, was to impose a "low evidential bar", but only in relation to D&I, under which, unless the documentary evidence actively contradicted the customer's version of events, the customer would be believed.

12.69. However, when assessing D&C loss, the Bank not only applied a different evidential standard (as I have explained above), but it also appears to have unduly focused its approach on the contemporaneous documents.

12.70. The Bank explained in its submissions to me that, in its view:

> "the approach adopted allowed for sufficient documentary evidence to be collated and scrutinised by the Independent Reviewer in order for a fair assessment to take place in the time available, consistent with the desire for a swift process."

12.71. As explored in Chapter 11, the documentary evidence collated by the Bank for the purpose of the Customer Review primarily comprised hard-copy documents. Where requested (for example, by the assessors if they perceived obvious gaps, or where a customer referred to a specific document that was not on the hard copy file) searches of the electronic files were undertaken. The pool of documents comprising the Bank's review files was therefore more limited than the scope of disclosure required of parties in court proceedings. It was also more limited than what had been represented to customers, who were told in the Next Steps letter sent out from 21 April 2017 that "The assessment process will consider all of the information available to us from our own records".

12.72. The Customer Review was not a litigation process. It was designed to be fast and simple. It is therefore understandable that the Bank did not collate the breadth of documents that it would do for the purposes of litigation. It does, however, mean that the documentation made available for the purposes of the Customer Review was of a limited scope. I would have expected this to be acknowledged by reviewers in the course of the Customer Review and reflected in the application of a more relaxed, forgiving approach to the evidence.

12.73. Moreover, although documentary evidence is generally accepted to be some of the most persuasive evidence available, it is not infallible. This is particularly so in fraud cases, as fraud is seldom deliberately documented by the fraudster, and a fraudster may take steps to conceal the fraud by either creating documentation to cover his or her tracks, or by destroying or doctoring documentation which might otherwise give rise to suspicion. I have discussed in Chapter 11 the potential unreliability of the Bank's records because of the fraud.

12.74. In the absence of cross-examination of the authors of the documents it is often difficult to test these matters. As I have said earlier in Chapter 11 my team did not identify any documents that had obviously been falsified, but they could not rule out that possibility given the nature of our review. Moreover, some customers indicated that Lynden Scourfield

had told them to document matters to look as though certain business proposals had been initiated by the customer, rather than from the convicted individuals.

12.75. The possibility that the documentary record may be incomplete, incorrect or otherwise unreliable is something that I would have expected to see recognised by the reviewers and reflected in their approach to the evidence when assessing customer submissions concerning D&C loss.

Customer submissions

12.76. As I have explained above, the Bank was generous in its treatment of customer submissions in respect of D&I loss:

> "To mitigate the absence of cross examination of witnesses, a low evidential bar was established when considering the personal impact on individuals (i.e. in the absence of any express evidence to contradict, the customers recollection of events would be accepted by the Independent Reviewer when determining D&I."

12.77. However, its treatment of customer submissions in respect of D&C loss was different. Essentially, the Bank did not give weight to the evidence of customers as set out in their submissions unless their version of events was supported by the contemporaneous documentary record. In other words, the customers' written submissions were not accepted as primary evidence in support of their claims.

12.78. The application of "legal principles" to the D&C assessment (and not to the D&I assessment) cannot justify the distinction. As I have noted above, legal principles and legal process are two different matters. It does not follow from the fact that the Bank applied "legal principles" to one type of loss but not the other that there should be a different approach to the customers' submissions in respect of each type of loss. Rather, the Bank's argument was a practical one: D&I losses being typically inherently personal and not readily susceptible to documentary proof, evidence would not as a general rule be reasonably expected to be in the Bank's files, whereas information about the company's financial position and prospects would be.

12.79. In the context of the Customer Review, I do not accept this as a sufficient justification for dismissing a customer's evidence regarding D&C loss unless expressly underpinned by documentary evidence, whilst accepting that same witness' evidence regarding D&I loss unless contradicted by documentary evidence.

12.80. Nor do I accept that these are, in any event, the only two alternatives in the absence of oral cross-examination. I can understand that unquestioning acceptance of customer submissions (subject only to active contradiction in the documents) presents an extremely low evidential bar. But that does not mean that the only other option is rejection of the evidence unless expressly supported by the documentation available to the Bank. Although the testing of evidence is ordinarily carried out by way of cross-examination in the courtroom, there is no reason why a similar evaluation process cannot be undertaken in the absence of oral examination. The question is whether, on the balance of probabilities, what

the witness is saying is true. Circumstantial evidence and corroborative witness evidence are both tools that can be employed without cross-examination.

12.81. Therefore I do not consider that the Bank's decision to limit its acceptance of the evidential value of customer submissions to its D&I assessment, and focus on the documentary record when it came to the assessment of D&C loss, was fair and reasonable within the context of the Customer Review. I also consider that it had material consequences for the integrity of the D&C loss review.

Consequence of the Bank's over-reliance on the documentary record

12.82. From our review of the sample cases, the consequence of placing the burden of proof in claiming a D&C loss on the customer and requiring the customer to prove their case was that, in practice, the Bank treated the customer as an adversary. The combined effect of this and the Bank's over-reliance on the documentary record, meant that it was only if the contention advanced in the customer statement was supported by documents held by the Bank or supplied by the customer that the contention (and the claim to D&C loss) was accepted as proved.

12.83. Moreover, it appeared to the team that as individual directors' statements were treated as separate claims, insufficient weight was on occasion given to the potentially corroborative value of these other statements. In one sample case, the Bank received submissions from seven individuals involved with the business. The solicitor representing all seven individuals had made clear that the (sample) director's submissions constituted the lead submissions for the other six individuals. The submission therefore should have been treated as evidence carrying additional weight on the basis that any given part of it was likely to be corroborated by others. Rather, it was assessed against the documentary evidence held by the Bank, with much of its content being dismissed as being not made out on the documents.

12.84. This is not to say that the Bank's assessors were unaware of, or always ignored, the submissions of other directors. In one case, a director had confirmed his participation in the Customer Review, but provided no information, and the records held by the Bank appeared to have been almost entirely lost. (As I explained in Chapter 11 I asked the Bank about this, and the Bank confirmed that it did undertake additional searches, including searching its electronic records, but could find nothing further.) In its assessment of the customer's case, the Bank's review team supplemented the material available for the Customer Review by looking at the submissions of other directors related to the business.

12.85. Other particular effects of the Bank's approach to customer submissions when assessing D&C loss were observed widely, across the files, and cannot therefore be dismissed as the odd divergence in specific analysis of a given file. It is difficult to assess the impact of the Bank's approach. The following list provides four examples from sample cases, but is by no means comprehensive:

(1) In the first sample case, the customer's statement contended that his earning capacity (and therefore income) had been reduced by 25% following the forced sale of 25% of his income producing assets. Whilst accepting that under IAR's oversight, the assets had

been sold, the Bank rejected both the contention that the sales were forced, and that they had reduced the customer's income (at all), in each case on the grounds that there was "no evidence" to support the customer's statement. In neither case were the customer's contentions contradicted by the documentary evidence in the Bank's files. In both cases, the contentions were prima facie logical, and were evidenced by his statement, which provided explanatory detail. Yet the Bank's legal assessment of that point was that the customer "has not demonstrated that there was any actual loss of … production capacity resulting from these property sales." The Bank's conclusions demonstrate not only the strictness of the documentary evidence requirement, but also that its practical effect was to apply a standard of proof that went beyond the civil standard of "balance of probabilities".

(2) In the second sample case, a key contention by the customer was that Lynden Scourfield had withdrawn the company's overdraft at a particular time. The Bank's assessor concluded, from the chronology of events and correspondence before and after the date that the overdraft was allegedly withdrawn, that the overdraft may well have been withdrawn by HBOS at that time. On that view (with which my legal team agreed), the customer's version of events on this point was credible and corroborated by the circumstantial evidence. Despite the assessor's comments, the Bank's legal assessment concluded that there was "no evidence" that the overdraft had been withdrawn. Whilst it is correct that on the papers available, there was no express record of either any threat to withdraw, or that the overdraft was in fact withdrawn (rather than voluntarily repaid), the circumstantial evidence was sufficient to support the customer's contentions, applying the standard of the balance of probabilities.

(3) In the third sample case, the Bank's reviewers had concluded that the Bank would have (absent the fraud) exited the relationship at a certain date. The customer statement contended that the customer would have been able to obtain finance from elsewhere at that time (either from another market lender, or because the customer had strong contacts in the industry and could have obtained private funding). Save for a short comment in one internal email on the file opining that the customer would not be able to re-finance elsewhere, the file was silent on the point. The Bank did not revert to the customer seeking further clarification or evidence, but dismissed the customer's contention because "[the customer] has not provided any evidence that [they] would have been able to obtain alternative financing elsewhere had [they] sought to do so" and that, therefore, "It has not been established that the Company could or would have successfully obtained alternative financing elsewhere but for the involvement of [Lynden Scourfield]." As the customer's submission had expressly addressed alternative financing, it is clear that by "evidence" the Bank was referring to documentary evidence.

(4) In the fourth sample case, a customer complained that the fraudsters had coerced them into acquiring the assets of the business through a Newco, at a price which did not reflect the value of the assets. The customer's claims were rejected on the basis that a number of facts "had not been demonstrated", but each of those facts was expressly referred to in the customer's submissions. It is clear that, in rejecting the claims, the Bank was relying

on the lack of supporting documentary evidence in dismissing the customer's assertions. However, applying the lower D&I evidential threshold, the Bank took those same assertions into account when implementing a sizeable uplift to the customer's D&I redress.

12.86. In many cases it is difficult to see what documentary evidence customers could reasonably or realistically have been expected to produce, in view of the lack of disclosure and access to documentation, and in view of the fact that the Customer Review took place a decade or more after the events it was reviewing.

12.87. Hypothetical counterfactuals are even more problematic. By their nature, there would not be any contemporaneous documentary evidence of such hypotheticals. Nor, in all but the simplest of cases, is it reasonable to have expected the customer to have sourced documentary evidence at the time of the Customer Review to prove such hypotheticals. No lender is going to confirm that it would have been willing to provide finance over a decade previously, and without seeing any evidence of the company's financial status at the time. In litigation, the matter would likely require expert financial evidence, but the Bank declined to provide funding for such advice in all but a very small number of cases.

Conclusions on the D&C evidential threshold

12.88. In my view, the Bank's approach to evidence in relation to claims for D&C loss was not fair and reasonable:

(1) The Bank made no allowances for the fact that these were fraud claims, and therefore the documentary record maintained by the fraudsters might be incomplete or misleading; or for the fact that the events in question occurred many years ago; or for the fact that often customers did not have access to the necessary documents, information or expert advice to make their case.

(2) The Bank failed to communicate its approach to customers, and such communication as there was, was unclear and uninformative. Customers were not aware of the D&C evidential threshold being imposed by the Bank, of the limited weight being attributed to their written submissions, or of the extent to which the Bank focused on the documentary record.

(3) The D&C evidential threshold which was imposed by the Bank was higher than the standard applied by courts in civil proceedings. The Bank required all claims to be reflected in the documentary record, and the Bank gave little to no weight to the evidence of the individuals involved unless their evidence was corroborated by the documentary record. The Bank also appears on occasion to have given little weight to the corroborative evidence of other directors making similar claims.

12.89. The point was accurately captured during one notably exasperated exchange between Professor Griggs and the Bank in one of the sample cases, in which Professor Griggs stated that:

> "[the Bank] cannot have [its] cake and eat it in terms of this not being a legal process…. There has to be an element of good faith by [the Bank] which falls within [the Bank]

stating that this is a voluntary process where the bank wants to provide fair and generous redress. I am not sure that asking for evidence on everything chimes with that."

12.90. I agree with Professor Griggs' sentiment.

12.91. Customers' claims for such losses would have had no chance of success as a result of the Bank's approach to evidence in relation to D&C loss. Customers were told to put together a statement setting out what loss they believed they had suffered as a result of the IAR fraud, based upon what they could recall of the events from over a decade previously, and without the assistance of either contemporaneous documentation and without in most cases financial expert assistance. The result was, understandably, that many customer submissions were relatively high-level and emotionally driven, and factually far less detailed and accurate than they otherwise would have been. This then provided the Bank with a reason for dismissal of the claim when assessed against the requirements of a formulated legal claim, and against an evidential threshold by which, unless what the customer said was expressly reflected in the documentation held by the Bank, it was dismissed. The result was a standard of proof above the civil standard.

12.92. Unfortunately, a process designed to be a "customer-focussed compensation scheme" that delivered "swift, fair and appropriate compensation without the need for customers to engage in a lengthy, onerous or distressing legal process" did not turn out that way. The reliance on the need for "ease" and "speed" as a justification for applying standards that are stricter than those that would be applied in court in one part of the Customer Review (D&C loss), but invoking those same requirements as the justification for applying a laxer test in the other part of the Customer Review (D&I), is difficult to understand. In those circumstances, the Bank's application of strict evidential standards when assessing D&C loss, but not when assessing D&I, appears inconsistent and difficult to justify.

12.93. I should also note that my team observed that the Bank did not necessarily apply the same evidential strictures when reaching its own conclusions. For example, in one sample case, the Bank's reviewer repeatedly commented that four of the directors must have been "happy" to work with the fraudulent individuals, and with the decisions being taken by them, because there was no evidence in the contemporaneous documentation that they had complained about the fraudster's behaviour at the time but had continued to work with QCS in the new entity. This assumption was based largely upon an absence of information, an absence that would have been fatal to a customer submission. Nor was it logical, given that the individuals were not at the time aware of the fraud being perpetrated. Yet it formed part of the Bank's basis for concluding that those individuals had not suffered any detriment as a result of working with the fraudsters.

(d) Causation and counterfactuals: value of the business

12.94. As I explained above, the Bank's approach to assessing the impact of the fraud on the value of the business was dictated by a series of business and individual level questions. These focused primarily upon the financial distress that the business was under at the time of entry into IAR, the reasonableness of actions taken in respect of the entity, QCS fees,

loans advanced and the value of the business at the time of exit from IAR (invariably, upon failure of the business).

12.95. There are three key concerns as to how this methodology was applied in practice:

(1) First, there was an over-emphasis on the balance sheet valuation of the business at the time of entry into IAR. The Bank's approach appears to have been to assess its valuation at the moment in time when it entered IAR and, if it had no shareholder value at that time, generally to have made the presumption that the fraudsters' actions caused no loss.

(2) Secondly, there was an inappropriate focus on whether individual actions of the fraudsters were "reasonable".

(3) Thirdly, there was a failure to properly consider a non-fraudulent counter-factual.

12.96. Let me address each of these in turn.

(1) Over-emphasis on the valuation of the business at time of entry into IAR

12.97. Across the sample files that my team reviewed, the primary question that the Bank appears to have focused on is the value of the business at the time of entry into IAR, from which the Bank then reached a view as to the appropriateness of it being referred there. In performing these valuations, the Bank primarily concentrated on the balance sheet value of the business, and generally gave little or no consideration to its future prospects (although in many cases the Bank noted that the business was reliant on continued support from the Bank to continue trading).

12.98. Many customers pointed out to me that their businesses were small, early stage and reliant on meeting liabilities from day-to-day trading receipts. Over-reliance upon the balance sheet value in the majority of cases therefore produced a negative outcome. The Bank then built upon this negative figure to conclude that, first, the referral of the business to IAR had been appropriate, and, secondly, that the business, having had a negative value from the outset, was bound to fail in any event and accordingly suffered no loss as a result of the fraud. As I have indicated, a number of customers indicated to me that the Bank had expressed the view to them during outcome meetings in particular, that there could be no loss to the company because it was in IAR.

12.99. In my view the Bank placed too much emphasis upon the valuation of the business at the time of entry into IAR, and whether or not its entry into IAR was justified.

12.100. The Bank concluded, in all but one sample case, that the businesses had no value at the point of entry into IAR, and in all sample cases, it concluded that the businesses would have failed even in the absence of the involvement of Lynden Scourfield and his associates.

12.101. Divisions such as IAR are for businesses experiencing financial difficulties. It is to be expected that the vast majority of companies would fail a test of "Did the company have any value at the point of entry to IAR?" if the emphasis is on the balance sheet position at the time.

12.102. However, the purpose of turnaround specialists is to enable, where possible, businesses to be managed out of their financial difficulties and back into the Bank's "good book". These departments are not simply for the purpose of winding companies up at minimum loss to the bank's position (although that is generally their purpose if a return to the "good book" is unachievable). Where there is a prospect of a business being turned around, directors and shareholders are often encouraged to inject additional funding, whether by way of personal loans and guarantees, or raising additional equity, in the hope that this will enable the business to be returned to health.

12.103. On the assumption that turnaround divisions serve their purpose and are even modestly effective, one would expect a percentage (however small) of businesses to be successfully turned around. For comparative purposes, I requested turnaround rates for other IA offices (i.e. those that had not been tainted by any suggestion of fraud) from the Bank, but was told that these were not available. Therefore it is not possible to ascribe, even at the most general level, the statistical percentage of businesses that might have been turned around but for the intervention of the fraud. However, it seems to me that a 100% failure rate of sample businesses that have been identified as having been fraudulently managed by individuals who have been convicted of fraud, indicates a likelihood that the IAR fraud impacted and/or impaired the prospect of a successful turnaround for at least some of the businesses concerned.

12.104. The Customer Review did not make a single finding of D&C loss across any of the businesses that it reviewed. This should, in my view, have caused the Customer Review to question its approach to the assessment of business value and the prospects of turnaround.

12.105. In summary, I consider that the Bank placed too much emphasis in its analysis on the balance sheet value of the business upon entry into IAR, and the appropriateness of its entry to IAR. As one customer's solicitor pointed out in correspondence with the Bank, a company's value is not simply a matter of its balance sheet, or even its revenue generation. There are many companies that have high valuations before they have generated any revenue, or indeed whilst they are at an early stage and loss making.

12.106. The analysis of whether a company may succeed or fail is far more nuanced than its valuation at a given point in time. Although the Bank's methodology did proceed to consider the impact of the treatment of the business during its time in IAR (which I turn to below), that analysis was pervaded by the overarching attitude that the businesses did not have any value at the time of entry into IAR and were bound to fail, with the Bank being placed as the victim of all further loss thereafter. As expressed by one customer's solicitor in an email to the Bank in the course of the Customer Review, the Bank's approach infers something approaching denial of the real consequences of the fraud.

(2) Relevance of the "reasonableness" of the fraudsters' actions

12.107. Following questions concerning the value of the business upon entry into IAR, the methodology turned to questions investigating the actions taken by the convicted individuals during the business's time in IAR. In each case, the question asked the

reviewer to assess the reasonableness of the specific action as part of a turnaround strategy, and the reasonableness of the fees being charged by QCS.

12.108. In its submissions to me, the Bank said that it was:

> "especially keen to understand how Businesses were treated while in IAR, particularly in circumstances where actions taken during their relevant 'turnaround' phase could be considered to have been reasonable (i.e. had they been taken by individuals other than the convicted criminals)."

12.109. I address the enquiry into the "reasonableness" of the convicted individuals' actions in Chapter 13 in the context of D&I. The impact appears to have been to extend the Customer Review to non-fraudulent behaviour for the purposes of the D&I review (but not the D&C review).

12.110. In the context of the D&C review the approach appears to have been that, were the individual action in question something that could equally have been done by a non-fraudulent individual, it could be disregarded as having any relevant causative impact.

12.111. This approach was applied even in respect of files where the *modus operandi* of the fraud was clear on the file. It was also applied to files that had formed part of the criminal proceedings, and based upon which Lynden Scourfield and his associates had been convicted.

12.112. Thus for example, in one of the sample cases that had formed part of the criminal proceedings and which exhibited significant fraudulent activity, the assessor noted that a document purporting to advise the business to cease an acquisition strategy indicated that IAR had acted reasonably. The assessor went on to note that the advice appeared not to have been implemented, and other comments in the file suggested that the assessor questioned how much influence the convicted individuals had over the director in question (with the clear implication that the customer may have been to blame for the failure to implement the advice). It was, however, clear that, notwithstanding the advice to cease the acquisition strategy, the Bank had continued to fund expansion. Indeed, as a practical matter, the expansion could not have continued without further funding, over which Lynden Scourfield had control. The customer's evidence (in the customer submissions) was that the continued expansion had been instigated or encouraged by Lynden Scourfield and his associates. Moreover, their bullying and aggressive behaviour had been expressly noted in the criminal proceedings and was widely acknowledged across the files. The methodological compartmentalisation of individual actions and advice in this way, with a "yes/no" assessment as to the reasonableness of each individual action, meant that the relevant context of that aspect of the review was lost.

12.113. It is true that this issue is closely linked to the issues arising out of the D&C evidential threshold. In my view, however, the approach of analysing each action by the convicted fraudster against a test of reasonableness was only appropriate to the primary assessment of whether the fraud was perpetrated on the file. It is of course necessary to identify whether, in any given file, fraudulent conduct has been displayed. It cannot be assumed that the mere involvement of the convicted individuals means that they

perpetrated their fraud in relation to every file that they touched. However, that analysis must be holistic, focusing on whether the overall treatment of the business exhibited the hallmarks of the IAR fraud as identified in the criminal proceedings.

12.114. However, if it is concluded, following that enquiry, that fraud or attempted fraud has occurred on the file, then the question turns to the impact of the fraud. At that point the objective reasonableness of any particular action within the fraud is irrelevant. One does not look to identify which actions were sufficiently fraudulent to cause loss, and which action from within a chain could (in isolation) have equally been implemented by a non-fraudulent individual. The causative impact of the fraudulent from the non-fraudulent cannot be separated out in that way. The correct approach is to apply a counter-factual in which the file had never been near the fraudster. How would the business have been handled, from the outset and onwards, by a non-fraudulent individual? It is only in the very narrow circumstances that the non-fraud scenario would have resulted in the same action being taken at the same time and following the same sequence of events that the counterfactual will show the fraud to be causatively irrelevant to the action in question. But that will be rare and is not what the Bank's assessment of reasonableness of each individual action achieved.

12.115. Conversely, if it is found that fraud is not sufficiently evident on the file, then assessing the reasonableness of individual actions would be relevant only to the assessment of a claim for bad/negligent/aggressive banking practices - a matter with which the Customer Review expressly claimed it was not concerned.

12.116. In my view, the application of a "reasonableness" test to individual actions was not a sensible approach to apply when assessing D&C loss flowing from fraudulent conduct.

12.117. The approach also had the unfortunate effect of creating the impression that the Bank was denying the IAR fraud itself. As I mentioned in Chapter 8, a number of customers expressed the view to me that the Bank, having purported to apologise and recognise that the individual had been a victim of fraud, then appeared to deny the existence of the IAR fraud and responsibility for its consequences when considering their claim. This was all the more acute in relation to those cases that had formed the subject-matter of the criminal proceedings, and where customers had given evidence at the trial that had been accepted. Customers expressed the view that they felt that they had been believed in one, far more stringent, forum, only to be disbelieved by the Bank.

(3) Non-fraudulent counterfactual

12.118. The Bank's over-emphasis on the status and value of the business upon entry into IAR also resulted in the Bank failing properly to consider the non-fraudulent counterfactual. What the Bank should have asked was "What would have happened to this company but for the involvement of the fraudsters?"

12.119. The question of what would have happened had the business been managed by a reasonable (and non-fraudulent) turnaround team is not an all or nothing question, but involves a number of possibilities: Would the company have had any chance of

turnaround at all? If so, what would have happened to it along the way? Even if, on the balance of probabilities, ultimately it would not have been successfully turned around, would this have been immediate? Or would it have survived for some time before being put into administration (or equivalent)? If so, when, what would the administration have looked like, and what would have happened in the interim period? What would the directors' liabilities have been (for example, under their personal guarantees) had the business been put into administration at a different point in time? Would the directors have invested (and lost) less of their own funds without the influence of the fraudsters?

12.120. These questions may well involve considering not simply the issue of whether the Bank would have been willing to finance the business, but also the likelihood (or "chance") of various third-party actions. The evaluation is therefore complex and nuanced. Whether the Bank would have advanced funding (and, if so, when and in what amounts) may be a question to be analysed on the balance of probabilities, but whether external (re)financing would have been available, or what other third parties might have done, may entail a loss of a chance analysis. It would, in the context of a litigation process, almost invariably require expert evidence.

12.121. In a non-legal process such as the Customer Review, investigation of these matters in the same depth cannot be expected. This is where applying legal principles to a non-legal process calls for common sense. As I have noted in Chapter 10, in the Customer Review, except in a small number of cases, the Bank declined to provide funding for any expert financial assistance. The customers could not therefore be expected to "prove" the value of loss of a counterfactual in the same way that they would be required to in litigation. Rather, the onus fell on the Bank to consider properly and fairly possible counterfactuals, taking into account any relevant customer submissions.

12.122. Whilst the Bank did evaluate customer claims, including counterfactuals advanced by customers in the course of their D&C claims, the analysis of these claims suffered from the issues that I have already identified, including:

(1) Placing the burden of proof on the customer to prove that it was the involvement of the convicted individuals that caused the company to fail, combined with the application of the D&C evidential threshold, discussed above. This meant that much of the customer submissions was dismissed, given the absence of express documentary evidence underpinning them, with the Bank simply concluding that it had not been established that the company would not have failed but for the involvement of IAR.

(2) The over-emphasis upon the negative value of the business at point of entry into IAR, and the over-arching presumption that those properly referred to IAR were almost certain to fail.

(3) The adoption of an adversarial approach, with the result that, if the customer's (often overly optimistic) version of events was rejected, there was little or no consideration of an alternative, more reasonable counterfactual.

12.123. My financial team did not undertake detailed analyses of counterfactuals in individual cases. However, for the purposes of testing whether the Bank's approach may have impacted the outcome in the sample cases, they considered what, in their view, a reasonable bank would have done in respect of each sample case, taking also into account the customer submissions and documentary evidence available.

12.124. The team's views may be summarised as follows:

(1) In a significant number of cases, they agreed that the financial outlook of the business was sufficiently unsatisfactory that a reasonable banking turnaround team would have put the business into administration or a pre-pack sale within a relatively short period of time after entering IAR (the "failed businesses").

(2) In a small, but not insignificant, number of cases they considered that a reasonable banking turnaround strategy could have had a credible prospect of resulting in a successful outcome for the business. Applying reasonable assumptions as to the likelihood of third-party actions, they concluded that in those cases, the business could have had a positive valuation following such a turnaround strategy, and therefore there is a case that D&C loss was suffered as a result of the IAR fraud. I should add, however, that they thought that the valuations asserted by customers relied upon unrealistic assumptions as to third party actions, and/or overly optimistic profit projections (the "turnaround businesses").

12.125. The result is that I consider that the Bank's failure to properly consider counterfactuals may have resulted in D&C loss being denied, on the basis that the business would have failed, where it should not have been. I return at the end of this chapter to briefly address the relevance of the D&I redress paid by the Bank in this context.

(e) Other consequences of the IAR fraud

12.126. As noted above (paragraph 12.37), the Bank's methodology identified a list of types of D&C loss that it was anticipated might be claimed by customers. These included loss of opportunity, refinancing costs, loss of management time and damage to reputation.

12.127. Others, not included in the list, would include any cash injections or loans advanced by the customer, and loss of income from alternative employment or business ventures.

12.128. Given the nil outcome for D&C loss across the Customer Review, it follows that no claims for such losses were accepted by the Bank. It is not always clear why, but where express reasons are recorded the Bank's reasoning appears to have been that the business would have failed anyway, combined with a failure to meet the D&C evidential threshold. It therefore appears to again result from the failure to consider the proper counterfactual, even for failed businesses.

12.129. This seems over-simplistic. Loss of opportunity to engage in alternative employment/business activities during the years that a business had been artificially kept alive by IAR could have been compensated as D&C loss. There is a case that the IAR

fraud caused some loss, even in relation to failed businesses, yet in no cases was any D&C loss paid out under these heads.

12.130. On the contrary, my team saw a number of occasions on which the Bank's assessors seemed to take the view that the impact of the IAR fraud was to the benefit of the companies and individuals (because they continued to be funded when they should have faced insolvency much sooner) with only the Bank suffering loss. In a number of the sample cases, my team observed assessor comments that directors had benefitted by the actions of the fraudsters, because they continued to draw a salary from the business whilst it was being artificially kept alive by Lynden Scourfield and his associates injecting further bank lending.

12.131. Undoubtedly the Bank was the biggest victim of the IAR fraud, to the tune of hundreds of millions of pounds that were improperly lent to businesses where there was little if any hope of such borrowing being sustainable, or ever repaid. But the fact that the Bank was a victim does not mean that the businesses, their directors, owners and others (such as other creditors) were not. Indeed, from the customer perspective, the Bank stands in the position of having vicarious liability for the actions of the fraudsters. If the only possible counter-factual were immediate administration (rather than any chance to resurrect the company having been lost), the correct assessment of the individual's loss would involve an enquiry into what alternative earnings the individual would have made, in the absence of the fraudsters' actions (e.g. through employment by another company). Any earnings deriving from the IAR fraud (i.e. salary during the continued life of the company) would then fall to be set off against any such counter-factual income. But the simple fact that the individual continued to receive income from the company as a result of (or despite) the IAR fraud does not mean that they have net benefitted from it. The enquiry must engage with the non-fraudulent counterfactual, including alternative income streams.

12.132. These are heads of loss where it is difficult to see what evidence over and above witness evidence could realistically have been expected of the customer. The D&C methodology expressly acknowledged that claims for loss of profits (similar to earnings) were "inherently speculative" and envisaged that the Bank would apply a:

> "probabilistic approach (applying a percentage discount to allow for the fact that the transaction may have been less profitable than anticipated or to reflect the uncertainty of the outcome more generally)".

12.133. I have commented above that such an approach would have been appropriate, given that hypothetical counterfactuals reliant upon third party actions should properly be addressed on a loss of a chance basis. However, we did not come across any instances of the Bank applying such a nuanced approach in practice.

12.134. Funds injected by customers (even in failed business cases, where but for the fraud the business would have been put into administration at a much earlier date), should similarly have been an obvious form of D&C loss, and acknowledged as such. Yet the

Bank took the approach of either presenting these as D&I redress, or as a special category of "voluntary payment".

12.135. Similarly, at the business level, QCS fees were returned as a separate payment, as explained in Chapter 4, expressly without being recognised as a D&C loss. The Bank explained this in its submissions to me as being a policy decision to refund these fees as a "voluntary payment", made "even if the fee appeared to have been appropriate or funded from increased borrowing from the bank that was not later repaid." This response again exemplifies the siloed approach to whether individual actions of the fraudsters were "reasonable" or not, in place of assessing the non-fraudulent counterfactual.

12.136. Turning to reputational damage, as I have noted above, the Bank's methodology took a narrow view that such claims could only be brought as a claim in defamation. This approach was carried through into the assessors' approach in sample cases:

(1) In one case, a customer complained about a confidentiality agreement that HBOS had pressured them to enter into at the time of the insolvency and sale of the business. The customer contended that the confidentiality agreement had prevented them from responding to adverse media coverage implicating them in the failure of the business, and that this had impacted their earning ability and personal life. The Bank assessed the complaint in defamation, flowing from the media statements, and dismissed the claim on the grounds that the customer had not proved that the Bank was responsible for the statements in the media. It seems to me that this was an overly defensive analysis. Until the public exposure of the IAR fraud, the failure of these businesses was said by many customers to have prevented them from engaging in further business activity, for example by affecting their credit rating or their professional reputation. Treating the customer's (non-legal) submissions as restricted to a claim in defamation, and then assigning, without any investigation, the media reporting as the dominant cause of loss (rather than the fact of the IAR fraud itself), was unduly defensive and narrow. The claim could more easily have been analysed as being for loss of earnings due to the reputational damage caused by the IAR fraud. There was no reason to restrict it to being claim for damages for loss of reputation per se. The defensiveness of the Bank's approach was compounded by the Bank's dismissal of the customer's concerns over the confidentiality agreement, and the unrealistic contention that as a matter of fact it had not inhibited the customer's ability to correct the record. The review of this matter exhibited an inappropriately adversarial approach in the context of the Customer Review.

(2) In other cases, the Bank failed to acknowledge a claim for loss of earnings attendant upon reputational damage caused by the fraud, concluding that the claim for loss of earnings had not been made out because the customer had not made out that the business would have continued trading successfully but for the IAR fraud. This analysis overlooked the impact of the reputational damage of the IAR fraud upon the customer's ability to earn. I assume that the failure to consider

this aspect of the claim may have stemmed from the view taken in the methodology that such claims could only be brought as a claim in defamation.

12.137. There were various further, more specific, heads of consequential loss alleged by customers. These included acts of the Bank at the time of failure of the business, which were not necessarily the actions of Lynden Scourfield and his associates, but which may well have "flowed" from the IAR fraud. For example, in a number of cases customers complained that they had been pressured to take actions by the Bank under threat of consequences to unrelated lending, such as in respect of their private property or unrelated businesses. None of these claims were upheld as D&C losses (although some resulted in, for example, outstanding debt with the Bank being written off, or the D&I redress being increased). The basis for refusing them is unclear. Again, they are claims which, even for failed businesses, required considering against the non-fraudulent counterfactual, and there may have been D&C loss caused by the fraud.

12.138. These matters are not inconsequential. Customers described how they struggled to get themselves onto a financially secure footing again, and in particular the impact of the IAR fraud on their ability to move forward, engage in alternative business ventures and/or alternative employment. In one respect it was a far more destructive effect of the IAR fraud than any loss of business value, as it prevented people from moving on with their lives, and left them dependent upon others. By categorising these claims as claims for reputational damage (and dismissing them as therefore only being concerned with a defamation claim), the Bank failed to give one of the potentially most important impacts of the IAR fraud due or proper consideration.

(f) Writing off customer debts with the Bank

12.139. There is a further curiosity in the Bank's dealing with customers that is relevant to D&C loss. As I have noted in Chapter 10, and as outlined in the Bank's press release of 7 April 2017, the Bank took the approach of writing off customers' business and personal debts that remained outstanding with the Bank. We saw in Chapter 3 that in a number of cases this amounted to a significant sum, which was in addition to the redress paid out for D&I.

12.140. As we have seen, the methodology expressly envisaged that it was hoped that the addition of 8% compensatory interest and the write-off of any relevant business and/or personal indebtedness to the Bank would cover consequential losses (see paragraph 12.27 above). It is therefore clear that the Bank appreciated that the write-off of such debts might in some cases represent a form of compensation for consequential loss. (Although as no compensation for direct loss was awarded, no compensatory interest in respect of the same was awarded.)

12.141. The payment of what was effectively D&C loss for customers whose debt remained with the Bank, whilst refusing compensation for the same loss for those who had refinanced elsewhere, was not reasonable for the reasons given in Chapter 10.

(g) Outcome meetings, and the role of additional information in assessment of D&C loss

12.142. In its submissions to me the Bank explained that, for losses claimed that did not meet the legal tests:

> "details were provided to explain why the loss was not recoverable. These explanations allowed customers the opportunity to respond with additional information that might strengthen their claim, for example by providing supporting evidence".

12.143. The position with D&I loss was different, as we see in Chapter 13.

12.144. As I explained in Chapter 10, we did not see this reflected in the sample cases. Explanations were at a high level and did not reflect the full complexity of a business' history. I am unable accept the Bank's submission that it provided sufficient details to the customers to explain its conclusions as to why loss was not recoverable. The lack of any detailed explanation, combined with the lack of transparency over the evidential threshold being applied to claims for D&C loss, means that I am also unable to accept the Bank's submission that the opportunity to "respond with additional information" gave the customer an appropriate opportunity to change the outcome of the Bank's D&C loss assessment.

IV RESISTANCE TO PROFESSOR GRIGGS' VIEWS ON D&C LOSS

12.145. In a number of the sample cases, Professor Griggs expressed a view as to there being a viable case for D&C loss. As my team has not had access to the majority of Professor Griggs' papers, we are not able to assess the underlying analyses undertaken.

12.146. However, in each of these cases Professor Griggs met resistance from the Bank. The correspondence indicates that the Bank persuaded Professor Griggs to reclassify the redress as a D&I increase, by finding aggravating factors to justify characterising the redress as D&I. The Bank's correspondence then referred to it being agreed that there was no claim for D&C loss.

12.147. Thus in one sample case, the Bank recorded in correspondence with Professor Griggs that "It is important to note that in this case there has been no finding by the Review that the relevant company of the individual has suffered any financial loss". This point was reiterated at least twice in subsequent correspondence. Professor Griggs' view in fact appears to have been that the business "could have been break even and not loss making", but that the counter-factual necessary in order to properly calculate D&C loss was extremely complex. The issue was therefore one of difficulty of assessment, not the absence of D&C loss. However, the Bank simply reiterated the view that "we are agreed that there is no actual value/loss" and that "the customer has not established a financial loss". This illustrates how the combination of the burden of proof and D&C evidential threshold was applied in a manner which rendered the obstacles placed in the way of the customer insurmountable.

12.148. Similar resistance to acknowledging any D&C loss was noted on another sample case. Professor Griggs' note set out the formal advice that he had received from his financial advisers that the company could have had an enterprise value on entry into

IAR in 2003. On the basis of the counterfactual considered by his advisers, the company could have had potential equity value at the relevant later point for the purposes of assessing D&C loss.

12.149. Following a later call between the Bank and Professor Griggs, the Bank sent an email to Professor Griggs in which it summarised Professor Griggs' view as follows:

> "[Y]our team confirmed on the call that the above recommendation was based on what you considered to be a 'fair' outcome taking into account the potential enterprise value of [the customer] on entry into IAR rather than the legal assessment of the merits of the claims advanced in the Review including on the basis of the potential enterprise value argument. Therefore on the call we agreed that in respect of the methodology for the Review, where risk of the alleged losses are assessed on general legal principles, the legal tests for establishing recoverable loss in this case had not been met. However, it was also noted that, based on your experience of having delivered outcomes in more than 70% of the cases in the Review to date, there were various aggravating factors that you had identified on this case which were not necessarily evident in other cases within the Review. For example, you believed that the Bank could have provided a better service to [the customer] on entry into IAR and could have suggested certain actions in support. In addition, you wanted to recognise the specific distress experienced by [the director] when Michael Bancroft became involved. Taking account of these aggravating factors, in your judgment, the compensation figures noted below would be fair and appropriate for this connection and you would apply your discretionary uplift to the D&I awards of [the directors] on this basis…"

12.150. Professor Griggs subsequently acquiesced to this characterisation of the calculation of the redress figure offered.

12.151. In its submissions to me, the Bank said this (reflecting a passage in Professor Griggs Post-Scheme Completion Report following the Customer Review):

> "In a very small number of cases, [Professor Griggs] and his team reached the view that there was a plausible case for financial loss. While in those cases [Professor Griggs] and his team did not conclude that the alleged losses would be recoverable when applying the legal principles, he sought (and [the Bank] agreed) an increase in compensation to reflect his view that the D&I impact on participants was aggravated by that plausible case, based on what he believed to be fair and reasonable. [Professor Griggs] considered that his ability to ensure compensation was awarded in this way, taking into account what was fair and reasonable, as well as the relevant legal principles, delivered a fairer outcome to participants."

12.152. In contrast to how the matter was presented to me in this passage, the correspondence during the Customer Review indicates a reluctance by the Bank to acknowledge a D&C loss, and an attempt to persuade Professor Griggs to re-characterise the compensation as D&I redress. As I have noted in Chapter 5, Professor Griggs had the power to increase the Bank's redress decision, but that formed part of the D&I methodology. As such, Professor Griggs could express disagreement with the Bank's

outcome on D&C loss, but under that methodology he did not have the same power to overrule the Bank's D&C loss decisions. It seems to me that, given these limitations, he did the best that he could in those cases where he considered there to be a D&C loss, to ensure that the customer received some level of financial compensation, despite the Bank's reluctance to acknowledge it as such.

12.153. Indeed, even if the Bank were right that the D&C evidential threshold had not been met, the use of the D&I redress scheme as a conduit to ensure payment of compensation for this purpose lacked transparency, and involved finding "aggravating factors" to justify the application of an uplift instead. This is a tacit acknowledgment by both Professor Griggs and the Bank that the stringency of the D&C evidential threshold unfairly and unreasonably precluded compensation.

V OTHER STRUCTURAL ASPECTS OF THE CUSTOMER REVIEW THAT INHIBITED D&C LOSS CLAIMS

12.154. In addition to the aspects of the D&C methodology that I have identified above, my team has noted that a number of the broader structural aspects of the Customer Review combined to further inhibit D&C loss claims. I have covered a number of these in detail in Chapters 10 and 11. I list them here simply to note their cumulative impact upon the Customer Review's ability to properly assess and redress D&C loss.

Lack of access to financial analysis undertaken by or for the Customer Review team, or funding for customer financial analysis

12.155. The Bank's refusal to disclose to customers any of its financial analysis of the business meant that customers were unable to challenge or assess the accuracy of the Bank's conclusions concerning the business' value and prospects. In parallel, the Bank's refusal (in all but a few cases) to provide funding for the customer to obtain expert financial assistance (as well as its refusal to provide access to the company documents), prevented the customer from undertaking their own analysis so as to evidence their case.

12.156. In view of the D&C evidential threshold being applied by the Bank, the effect was that no customer had any real chance of being able to succeed in a claim for loss of value of the business.

Exclusion of shareholders from the Customer Review

12.157. The modus operandi of the fraudsters was to take control of a business and, by inflating its borrowing (through which they obtained personal gain), ensuring it was failed. By focusing the Customer Review on directors, the Bank did not identify those who were most likely to have suffered the greatest D&C loss. As one customer's solicitor put it in correspondence to the Bank:

> "Directors owe duties to a company; they have few rights. Shareholders, on the other hand, have rights and in this case are clearly the principal victims of the fraud that has been perpetrated on [the business]. [The business], having been dissolved, leaves the shareholders in the position that they, rather than the company, become the rightful

claimants. […] We had thought that the Bank was looking to do the right thing and to compensate the victims. It is obvious that [two shareholders] were forced out of the Company by the Bank […]. Let me be clear. In our view [these individuals] are "victims" (whether badged as shareholders or otherwise). That we have understood is the bank's focus and hence ours likewise."

12.158. Legally, shareholder claims are generally claims for loss which reflects the company's loss (this is referred to as reflective loss). Assessment of the value of the business in the correctly analysed non-fraudulent counterfactual should have enabled assessment of much of the loss suffered by shareholders and creditors. Notably, this would not simply be a question of whether the business would have failed in any event, but also whether any failure would have been sooner and/or on a sufficiently smaller scale to have prevented equity injections or afforded better creditor/shareholder outcome.

12.159. The Bank's methodology correctly identified the issue of reflective loss. However, in practice, the Bank did not permit shareholders to have an input into the Customer Review, including its entity review, in relation to which the Bank similarly concluded a nil outcome across the board. As the Bank's approach to valuation of the business, which I have already addressed above, took a narrow view of valuation at the date of entry into IAR, and gave insufficient consideration to the proper non-fraud counterfactual, resulting in an over-focus on the Bank as the only victim, my concern is that its assessment was insufficient to properly evaluate any shareholder loss.

12.160. As to potential direct claims by shareholders, as noted above, the Bank's methodology, again correctly, identified the possibility of direct shareholder claims, and, moreover, expressly provided for flexibility in considering such claims, should they arise. It should be noted that my team did come across one email in which the Bank informed a customer that "if it is identified during the assessment that potentially [shareholders] may have been impacted by the criminal activities at HBOS Impaired Assets Office in Reading, we will contact them at that stage to discuss next steps". However, we did not come across any case in which the Bank had done so. On the contrary, it appeared to us that in practice, the Bank simply excluded shareholders as a matter of course. Similarly, the Bank resisted those customers who tried to bring shareholders in. The flexibility referred to in the methodology does not seem to have been displayed in practice.

12.161. Furthermore, for those shareholders and creditors excluded from the Customer Review, their chance of bringing a claim in the courts was generally stifled by way of the broad settlement agreements that the Bank required them to sign in order to be paid the QCS fees, and/or for practical purposes by way of the non-assistance clauses in the directors' settlement agreements. I address this further in Chapter 14.

12.162. The combination of excluding shareholders and creditors, and imposing settlement agreements when and on the terms that it did, had the effect of successfully inoculating the Bank from either considering or facing a claim from a significant category of those most likely to have suffered D&C loss.

VI CONCLUSIONS

12.163. In my view the approach to the assessment of D&C loss in the Customer Review did not provide a reasonable basis on which to deliver fair and reasonable outcomes:

(1) The Bank applied unduly onerous evidential thresholds to claims for D&C loss. This was exacerbated by the fact that:

a) The burden of proof was placed on the customer to prove a cause of action, a causal link between specific fraudulent acts and the losses claimed, and the quantum of loss.

b) The Bank did not sufficiently communicate its expectations to customers, and encouraged them not to frame their submissions as legal submissions. There was a lack of transparency.

c) The Bank refused disclosure of any company documents to the customer, in circumstances where it should have been obvious that most customers would no longer have access to company documents. This caused a significant imbalance between the parties to the detriment of customers.

(2) On the whole, the Bank refused funding for expert financial assistance. This would have been necessary to assess a business' prospects in a non-fraudulent counterfactual situation to the standard required by the Bank. It further refused disclosure of its own analysis of business value. This caused a significant imbalance between the parties to the detriment of customers.

(3) The Bank failed to give adequate weight to customer submissions. As a result, the Bank failed to take matters into account that it should have done.

(4) The Bank took an adversarial approach to claims for D&C loss which was inconsistent with the stated context of the Customer Review.

(5) The difference in approach to evidence and causation between the assessment of D&C loss and D&I redress was not properly justified, and was not communicated to customers. There was therefore a lack of rationality, and a lack of transparency.

(6) The Bank placed too much reliance upon the documentary record, without accommodating the fact that the record was limited, and that the documentary record might not be reliable.

(7) The Bank's legal approach to counterfactuals was flawed. In particular, its assessment of the reasonableness of individual actions failed properly to apply the non-fraudulent counterfactual. These matters may have caused incorrect outcomes in a number of sample cases we examined.

12.164. Cumulatively, the factors identified combined to create an environment which, from the outset, was resistant to D&C claims and minimised the likelihood of a finding of D&C loss.

12.165. Drawing together the key points which I have outlined in the course of this chapter, I conclude with the following observations:

(1) First, it seems to me that the manner in which the redress scheme was structured and implemented, minimised the likelihood of D&C losses being paid out.

(2) Second, the Customer Review process was avowedly customer-focused, non-litigious, and contained none of the disclosure or transparency safeguards of litigation. It was essential to the fair and reasonable operation of the Customer Review that the Bank did not revert to treating the customer as a counterparty in an adversarial process. It appears to me that it did fall into that error, to the detriment of customers.

(3) Third, whilst the existence of a very generous D&I redress scheme may have equated to, or, in some cases, surpassed, any D&C loss, it was not, and could never have been, a sufficient alternative to compensation for D&C loss. As a practical matter, the D&I redress scheme distributed redress differently, and to different persons, compared with where D&C loss might have fallen.

(4) Fourthly, the failure to acknowledge D&C loss overtly, as D&C loss, impacted on how customers as the victims of the IAR fraud could have interpreted the Customer Review. An award of D&C loss carries the acknowledgment that the customer is the victim of the fraud. Conversely, the failure to acknowledge D&C loss could carry the message that the blame for the financial failure of the company ultimately lies with the customer.

(5) By contrast, D&I redress acknowledged only that customers dealt with the fraudsters, not that this might have had something to do with the failure of their business. From my regular engagement with customers over the course of the past few months, the impact cannot be understated. It has unfortunately undermined the sincerity of the Bank's apologies and acknowledgments that the customers were victims of the IAR fraud. Moreover, it has denied many customers the sense of justice and closure that I understand the Customer Review was intended to provide.

CHAPTER 13 DISTRESS AND INCONVENIENCE PAYMENTS

13.1. The Bank's methodology for distress and inconvenience ("D&I") payments in the Customer Review was designed so that the amount of the awards capable of being generated was very generous when compared to comparable awards made by the courts. The maximum award achievable under the D&I matrix was over £1million, whereas court awards are generally in the range of a few hundred to a few thousand pounds.

13.2. This chapter proceeds as follows. Part I outlines the legal principles governing D&I payments. This brings out the generosity of payments under the Bank's D&I methodology. Part II describes that methodology. Part III turns to the awards the Bank made under the D&I methodology and matrix. Parts IV-VIII turn to an analysis of the Bank's D&I methodology. Running as a thread through the analysis is the Bank's policy, examined in the previous chapter, of keeping both the D&I methodology and matrix confidential.

I DISTRESS AND INCONVENIENCE: LEGAL PRINCIPLES

13.3. Damages for D&I in tort are strictly controlled. A summary of the position is as follows:

> "As a general rule, torts that require proof of damage do not count "mere" distress or injury to feelings as compensatable loss. So with a claim in negligence for "pure" psychiatric harm (i.e. psychiatric harm that is not consequent on physical injury to the claimant) there can be no claim for emotional distress, anguish or grief, and with the tort of misfeasance in public office damage does not include "distress, injured feelings, distress or annoyance". On the other hand, where the claimant suffers physical injury, the distress and anguish associated with coming to terms with the resulting disability or the knowledge that one's life expectancy has been reduced can be compensated as part of the overall award of damages for pain and suffering…. … in limited circumstances damages for distress following negligent conduct may be available in contract, or in bailment." [47]

13.4. A court may award "aggravated damages" to compensate a claimant who is an individual for additional distress that the claimant proves they have suffered as a result of the defendant's motives or conduct in committing a tort. The distress is an additional injury to the claimant. Examples of such motives and conduct are: malevolence, spite, malice, cover-up, and humiliating, distressing, insulting or offensive conduct.

13.5. As to contract, damages for D&I are uncommon outside personal injury claims, where the loss is claimed as an adjunct to damages for physical injury. They are restricted to situations in which either one of the primary purposes of the contract in question was to afford pleasure, relaxation, peace of mind or freedom from molestation, or they are attendant on physical inconvenience or discomfort caused by the breach.[48]

[47] *Clerk & Lindsell on Torts*,22nd ed (2017), paragraph 1.32.
[48] *Harrison v Shepherd Homes Ltd* [2011] EWHC 1811 (TCC).

13.6. In cases where damages for D&I may be awarded the claimant must prove a causal connection between the tort or breach of contract on the one hand and the D&I on the other. In a case where physical injury is suffered, for example, the tort or breach of contract must have caused the physical injury which in turn causes the D&I.

13.7. Where the court does award damages for D&I, there is no hard and fast rule as to the quantum of the compensation. As I have said above, awards are generally in the range of a few hundred to a few thousand pounds.

13.8. For example, in *Watts v Marrow*[49], (which was decided in 1991) the court awarded a couple £750 each for two years of D&I caused by remedial works to their home which they were forced to undertake because of their surveyor's failure to report on substantial defects before they purchased the property.

13.9. In *Milner v Carnival Plc,*[50] decided in 2010, the court awarded £4,000 and £4,500 respectively in relation to a disastrous luxury world cruise that was cut short.

13.10. In *Hamilton Jones v David & Snape (a firm)*,[51] decided in 2004, damages for D&I were significantly higher than the norm for breach of contract cases. In that case, the compensation was for distress arising out of a mother's loss of her two children for 11 years following their abduction by their father as a result of negligence by the mother's solicitors. The court awarded £20,000 to reflect the seriousness of the distress caused.

13.11. Many awards of aggravated damages do not distinguish the "aggravated" part of the damages award. Where judges have set out the amount of the aggravated damages the aggravation, even in very serious cases, only increases the award by a few thousand pounds.

13.12. In *Rees v Commissioner of the Police of the Metropolis*,[52] decided in 2019, a malicious prosecution and false imprisonment case relating to a murder, the court awarded each claimant aggravated damages of £18,000 to reflect the drawn-out and cynical nature of the underlying police misconduct.

13.13. In *Cairns v Modi,*[53] decided in 2012, the Court of Appeal approved an award of £15,000 as aggravated damages for libel to reflect conduct at trial, including repeated cross-examination on the basis that the claimant was a liar. The "sustained and aggressive" assertion of the defendant's case increased the damages recoverable "by a factor of about 20%".

13.14. In *Gulati v MGN,*[54] decided in 2015, the court awarded one claimant in phone-hacking litigation aggravated damages of an unspecified "small amount" for the manner of his cross-examination. Another claimant received aggravated damages of less than £10,000. The judge refused to award any claimant aggravated damages for the defendant

[49] [1991] 1 WLR 1421
[50] [2010] EWCA Civ 389
[51] [2004] 1 WLR 924
[52] [2019] EWHC 2120 (Admin)
[53] [2012] EWCA Civ 1382 [2013] 1 WLR 1015
[54] [2015] EWHC 1482 (Ch)

newspaper group's denials that phone hacking had occurred. The judge also rejected the claimants' contention that the aggravation should increase all awards by 100%.

II D&I IN THE CUSTOMER REVIEW: BANK'S METHODOLOGY

13.15. The Bank's approach to compensation for D&I was set out in two methodology documents, the Conduct and Legal Assessment and the Redress Calculation. I refer to these two documents together as the D&I methodology.

Conduct and legal assessment

13.16. The conduct and legal assessment was relevant to individuals (i.e. directors) as opposed to entities (i.e. businesses and companies).

13.17. The document explained that the conduct and legal assessment was:

> "an assessment of the individual's experience during the time the entity was in IAR, including their interaction with those individuals convicted of criminal activities at trial, and informs the level of redress which is offered to the individual for Distress and Inconvenience (D&I)".

13.18. The document stated that it was a design principle that the assessment should identify whether there was any personal interaction between the individual and IAR (in particular, with the convicted bankers, Lynden Scourfield and Mark Dobson), QCS and/or RPC.[55] The Bank's assessor working on the Customer Review was to consider the nature and level of the interaction (whether it was high, medium or low).

13.19. To assess the level of interaction with IAR, the assessor was required to consider a number of matters including:

(1) how involved the individual was in the running of the business;

(2) the frequency, nature and timeframe of any interactions with the convicted bankers;

(3) any pressure exerted by the convicted bankers, including undue pressure to work with QCS (including the effect on the individual's decision making as a result of any such pressure); and

(4) any complaints made to HBOS or the Bank or legal proceedings issued against HBOS or the Bank by the individual in relation to events during their time at IAR.

13.20. To assess the level of interaction with QCS, the assessor was to consider a number of matters including:

(1) the frequency, nature and timeframe of the individual's interactions with QCS (including with David Mills, other convicted QCS associates, and any other related consultant); and

(2) any undue pressure exerted by QCS and/or RPC (including the effect on the individual's decision making as a result of such pressure).

[55] RPC was, like QCS, a David Mills business.

13.21. Another design principle was stated as follows:

> "Where the [Customer] Review identifies any information that raises a suspicion of fraudulent or *inappropriate* activity by the Bank or its employees/former employees, it will be appropriately considered and, if required, escalated for further investigation. Decisions in this regard will be discussed at QC Panel i.e. the Review will not "walk past" evidence of wrong doing or detriment" (emphasis supplied).

13.22. The conduct and legal assessment was to be informed by the assessor's responses to a number of questions in the "individual analysis" section of the assessment template. As I have explained in Chapter 4, the Bank developed a detailed template, containing many questions, to be completed by assessors in relation to each business.

13.23. The assessment template contained various sections including "entity [business] analysis" and "individual analysis". The individual analysis section contained questions which related to the frequency and nature of the individual's interaction with IAR (in particular with Lynden Scourfield and Mark Dobson) and/or QCS/RPC. The entity analysis contained a series of questions relating to a business' treatment in IAR.

13.24. Whilst the conduct and legal assessment stated that the assessment was to be informed by the responses to the questions in the individual analysis section of the assessment template, as noted below, the questions in both the individual analysis and business analysis sections of the assessment template were in fact relevant to the assessment of the D&I award.

Redress Calculation

D&I matrix

13.25. The redress calculation provided that the calculation of D&I redress was to be based on the application of a matrix (the "D&I matrix") which in summary took into account the following circumstances:

(1) Category 1 – Direct involvement/interaction of Lynden Scourfield and/or Mark Dobson with the individual, and with the business insofar as that interaction "may have affected" the individual. The relevant involvement/interaction must be while the business was part of IAR.

(2) Category 2 – Direct involvement/interaction of QCS with the individual, and with the business insofar as that interaction "may have affected" the individual. Again, the relevant interaction/involvement is while the business was part of IAR.

(3) Category 3A – Weighted personal impacts: the extent of the individual's personal involvement in the business and the related impact on their life.

(4) Category 3B – Fixed personal impacts: "the detrimental impact on personal life." An award may be "higher" or "lower". "Lower" is "based heavily on the [c]ustomer's account/recollection of events but taking account of any conflicting information available in [the Bank's] files." "Higher" takes into consideration "circumstances where exceptional distress is alleged to have been experienced by an individual."

13.26. There were a total of 10 "assessment points" across categories 1, 2 and 3A. By way of example, the assessment points under category 1 were: (i) decisions made on Lynden Scourfield's and/or Mark Dobson's advice and/or recommendation; (ii) undue pressure to work with QCS; and (iii) period of time in IAR.

13.27. The matrix scoring for each assessment point was based on the assessor's responses to specific questions in the individual analysis and business analysis sections of the assessment template. For example, in scoring the assessment point "decisions made on Lynden Scourfield's/Mark Dobson's advice and/or recommendation" under category 1, the assessor would consider the answers to questions in the individual analysis such as "Did they have interaction with Lynden Scourfield?" and questions in the business analysis such as "Were actions taken based on Lynden Scourfield/Mark Dobson advice and/or recommendations received while being managed within IAR?".

13.28. The matrix scoring also took into account "additional matters raised" by the customer in the customer questionnaire or other information provided to the Customer Review.

13.29. The assessor was required to give a score of 0 (no involvement or impact), 1 (low detriment, involvement or limited impact), 2 (medium detriment, involvement or impact) or 3 (high detriment, involvement or impact) for each assessment point across categories 1 to 3A. It was noted that a degree of judgment was needed when scoring in these categories using the D&I matrix. For category 3B, the assessment required a "yes"/ "no" answer (the question being whether particular types of lower or higher personal impact were present) with a fixed sum being awarded if the answer was "yes".

Calibration of sums under the D&I matrix

13.30. The redress calculation explained that one point under the D&I matrix scored £10,000, two points scored £20,000, and three points scored £40,000, with a scalar then applied "to allow further differentiation between the points scored due to Lynden Scourfield/Mark Dobson and QCS involvement (1.5x) from those scored due to personal impacts (3x)." The fixed sums awarded under category 3B were £120,000 if the answer was "yes" for "lower" impact and £240,000 if the answer was "yes" for "higher" impact.

13.31. The Bank explained to me that in arriving at the figures used in the D&I matrix, it considered various references, including the level of damages awarded by courts for mental distress for deceit or other fraudulent conduct, the level of D&I payments made in relation to upheld complaints elsewhere in the industry and compensation levels for industrial or criminal injuries. In particular, the Bank said that it considered:

(1) The fact that court awards are relatively small (under £10,000). This gave it an "anchor point" for the calculation of D&I payments, which treated the figure of £10,000 as the minimum or base level of any payment offer.

(2) The approach to compensation for the BP Gulf of Mexico Deepwater Horizon oil spill incident in 2010. This influenced its development of the scalars referred to above. The Bank said that whilst the Deepwater Horizon scheme was a different set of circumstances, and within a different industry context, it had developed the concept of a "risk transfer

premium", which provided a useful reference point for the Bank's ultimate development of the scaling factors to reflect the nature of the "exceptional and individual circumstances related to IAR."

13.32. The Bank further explained that in an early "prototype" version of the D&I matrix, it applied a "payment per point" rate of £10,000, with 1 point scoring £10,000, 2 points £20,000 and 3 points £30,000. The result was that across 16 assessment points, the maximum award would be £480,000.

13.33. The Bank said that it considered this to be too low "when reflecting on [its] aim that D&I offers would be generously calibrated in recognition of the circumstances related to IAR." It therefore further developed the scoring system which included the application of scalars just described.

13.34. In addition, as explained in Chapter 3, the Bank introduced category 3B (higher) in July 2017. The effect was that the final version of the D&I matrix allowed a maximum award of £1,080,000 per director. The Bank described the result as a "unique and generously calibrated approach…to assessing D&I."

Uplifts and Overrides

13.35. The redress calculation provided for two distinct forms of increases from the figure that would otherwise result from the pure application of the D&I matrix:

(1) An uplift was to be applied to the matrix outcome where it was considered that there were additional aggravating factors requiring more to be awarded than the sum produced by operation of the matrix. Uplifts could be led by the independent reviewer (Professor Griggs), the Bank, or agreed. The methodology document did not provide any guidance as to when factors would be considered aggravating, or how the quantum of the uplift was to be calculated, but simply recorded that "rationales for uplifts will be documented for each instance and retained."

(2) Overrides were only relevant where the Bank had concluded that no D&I redress was due – i.e. a "no redress outcome". That decision could be "overridden" by Professor Griggs. Overrides were not, therefore, additional sums according to the D&I matrix methodology; they were simply the award of a sum in circumstances where the Bank had concluded that no payment should be made. As with uplifts, no further guidance in relation to overrides was provided, save that rationales were to be recorded in the same way as with uplifts.

13.36. In its submissions to my review, the Bank provided the following additional information concerning the manner in which the quantum of an uplift was fixed:

> "Where either the [Bank] or [Professor Griggs] determined that it was appropriate to exercise discretion to provide an uplift beyond the mechanical calculation of the D&I matrix, the uplift awarded was judgement rather than criteria based. Each case was reviewed on its own merits …

All discretionary uplifts were a matter of judgment based upon the specific circumstances of each case. Whilst this case by case approach was not easily amenable to consistency checking, the [Bank] and [Professor Griggs] did consider whether the final total award for the individual (i.e. the amount awarded through the D&I matrix plus any uplifts applied by the [Bank] and/or [Professor Griggs]) amounted to a fair and reasonable outcome set against our experience of outcomes generally across the Review and against the circumstances in which other uplifts had been applied.

All discretionary uplifts applied by the [the Bank] were considered and approved/challenged by [Professor Griggs] as part of his approval of the overall outcome for the individual."

Evidential and causation thresholds applied

13.37. In relation to category 3B, the guidance provided in the methodology stated that "[t]he evidential bar…is intentionally low – allegations or testimony provided will generally be accepted unless there is clear reason not to." The Bank emphasised to me that the Customer Review applied this low evidential standard when assessing D&I generally (the "D&I evidential threshold"). In contrast to the standards applied for D&C redress (the "D&C evidential threshold"),[56] for the purposes of D&I the customer's statement of distress and suffering was to be accepted, unless expressly contradicted by the Bank's files.

13.38. Similarly, whilst causation was necessary, it did not need to be proved to legal standards. As the methodology put it:

"The Distress and Inconvenience payment is offered to recognise the personal impact that an individual may have experienced as a consequence of their interactions with HBOS Impaired Assets Office Reading."

13.39. Moreover, what was required to be established was not fraud on the part of IAR but merely "interactions with" IAR.

13.40. In its submissions to my review, the Bank explained the position as follows:

"While the Review applies established legal principles to the assessment of direct and consequential losses, it takes customer evidence at face value when assessing redress for distress and inconvenience, absent evidence to the contrary. This assessment was designed to provide an understanding of the engagement and interaction the individual had with convicted former HBOS employees within IAR and/or QCS.

In order to reach a fair outcome on the extent of the D&I compensation offers that the [Bank] and [Professor Griggs] considered should be awarded, the [Bank] agreed with [Professor Griggs] that these payments should be heavily based on the customer's own account of their experiences. When assessing a case it was important to maintain a credible balance between the customer's account of events (their interpretation of the fact pattern, claims for loss and personal impact testimony) and the [Bank's] assessment

[56] See Chapter 12.

of the fact pattern based on the case file documentation. The default position agreed [by Professor Griggs] was that the customer's account of events should be accepted unless there was express evidence to the contrary in considering D&I. In that regard, [Professor Griggs'] independent assessment also acted as a safeguard to ensure a fair outcome was achieved for each case."

13.41. This approach is very different to the approach taken in D&C assessments, which I have explained in Chapter 12. In summary, when assessing claims for D&C loss, the Bank required the customer's version of events to be supported by the documentation.

13.42. So far as I am aware, the difference in evidential thresholds was not communicated to customers. In its submissions to my review, the Bank commented that:

"The [Customer] Review was transparent in that claims for financial loss were assessed against established legal principles. For D&I, where differing views existed between bank and customer, in the absence of express documentation from the bank, the customer's view was accepted by [Professor Griggs]."

13.43. As far as I can see, the Bank did not make it clear to customers that a different evidential threshold would be applied to the D&I assessment, nor what the extent and nature of the differences in the evidential thresholds were.

III BANK'S CALCULATION OF D&I

13.44. In light of the Bank's methodology and matrix, which I have just described, the first issue is how the Bank applied them in practice.

Awards in sample cases

13.45. In respect of the 21 customers associated with 16 businesses forming part of our sample population, the Bank issued outcomes to 20 customers, totalling £11.25 million in respect of D&I. One customer received a nil outcome.

13.46. A total of 10 uplifts were applied to the Bank's initial redress offer, totalling £8.6m. Of these, eight were awarded by Professor Griggs and two by the Bank. Further uplifts were additionally awarded in five instances, three awarded by the Bank and two by Professor Griggs. That totalled £3.6 million.

13.47. In all, that was a total of £23.4 million awarded to customers for D&I in the sample cases.

13.48. The median award for D&I in the sample cases was £525,000. Not all customers chose to accept the outcome issued by the Bank.

Accuracy of the Bank's own calculations

13.49. There is the further issue of accuracy in each assessor's calculation. There is little to quarrel with in this regard. My financial advisers re-performed the D&I matrix calculation for the 21 sample directors. In 95% of the cases they either agreed with the calculation, considered the difference minor, thought that the outcome was acceptable or

regarded any differences between the Bank's and their calculations to be extinguished in practice by the application of an uplift.

IV CONNECTING FACTOR: FRAUD NOT ESSENTIAL

13.50. Fraud did not have to be evident in a case for D&I compensation to be awarded; the focus was on interactions with the convicted fraudsters and the reasonableness of what they did. As I have noted already, a design principle of the conduct and legal assessment was that where the Bank suspected "fraudulent or inappropriate activity by the Bank or its employees/former employees", this would be "appropriately considered". That meant that D&I compensation was a possibility in cases of bad or aggressive banking.

13.51. Therefore in assessing D&I redress, the Bank did not limit itself to a consideration of whether there was fraudulent activity and the impact of that activity. In keeping with this approach, the D&I matrix did not require any fraud to be evident on the file. None of the questions asked whether there was any fraud. On the contrary, many of the questions focused upon the level and frequency of interaction between the individual and Lynden Scourfield/Mark Dobson/QCS.

13.52. Similarly, the guidance provided in the Bank's methodology document also emphasised that a key part of the assessment was a consideration of how reasonable or unreasonable the actions of Lynden Scourfield/Mark Dobson appeared to have been. This was relevant to determining the score for the assessment points relating to the involvement of, and interactions with, Lynden Scourfield/Mark Dobson (category 1 of the D&I matrix).[57]

13.53. "Reasonable" in this context expressly referred to the quality of the advice given and decisions taken by Lynden Scourfield or Mark Dobson. Furthermore, when applied to questions relating to the interactions between the business and Lynden Scourfield/Mark Dobson, it necessarily concerned the impact of such advice given to or the decisions made concerning the business on the individual.

13.54. In its submissions to my review, the Bank emphasised the focus of the assessment on reasonableness. It stated that:

> "It was important that the reasonableness of actions taken or recommended by IAR and/or QCS was considered in the context of usual corporate turnaround activities, to quickly identify any unfair or potentially unlawful treatment that ultimately may have led to detriment or losses being incurred. The methodology was also designed to ensure that the [Bank] did not 'walk past' or overlook any areas of concern that were identified during the course of any assessment even if not linked to the pattern of criminal behaviour or to allegations made by the customers."

[57] For example, the guidance for questions which relate to the amount of interaction with Lynden Scourfield/Mark Dobson explains that: "In scoring this question the following points will be considered for the period of time during which the Individual was a director: [i] If the interactions/decisions were limited, infrequent, caused no detriment or considered reasonable, a score of '1' may be awarded; [ii] If the interactions / decisions were of medium impact or caused limited detriment a score of "2" may be awarded. A "2" may also be awarded where the level of impact is unknown but there was an ongoing interaction with Lynden Scourfield/Mark Dobson; [iii] If the interactions / decisions were frequent, may have been significant in impact, may have caused severe detriment or deemed unreasonable, a score of "3" may be awarded."

13.55. Therefore, the Bank offered D&I awards in cases where there was what I have called aggressive or bad banking. This is what the methodology called "inappropriate" or "unreasonable" banking, and in legal terms might be negligent banking or banking in breach of contractual or regulatory terms. Indeed the Bank's concept of inappropriate or unreasonable banking was likely broader than this.

13.56. The extension of the D&I matrix to non-fraudulent behaviour may at first blush seem to be a good thing. However, it had a number of significant consequences. Most obviously, it ran contrary to what the Customer Review was publicly set up to do; namely, to compensate the victims for the effects of the IAR fraud.

13.57. As soon as compensation (of any kind, whether D&I or D&C loss) starts being given for negligent, aggressive or bad banking, without the need for the recipient to have been the victim of any fraud, it brings into question the basis for confining the Customer Review to the actions of those individuals who were convicted of fraud, and for confining the claimants to those individuals who were managed by the convicted fraudsters. What distinguishes their negligent, aggressive or bad banking from the negligent, aggressive or bad banking of other bankers?

13.58. This overarching issue had various consequential impacts on the procedural and substantive coherence of the Customer Review: (i) it was contrary to what customers were told; (ii) it was inconsistent with the definition of the review population; (iii) it was inconsistent with the D&C redress scheme, and was another reason for customer confusion; and (iv) it produced anomalous results.

Contrary to what customers told

13.59. First, this approach ran counter to what customers were told. In all the scripts in our sample cases for outcome meetings, when there was one, the following wording appeared, subject to small variations.

> "In general terms when we undertake these reviews we are seeking to identify and provide remediation for clients where criminality may have occurred either with officials at [IAR] or with QCS - that is the primary focus of the review. What we are not undertaking is to compensate clients or their businesses for losses or business failure that may have occurred in the ordinary course of events unless criminality is evident. The review is not a critique of historic lending or the terms of that lending - I stress the review is focussed upon the interaction and impact of those interactions with Lynden Scourfield and Mark Dobson at [IAR] and with David Mills and others from QCS if indeed these took place."

13.60. In circumstances where, as I have explained above, the Bank offered D&I awards where there was no criminality evident, this was not an accurate statement.

13.61. Unsurprisingly, as a result, many customers assumed that a significant D&I redress payment indicated that the Bank accepted their account of fraudulent behaviour, when that was not the case.

Inconsistency with eligibility requirements for review

13.62. Second, the eligibility threshold for inclusion in the Customer Review focused on the involvement of the fraudsters on the file, because they had been convicted of committing the IAR fraud on the Bank and its customers. In its submissions to me the Bank explained that:

> "Cohort 1 captured those clients that had the same connectivity as required for *the existence of the criminal conspiracy evidenced at trial.* The [Bank] added Cohort 2 on the basis that any contact with QCS was considered to be a potential indicator of detriment, regardless of direct involvement of the convicted former HBOS employees, *given the criminal findings against the principals of QCS[…].*
>
> The [Bank] additionally created Cohort 3 [because]…. There was no single 'golden source' that definitely confirmed all connections referred to QCS or that were managed by the *convicted ex HBOS employees* at the time[…]
>
> the [Bank]'s objective was *to compensate individuals personally impacted by the criminal events*" (emphasis supplied)

13.63. When it came to the application of the D&I matrix, the lack of requirement for fraud meant that some customers who entered the Customer Review "gateway" because of the involvement on their file of the convicted bankers then obtained compensation for the impact of merely bad or aggressive banking.

13.64. There is no objection in my view to compensating customers for D&I in cases of merely bad or aggressive banking per se. There is, however, a difficulty with doing so within a Customer Review that was ostensibly put in place to compensate the effects of a particular, identified, fraud. If there is no connection at all between the IAR fraud and the compensation, the requirement of involvement on the file of a fraudster as the threshold for inclusion in the Customer Review is not logical.

13.65. Thus in one case, Lynden Scourfield had a telephone call with the customer, and thereafter arranged for a contact of his to conduct a business review, on the basis of which the IAR department proceeded to subject the customer to extremely aggressive management. The initial involvement of Lynden Scourfield in that chain was sufficient to bring that customer into the Customer Review. The customer ultimately received a D&I redress payment of over £1 million as a result of the aggressive management of the file by IAR. There was, however, no finding of fraud on the file. Whilst it is not necessarily unfair for that customer to have received that compensation per se, the difficulty is that the only reason the customer was in the Customer Review was because of the involvement of a fraudster (Lynden Scourfield), not because of the bad/aggressive banking services that he had received. Having entered the Customer Review through a gateway designed to identify those most likely to have been impacted by the IAR fraud, the customer obtained redress despite not having been a victim. In contrast, other customers who alleged that they had been the victim of bad/aggressive banking, but who did not make it through a fraudster related gateway into the Customer Review, were

excluded and their allegations of bad/aggressive banking by IAR received no consideration.

Confusion over treatment of D&C loss resulting from bad banking

13.66. As I noted in Chapter 12, the Bank's D&C assessment was limited to claims for D&C loss resulting from the fraud. It did not extend to claims for D&C loss which the Bank concluded had not been caused by the IAR fraud, but were merely the result of aggressive or bad banking. The extension of the D&I redress scheme to cover the consequences of bad/aggressive banking, but not the D&C assessment, therefore created an inconsistency between these two regimes.

13.67. It also resulted in difficulties within the D&I assessment. Once the Bank had decided to review bad and aggressive banking as part of the D&I assessment, there was a question as to how financial losses consequent on it would be dealt with. Should they be considered at all? If so, which evidential threshold should be applied?

13.68. In practice, where bad and aggressive banking was analysed under the D&I matrix, the Bank appears to have considered not only its personal impact but also its financial impact, which would have (if it had been eligible for consideration in the D&C part of the Customer Review) represented potential D&C loss.

13.69. However, the Bank appears to have applied different evidential thresholds to each category of impact: it maintained the D&I evidential threshold when evaluating the personal impact of the bad or aggressive banking, but imported the D&C evidential threshold for the purposes of considering the financial impact.

13.70. Within the D&C part of the Customer Review, the application of the D&C evidential threshold resulted in a zero rate of redress for claims for D&C loss alleged to have been caused by the IAR fraud. The same outcome appears to have resulted in the context of evaluation (within the D&I methodology) of D&C loss for bad or aggressive behaviour – although it appears that in some cases the level of D&I redress was increased by an uplift to an amount which came close to the amount claimed for D&C loss.

13.71. Two sample cases illustrate the point:

(1) In the first case, once the Bank had accepted that the account had been handled badly, any contentions by the director which were in effect D&C loss claims consequent on the bad and aggressive banking – such as his claim for loss of income following the forced sale of income producing assets – were subjected to the D&C evidential threshold and causation requirements. The customer's claim for this financial loss was rejected as failing to meet the D&C evidential threshold and causation requirements. Instead he was awarded a sum in excess of £1 million for D&I by way of uplifts applied by Professor Griggs and the Bank.

(2) In the second case, the Bank concluded that there had been no fraud on the file. Nonetheless, various of the directors were awarded significant D&I redress because they had interactions with Mark Dobson. The Bank accepted that the latter's behaviour may have been bullying and unpleasant. The D&I evidential

threshold was applied and the directors were compensated for the personal impact of his behaviour. However, the financial impact of his actions (which two directors argued had caused the failure of the company) was evaluated by applying the D&C evidential threshold and causation requirements. The upshot was that that contention failed.

13.72. The additional points raised by these examples are consistency and transparency. I do not consider that it was either consistent or transparent to consider D&C loss arising out of bad banking behaviour as part of the D&I redress, whilst refusing to do so under the D&C methodology.

13.73. It simply created confusion, and again lacked transparency, to bring in the D&C evidential threshold to certain parts of the D&I assessment. If bad or aggressive banking was to be considered within the Customer Review, it should have been considered across both the D&I redress scheme and the D&C loss assessment as appropriate. The differing evidential thresholds that would be applied, and what was expected of the customers, should also have been clearly communicated.

Anomalous results

13.74. The fact that no fraudulent behaviour was required for D&I redress, and that the D&I matrix focused on the interaction between the fraudsters and customers, meant that even where the Bank had concluded that there was no fraud a director could potentially achieve higher D&I redress than cases where there were markers of the fraudulent conduct.

13.75. Indeed, as the D&I matrix included questions that focused mechanically on factors such as how many meetings the customer had with any of the convicted individuals or QCS, the result was that a customer could even score under the D&I matrix (albeit at the lower end of the scale) where there was not even any indication of bad, aggressive or inappropriate behaviour.

13.76. These outcomes are counter-intuitive for a review put in place to compensate for the effects of fraudulent behaviour.

V EVIDENTIAL THRESHOLDS AND CAUSATION

13.77. The application of different evidential thresholds and causation requirements as between the D&C methodology and the D&I methodology has been touched on earlier. It gives rise to two issues. First, there was confusion in the Customer Review as to what was expected from the customer by way of evidence, submissions and proof to obtain a D&I award because of the Bank's policy of non-disclosure of its methodology. Secondly, D&I redress was offered for the consequences of matters for which the Bank had expressly disclaimed causative responsibility following its D&C analysis.

Customer confusion

13.78. The application of differing evidential thresholds obfuscated the question of what was expected of the customer by way of evidence, submissions and proof. In particular, customers told me that it was emphasised to them that the Customer Review was not a legal

review, and that they should therefore not put in legal submissions. Yet for D&C loss, legal submissions and documentary evidence were in practice what the Bank required, whilst for D&I redress, they were not.

13.79. It is impossible to measure the impact, in particular, of the failure properly and transparently to communicate to customers the differing approaches and evidential thresholds being applied as between the D&C analysis and the D&I analysis.

13.80. It is likely, however, that customers would have produced different submissions and evidence in respect of loss had they been aware of the differing evidential thresholds. It is also likely that more customers would have pressed the Bank to reimburse them for the costs of expert financial advice which, as we have seen, the Bank generally resisted. It is also likely that customers' submissions both legal and evidential would have been better focused so as to meet the standards being applied. Had the Bank been more transparent about its requirements, it would likely have had a material impact on the evidence presented to it for consideration of a claim.

Relationship with D&C

13.81. Whilst some D&I was recognised as having been caused directly by the bullying, unpleasant and unreasonable behaviour of Lynden Scourfield, Mark Dobson and QCS, in some cases it was consequent upon the financial impact of their decision-making and handling of the customer's business.

13.82. For example, in one sample case the uplift applied by Professor Griggs to the D&I redress payment included recognising the D&I suffered by the customer as a result of not being able to have their spouse at home following an operation. That D&I, however, resulted from the director being unable to afford to heat the property as a result of financial difficulties, which the director contended were the direct result of mishandling of their business' account by Lynden Scourfield and IAR.

13.83. The D&I payment therefore tacitly accepted that the Bank must bear some responsibility for the director's impecuniosity, in circumstances where the D&C loss assessment had expressly rejected the Bank's responsibility for it, and had refused to award compensation for D&C loss on that basis.

13.84. In another case, the director received D&I redress payments to reflect the fact that the director's own funds had been injected into a business venture as a result of misrepresentations made by Lynden Scourfield and QCS, in circumstances where the Bank had concluded, in its D&C loss analysis, that the fraud had not caused such loss.

13.85. This is more than simply not requiring the customer to have proved the causative link between the actions of the criminals and the D&I suffered. It is assuming a causative link in circumstances where the Bank had already expressly rejected the argument that any actions of the criminals (whether fraudulent or otherwise) caused the D&C loss from which the D&I stemmed.

13.86. The point is, again, the inconsistency: compensation was awarded for D&I caused by mistreatment, when legal responsibility for that mistreatment had been rejected. It is

precisely to avoid such irreconcilable results that, in accordance with well-established legal principles, culpability for physical or financial damage is required in order to found any claim for D&I that flows from it.

VI D&I UPLIFTS AND OVERRIDES

13.87. As noted previously, redress under the D&I methodology could be further increased, by either the Bank or Professor Griggs, through uplifts. (Professor Griggs did not exercise the override power in any of the sample cases we reviewed i.e. where the Bank awarded no redress.) However, no similar provision for uplifts was included within the D&C assessment methodology.

13.88. This may explain why, in some sample cases where he disagreed with the Bank's D&C analysis, Professor Griggs requested an uplift in respect of the D&I redress payment in order to increase the sum awarded to the customer. I have discussed two such cases in greater detail in Chapter 12.

13.89. In brief, in the first case, a number of uplifts were applied which resulted in the customer's final D&I award being more than double the initial award. In the second case, substantial uplifts were applied to the redress offers of the two directors, with the uplifts calculated by reference to the estimated value of their shareholdings and lost earnings.

13.90. In the two sample cases noted above, Professor Griggs clearly believed that there was a viable case for D&C loss, but in both cases the Bank resisted characterising any part of the redress as compensation for D&C loss. As I have noted earlier, the impression from the correspondence is that the Bank persuaded Professor Griggs to reclassify the redress as a D&I uplift payment, by finding other "aggravating factors" to justify the characterising of the compensation as D&I redress, and ensuring that it was thereafter expressly recorded in writing that Professor Griggs did not think that there was a claim for D&C loss.[58] The result was that Professor Griggs exercised his uplift powers to increase the D&I redress offer, outside the D&I matrix sums, and by way of sizeable additional sums.

13.91. In a third sample case, the uplift figure was utilised as a vehicle through which to refund a director sums injected into the company, but which the Bank had concluded it would not compensate as direct loss. It is notable that, in another sample case, the Bank similarly concluded that it would not award redress for direct loss in respect of sums injected by the customer, but instead repaid them by way of a "voluntary payment", classified as neither D&C nor D&I redress.

13.92. In Chapter 12, I noted that both Professor Griggs and the Bank provided the following explanation to my review:

> "The [Customer] Review's approach to direct and consequential loss was to follow accepted legal principles. Both [Professor Griggs] and [the Bank] followed that approach during the review. In a very small number of cases, [Professor Griggs] and his team reached the view that there was a plausible case for financial loss. While in

[58] See Chapter 12, paragraphs 12.145ff.

those cases [Professor Griggs] and his team did not conclude that the alleged losses would be recoverable when applying the legal principles, [Professor Griggs] sought (and [the Bank]agreed) an increase in compensation to reflect his view that the impact on participants was aggravated by that plausible case, based on what he believed to be fair and reasonable."

13.93. On the basis of this explanation, it seems that the lower D&I evidential threshold was employed as a vehicle through which to offer redress for D&C loss that had failed to meet the D&C evidential threshold. The differing evidential thresholds do not, however, provide a justification: the utilisation of redress for D&I to make payments that were really for D&C losses, so as to take advantage of a differing evidential standard, is not logically or procedurally defensible.

13.94. I have already said that the outcome undermines the substantive and procedural integrity of the Customer Review. Because D&C loss payments were characterised as D&I payments, customers misunderstood the basis on which the Bank was compensating them and they were deprived of the opportunity to challenge the quantification of the financial loss.

Circumstances triggering uplift

13.95. Further issues arise from the approach as to what prompted consideration of an uplift. Overall, my impression is that those who were most forceful obtained the greatest uplifts. This included, in particular, by way of one or more of:

(i) having legal representation, particularly where the lawyers represented more than one customer. It appears that those lawyers discerned, as the process progressed, the key triggers in the undisclosed methodology that would increase payments, enabling their clients to direct their evidence to those matters;

(ii) obtaining a direct meeting or call with the Bank's accountable executive for the Customer Review. This was not provided for within the methodology. I asked the Bank for further information about these meetings or calls. It indicated that of 14 individuals (across nine businesses) who secured a direct audience or call with the Bank's accountable executive, five individuals obtained at least one increase in uplift/redress;

(iii) engaging in direct communication with Professor Griggs;

(iv) threatening to go to the media; and

(v) assistance from the SME Alliance.

Quantification of uplifts

13.96. As noted earlier, in its submissions to my review the Bank explained that the uplifts were "a matter of judgment based upon the specific circumstances of each case" which the Bank and/or Professor Griggs considered "amounted to a fair and reasonable outcome".

13.97. It seems from this explanation that the quantum of any uplift was a subjective matter. The Bank acknowledged that the consequence of this was that the approach "was not easily amenable to consistency checking." It is also not possible to identify the criteria by which the payments were considered to be fair and reasonable. It appears that the baseline requirement was that the customer had provided new information which could be relied on as justifying the uplift. In response to an email from an official of the Bank proposing uplifts in respect of two directors, Professor Griggs noted:

> "My main concern (as I know you are also very conscious of) is to ensure the integrity of the Review, so provided what you learned was new information/colour/detail about the [two] cases (or, I suppose, new to you) then I am happy for it to be treated as further [additional information] which would justify a re-assessment (upwards) of D&I within the parameters of the Review methodology."

13.98. In one sample case, the Bank emphasised that the decision to award an uplift to the D&I payment was solely based on the level of personal impact and distress asserted by the customer, following further reflection on the file by Professor Griggs. Notwithstanding that contention, the uplift was applied shortly after the customer's solicitors had responded with a final settlement offer following the Bank's decision that additional information submitted by the customer would not change the outcome. The additional uplift produced a revised redress offer which was almost identical to the settlement figure which the customer had proposed. The correspondence between Professor Griggs and the Bank also shows that Professor Griggs took into account the "litigation risk" which the Bank faced in respect of the case.

13.99. Similar considerations were noted in other sample cases. For example, in one case, Professor Griggs urged an increase to the redress offer, explaining that:

> "While I had always thought that [the customer] would not pursue their case through the courts that seems to have changed […]. They also are clever and do have I believe information from the time of the fraud that will not only help their case but also show that the bank knew about [Lynden Scourfield's] fraud and defended it rather than sorting it out. I do not think they are bluffing […]. My view is also that you will never let them bring this to court due to both the PR and I think Regulator impact this might have. Therefore if you know you are going to settle why not do it now and come to a friendly settlement rather than one later that aggravates them even more and after they may have been evicted from their house."

13.100. In another case, following a meeting with the customer, an official of the Bank informed the Bank's Customer Review team that:

> "I quickly moved [them] onto 'what will it take' – again a bit of range finding but in the end [they] said [they] will settle for another £[XXX]. […] At this level I indicated that we could get there. I explained that I would need to re-consider the structure of the offer as we still assigned no value to [their] direct/consequential loss claims"

13.101. It is therefore seems that the D&I uplift was also used, on occasion, as a vehicle through which payments could be increased to secure a settlement.

VII D&I REDRESS: RELEVANT PERIOD

13.102. The methodology stated that D&I focused on the individual's experience during the time the business was in IAR. In practice, however, it appears that the Bank factored in matters occurring after the customer's time in IAR, the length of time taken to achieve redress, and even delay in the conduct of the Customer Review itself, as the basis for increasing the D&I award.

13.103. Thus, for example, the considerations under category 3B/higher (Exceptional distress suffered by impacted party) were stated to include the following:

> "Were they persistently rebuffed in their pursuit of justice over many years?/ Were they subject to public disclosure through the trial? / Is there other evidence that [sic] exceptional distress being suffered? For example, where the relevant individual was also involved with extensive media coverage surrounding their particular circumstances and / or the trial."

13.104. The methodology expressly included taking into account the impact of events after the business' involvement in IAR, the treatment that customers had received from the Bank, and any impact on them as a result of the trial, rather than simply the impact on them of their experience in IAR. Six sample directors received an award under Category 3B/higher as a result of their participation in the criminal trial.

13.105. In one sample case, personal events up until the final award contributed to the decision to increase the customers' redress payments.

VIII CONCLUSIONS

13.106. The D&I methodology was designed to provide generous payments. It is, on any view, more generous in terms of quantum than court awards for D&I, and with a low evidential requirement for causation that was favourable to the customer. For that reason the Bank is to be commended.

13.107. Nonetheless, I have come to the conclusion that the D&I methodology was flawed.

13.108. My reasons for this conclusion are, first, that the D&I methodology and matrix failed to give weight to a key factor, whether fraud was evidenced on the file. Assessing, instead, interactions with IAR and/or QCS, and what was characterised as the reasonableness of the actions taken or recommended by them, was inconsistent with the stated aim of the Customer Review, what customers were told and the D&C methodology. Given that D&I payments were intended to compensate customers for the impact of fraud, this was a flaw in the design of the D&I methodology and matrix.

13.109. Secondly, by focusing mechanically on the interactions between customers and IAR and/or QCS, the D&I matrix produced anomalous results, including substantial D&I redress payments to directors who were not impacted by the IAR fraud.

13.110. Thirdly, the Bank failed to communicate adequately the differing approaches to D&I and D&C, in particular the evidential and causation thresholds. That, as I have

explained, meant that customers did not always advance their best case. To an extent, customers were actively discouraged from doing this by being told that, as this was not a legal process, submissions should not be legally focussed. If they were not told how the D&I matrix worked, they could not know how to pitch the best case for D&I compensation.

13.111. Fourthly, there was the arbitrariness of the uplift system. In a number of cases, D&I awards were used as a vehicle for effectively compensating for D&C loss without the Bank disclosing this fact. Perhaps unsurprisingly, customers interpreted high uplifts as an acknowledgment of fraud on their file, yet might still regard the sum offered as an underestimate of the true D&C loss that they believed they have suffered.

13.112. I return to my view of the D&I methodology in Chapter 15.

CHAPTER 14 SETTLEMENT AGREEMENTS

I BACKGROUND

14.1. In Chapter 6 I set out the Bank's explanation to me that anyone who wished to accept an offer of compensation (with the exception of those shareholders receiving £2,000 or less as repaid QCS fees) was required to enter into a settlement agreement with the Bank before doing so.

14.2. The importance of settlements within the Customer Review was that they were the mechanism by which the Bank sought to bring closure to the IAR fraud. As I discuss in more detail below, once a settlement agreement had been signed, the customer could no longer make complaints or bring any claims in relation to any wrongdoing at IAR or in relation to the Customer Review. However, there has been widespread dissatisfaction with having to sign the Bank's settlement agreements and they have become a focal point for customers' complaints about what they regarded as the "take or leave it" approach of the Bank.

Terms of Reference and assessing Bank's approach

14.3. My Terms of Reference specifically require me to look at the Bank's approach to settlement agreements, in particular the requirement to take legal advice before signing, and "whether the terms and conditions included within the Settlement Agreements were fair and reasonable".

14.4. At the outset I commend the Bank for funding customers so that they obtained legal advice before they signed a settlement agreement. This is in accordance with best practice in banking; it is in line with what the courts require in other areas where those lacking bargaining power enter contracts with banks.[59]

14.5. To assess whether the terms and conditions included within the settlement agreements were fair and reasonable, what my legal team did was to review the settlements entered into by 15 of the 21 sample directors. In five of the six remaining sample cases, the customer did not accept an offer of redress and therefore did not execute a settlement. In the final sample case the settlement was court approved and so there was no reason for me to review it.

14.6. The Bank also supplied me with copies of the settlement agreements entered into by the other individuals related to the sample businesses. In light of the importance of the settlement agreements to both customers and the Bank, my legal team have reviewed these as well.

14.7. So this means that we have reviewed in total approximately 60 settlement agreements. This review informs the conclusions at the end of the chapter.

[59] e.g., those giving personal guarantees/mortgages over a jointly owned home for a domestic partner's business debts: *Royal Bank of Scotland Plc v Etridge (No 2)* [2002] 2 AC 773.

II THEMES ARISING FROM BANK'S/CUSTOMERS' SUBMISSIONS

14.8. The Bank told me that the "broad principles underlying the settlement agreements" were:

> "To provide certainty of outcome and closure for both participants in the Review and the [Bank] in circumstances where participants have chosen to accept a settlement offer;
>
> To ensure that confidentiality was maintained in respect of the terms of the settlement agreement and the discussions and negotiations leading up to the agreement; and
>
> It was an express condition that all participants were required to take independent legal advice on the settlement agreement, paid for by the [Bank], prior to entering into the agreement."

14.9. In Chapter 8 I referred to some of the comments I received from customers about the settlement agreements, which potentially touch on their fairness and reasonableness. In summary, the principal complaints were that:

(1) the Bank refused variations to the settlement agreements which customers proposed, and inserted bespoke terms for some customers that were particularly onerous;

(2) the "release" clause in clause 2.1 (which defined the claims that customers would be settling when they executed the agreement) was too broad;

(3) the "non-assistance" provisions in clauses 2.2 and 2.3 prevented customers from assisting and/or obtaining assistance from their fellow co-directors in any action against the Bank; and

(4) the confidentiality clauses were too strict.

14.10. In addition to these four points, there are two other issues which are also relevant to the fairness and reasonableness of the settlement agreements. First, the settlement agreements included wide-ranging "exclusion clauses" which effectively prevented customers from bringing claims against the Bank in relation to statements made by the Bank and assurances given by it in the course of the Customer Review; and, secondly, the Bank required shareholders who had not participated in the Customer Review, but were refunded QCS fees in an amount of £2,000 or more, to sign settlement agreements.

14.11. So let me consider these six issues in turn.

III SELECT COMMITTEE TERMS VS TERMS USED

14.12. Several customers told me that the Bank had included additional, bespoke terms in their settlement agreements. What they had done was to compare their terms with the sample settlement agreement which had been published on the Treasury Select Committee website on 5 July 2018. They considered their terms to be oppressive and thought the Bank had inserted them to create a particularly harsh settlement in their individual cases.

14.13. Let me explain what happened.

Sample settlement agreement on the Treasury Select Committee website

14.14. We saw in Chapter 5 that the Rt Hon Nicky Morgan MP wrote to Professor Griggs on 26 June 2018 on behalf of the Treasury Select Committee. She asked specifically about settlement agreements which customers reportedly had signed, and their "undertakings regarding disclosure".

14.15. In his reply of 28 June, Professor Griggs reported that, at the date of writing, the Bank had offered compensation to 90 per cent of the businesses in the Customer Review and 80 per cent had accepted and settled. He said:

> "I have attached a sample of a settlement agreement that the Bank enters into with a customer when agreement is reached on the outcome. You will see that (as queried) there are standard confidentiality provisions, as would be expected in a legally binding settlement agreement."

14.16. That sample settlement agreement had been provided to Professor Griggs by the Bank, for the purpose of sending it to the Rt Hon Nicky Morgan MP.

14.17. In my view it was implicit in Professor Griggs' letter that the attached sample agreement was representative of the settlement terms upon which the Bank had offered redress in the Customer Review, and/or upon which 80 per cent of the businesses in the Customer Review had in fact settled.

14.18. In fact, what I will call the "Select Committee template" which Professor Griggs sent to the Rt Hon Nicky Morgan MP was not widely used. My legal team reviewed approximately 60 executed settlement agreements. Only three were based on the Select Committee template. The Bank has told me that it was sent to 18 customers (from the Customer Review population of 191) who signed settlement agreements.

14.19. The remainder were all based on other templates which the Bank supplied to me as part of the materials for my broader review of the Bank's methodology (what I call "the other templates"). These other templates have not been made public by the Bank.

The other templates

14.20. The Bank has told me that there were four templates in all.

(i) The first, version 1, was the Select Committee template.

(ii) Version 2 was in use from approximately September 2017 and sent to 27 customers who signed the settlement agreement. Among other things, it released claims arising out of or in connection with "Operation Hornet" in the release clause. Clause 2.2 was amended and clause 2.3 introduced.

(iii) Version 3 was in use from approximately October 2017 and was sent to 94 customers. For present purposes there were no material changes from version 2.

(iv) Version 4 was introduced from November 2018 and sent to 9 customers. It stated that "for the avoidance of doubt" the customer was not prevented from "assisting

or responding to" the Dobbs Review, Parliament, HMRC, law enforcement agencies and regulatory authorities.

Differences between the templates

14.21. There are important disparities between the terms of the Select Committee template and the other templates. In summary, the provisions of the other templates were more onerous, principally in the following ways.

14.22. Most importantly, the other templates contained an additional non-assistance clause, which prevented the customer from voluntarily assisting the relevant company and its associates in any action against the Bank in any jurisdiction. It also had the effect of imposing disclosure restrictions on customers. This clause caused difficulties for a number of customers. I return later to the issue in relation to the confidentiality obligations imposed by the settlements.

14.23. Secondly, the covenant not to sue in the other templates was wider than the Select Committee template because (a) they contained non-assistance wording consequent upon the non-assistance clause (a repetition of the agreement in the non-assistance clause not to voluntarily aid or cause any action against the Bank); and (b) they referred to "any action, complaint, suit or other proceeding" (rather than "proceedings" as in the Select Committee template).

14.24. Thirdly, the other templates contained a term preventing the restoration of the company if it had been dissolved.

Why were different templates used?

14.25. The Bank provided me with their methodology. It did not mandate the use of a particular settlement template.

14.26. I can well understand the Bank's approach of using a standard template when it was dealing with dozens of disputes arising out of a common factual background. It is also normal for settlement agreements to be formalised in a contract. Given the Bank's resources, and the fact that the Customer Review, which led to redress offers, was the Bank's own process, it was reasonable for the Bank to assume the burden of drafting these contracts. In the circumstances, it would have been surprising if the Bank had drafted and negotiated bespoke settlements with each customer.

14.27. However, the Bank's methodology does not acknowledge the existence of the different templates, nor does it explain the use of different templates for different customers.

Consequences of publication of the Select Committee template

14.28. The publication of the little-used Select Committee template and not the other templates caused high-profile criticism of the Bank that might otherwise have been avoided. In the debate in the House of Commons on 18 December 2018, Mr Kevin Hollinrake MP drew attention to the different agreements as part of his criticism of the Bank. Clearly, it caused concern and mistrust.

14.29. It also led to confusion and bad feeling among customers about what they suspected was the insertion of bespoke terms in their agreements. In one case the Select Committee template was published after the customers had received their draft settlements (which were based on one of the other templates) but before they signed. They sought amendments to their draft settlements but the Bank refused. This led them to believe (incorrectly) that the Bank had inserted a bespoke term into their settlements.

14.30. The Bank's failure to disclose the other templates undoubtedly caused confusion and increased customers' mistrust in the Customer Review process. If there had been greater transparency on the part of the Bank as to the actual standard terms that it used, this confusion could have been avoided.

Differences between agreements based on the same template

14.31. There were no major variations in the three executed settlement agreements we examined which were based on the Select Committee template.

14.32. There were only limited variations in the terms of those settlements based on the other templates. Mostly those were variations in the recitals (i.e. the introductory paragraphs to the agreements) which personalised the agreement by reciting the specific background. In my view such variations were appropriate in order to set out relevant background.

14.33. In a number of cases, a customer had died and the settlement agreement was between the Bank and the executors of the customer's estate. This meant that there were additional recitals and provisions. Again these were unobjectionable and appropriate.

Variations proposed by customers

14.34. I saw five cases where customers were successful in obtaining amendments to settlement terms. Four of these were amendments to the confidentiality clauses and reflected the carve out wording which later came to be included in Version 4 of the template settlement agreement.

14.35. Perhaps I could note that the Bank wrote to the Dobbs Review on 6 November 2018 confirming that it did not consider that the confidentiality clauses prevented customers from assisting it. Nonetheless, that is not immediately obvious on the face of the template clause. The carve out made that clear.

14.36. The fifth agreement contained a waiver of a previous confidentiality agreement, which had been entered into in relation to an earlier settlement (which was also waived). In this latter instance, there was a conversation between the customer and the Bank about what it would take to settle after the initial offer of redress. According to the customer, the Bank had for years resisted releasing the customer from the prior confidentiality agreement, including to permit the individual to assist the police in Operation Hornet. The police ultimately obtained an order from the court permitting him to assist. The confidentiality agreement had also prevented the customer from speaking publicly about the fraud and to clear his name. The new settlement agreement did contain new confidentiality provisions which (as I explain below) may mean the concession did not

make much difference. Nonetheless, the Bank's conduct in relation to this customer was an exception to its usual stance.

14.37. By contrast, two other customers gave me copies of correspondence with the Bank in which they asserted that the Bank itself had invited them to propose amended wording on particular points. The lawyers acting for the customers had therefore sought the amendments in sustained correspondence over many months. Ultimately, the Bank refused to accede to any of their proposed amendments.

IV BREADTH OF THE RELEASE CLAUSES

Clause 2.1 – main release clause

14.38. Clause 2.1 in both the Select Committee template and the other templates set out the claims that customers forfeited by signing the settlements. It was comprehensively drafted. Customers complained to me that the settlement agreements barred them from seeking redress in relation to matters that had never been within the scope of the Customer Review, as well as in relation to the Customer Review itself. Clause 2.1 in each template was very similar, except that the Select Committee template did not refer to Operation Hornet, whereas the other templates did.

14.39. I will therefore focus on clause 2.1 in the other templates (which I call "the main release clause"). Since I will be referring to it at some length, it is helpful to set it out in full:

> "[Party A] hereby releases and agrees that the Review Outcome Payment is in full and final settlement of any actual or potential claims or complaints (including but not limited to complaints to the Financial Ombudsman Service of whatsoever nature (including any claims for costs or interest), whether present or future and whether known or unknown and whether arising from or affected by any change in the law or any other change of circumstance of any sort, which [he/she] has or may have against the [Bank] or its Associates, including but not limited to claims or complaints based on fraud or otherwise based on allegations of dishonesty, impropriety, conspiracy, or other intentional or reckless conduct arising out of or in connection with, whether directly or indirectly, the Review [or X Limited (or its Associates)] or HBOS Reading or Operation Hornet ("the Settled Claims"). Future claims for the purposes of this Agreement includes any claims [Party A] has or subsequently obtains, including rights obtained from this parties by any means whatever including by way of an assignment, novation or subrogation."

14.40. The main release clause therefore covers actual and potential claims and complaints whatever their nature, including future and unknown ones, even if the relevant law or the facts change. It includes – but is not limited to – fraud, dishonesty, impropriety, conspiracy and intentional or reckless conduct, arising out of or in connection with the Customer Review, the company, HBOS Reading, or Operation Hornet.

14.41. The limitation on the scope of the release is the requirement of "connection". Customers remained able to bring a claim against the Bank which was unconnected to the Customer Review, the company, HBOS Reading (which the contract defined to mean IAR), or

Operation Hornet. This might, for example, be a claim in relation to a personal bank account or a product a director held with another branch or bank within the Lloyds Banking Group, if neither had come up in the Customer Review or Operation Hornet.

14.42. That is a meaningful limitation on the scope of the clause but it is narrow. It appears, for instance, that any wrongdoing by non-IAR employees would be caught by the main release clause if it related to the business, or had been raised in the Customer Review, the police investigation or the criminal trial, even if that wrongdoing had nothing to do with the IAR fraud.

The legal position

14.43. In our law there is nothing wrong with broad release clauses per se. A release clause can, for example, settle future claims or claims which do not yet exist as a matter of law, if the wording is clear enough. English law takes the view that parties who freely enter into a contract are bound by what they have agreed. In addition, the courts have stressed that the purpose of settlement agreements is to draw a line under a dispute and bring finality for all concerned.[60]

14.44. In my view the meaning and effect of the wording in the main release clause would have been clear to a customer's legal adviser. As I described earlier, the Bank commendably paid for customers to take independent legal advice prior to their agreeing to the release of claims in the settlement agreements.

14.45. Several customers complained to me that the Bank knew that they had other claims not covered by the Customer Review, either because they had told the Bank (before or during the Customer Review) about them, or in light of the Project Lord Turnbull Report. Their lawyers would have advised them that they would not be able to pursue the former by signing the settlements. As to the implications of the Project Lord Turnbull Report, I have explained elsewhere in this report that it would be wrong for me to consider its implications when it is part of the Dobbs Review.

14.46. Let me turn to the crucial issue of whether the release clauses in customers' settlements were fair and reasonable.

Was the breadth of the main release clause fair and reasonable?

14.47. Let me say at once that I appreciate the Bank's desire for finality. That was no doubt also shared by many customers. Finality is achieved by a full and final settlement. It is understandable that the Bank would have wanted to protect itself from future claims. It made sense for both parties that the settlement would draw a line underneath matters which had inflicted an emotional toll and cost over many years.

14.48. So I do not consider that it was unfair or unreasonable for the Bank to seek a release of future claims in relation to the subject matter of the Customer Review.

[60] *BCCI v Ali* [2001] UKHL 8; [2002] 1 AC 251.

14.49. However, there are other aspects of the main release clause which I consider were not fair and reasonable in the context of the Customer Review.

14.50. In particular, I consider that the scope of "settled claims" was too broad. That includes, but is not limited to, "claims or complaints based on fraud or otherwise based on allegations of dishonesty, impropriety, conspiracy, or other intentional or reckless conduct arising out of or in connection with, whether directly or indirectly, the Review [or X Limited (or its Associates)] or HBOS Reading or Operation Hornet".

14.51. The wording of the main release clause suggests that a claim with a link to the Review, the company, IAR or Operation Hornet might be barred. However, the list of claims identified in the main release clause is non-exhaustive: it is expressed as "including but not limited to" the potential claims listed in it. Therefore, it is potentially very wide in its ambit.

14.52. On a natural reading of the clause, it seems to me arguable that it would, for example, release the Bank from:

(1) claims founded on information revealed in the course of the Customer Review or Operation Hornet that set off a chain of inquiry;

(2) claims arising from the conduct of an individual who was connected to the fraudsters, but who was not convicted of fraud;

(3) claims in negligence against the Bank arising from the conduct of any employees working in IAR; and

(4) claims with a connection to the company, even if they had no connection to the Review, IAR or Operation Hornet.

14.53. A further aspect of the main release clause which makes it unduly broad is the reference to claims "whether present or future and whether known or unknown and whether arising from or affected by any change in the law or any other change of circumstance of any sort". Arguably if, for example, another individual at HBOS Reading were to be convicted in a future criminal trial, or it emerged that one of those already convicted had a previously unknown involvement with a particular company, the customer would be unable to claim or raise a complaint against the Bank.

14.54. Overall, my reading of the main release clause is that it enabled the Bank to protect itself from claims and complaints in respect of a range of wrongdoing, whilst only requiring it to compensate customers for claims arising from a narrower set of facts.

Clauses 2.2 and 2.3: non-assistance and covenant not to sue

14.55. Clauses 2.2 and 2.3 supplement the main release clause. They provide:

> "2.2 Without prejudice to the generality of the foregoing, [Party A] agrees not to sue, commence, voluntarily aid in any way, prosecute or cause to be commenced or prosecuted any action, complaint, suit or other proceeding against the Group or its Associates or any of them in connection with the Settled Claims save to enforce the terms of this Agreement.

2.3 [Party A] agrees not to voluntarily aid or assist the [Name of the Company] (or its Associates) in any way (whether directly or indirectly) to sue, commence, prosecute or cause to be commenced or prosecuted any action, complaint, suit or other proceeding against the Group or its Associates in connection with the Settled Claims or HBOS Reading or Operation Hornet, in this jurisdiction or any other."

14.56. The Bank accepts that one aspect of the practical effect of these two clauses was to prevent customers from voluntarily sharing information with other customers if the purpose of doing so was to assist them to bring claims against the Bank which related to the claims settled by the customer. The Bank explained that it had amended these clauses from the Select Committee template because there were timing difficulties in having all the directors of a business sign a global settlement, and the amended clauses were intended to reduce the risk of future claims being brought against the Bank where there had been a settlement by only some of the relevant parties. These clauses were necessary to ensure that some finality could be achieved. In this way, the Bank felt able to offer redress to customers who were directors where their fellow directors were delayed in providing their submissions in the Customer Review.

14.57. However, the effect of these provisions was to stifle claims in two respects.

14.58. First, as the Bank accepts, the effect of both clauses was to prevent customers from sharing information with any third parties not a party to the settlement agreement, including the company itself, and other directors, shareholders or creditors of the company. This prevention of information-sharing meant that a settlement by one director could shut down other directors' claims (or claims by other individuals connected to the affected company), but it could also hinder the presentation of their claims to the Customer Review because of a lack of information. In my view, that goes further than the Bank's interest in finality required.

14.59. Secondly, the effect of clause 2.3 was to prevent any claims by the company itself. To my mind this went too far. As I have already set out above, the scope of "settled claims" was broad. It is incorporated into clause 2.3. Clause 2.3 prevents customers (who were almost exclusively directors of companies affected by the IAR fraud) from assisting their companies in any claims against the Bank "in connection with the settled claims or [IAR] or Operation Hornet".

14.60. Company claims were a cause for concern to the APPG, which wrote to the Bank on 14 November 2017 in the following terms:

"We have been told that, if an individual accepts the payment for D&I, he/she must forego any rights with regard to company loss claims and, indeed, agree not to assist with the investigation into a company claim. Can you please confirm this position, as this would seem entirely unreasonable?

The concern is that stalling on company claims could be due to a number of factors […]

if it stalls long enough on the company claims, many victims will simply accept the distress and inconvenience payments, sign the settlement agreement compromising all

of their claims and forget about or reluctantly forego the company claims. This is seen as a deliberate tactic by the Bank to minimise its own losses to the detriment of victims."

14.61. As a matter of law the customers and their companies are separate legal persons. Their claims against the Bank were not the same as the companies' claims against the Bank. By imposing clause 2.3 on all customers who entered into settlement agreements, the Bank simultaneously managed to shut down claims by their companies as well.

14.62. In practice the companies may not have had a viable claim against the Bank. Many were no longer in existence. Further, it is conceivable that a company might be able to bring a claim without the assistance of a particular director. However, one can see how a company's claims might have been stifled if (as was often the case) more than one former director of a company settled their individual claims. In this regard the Bank's case is that in making generous D&I payments it compensated for this.

V CONFIDENTIALITY CLAUSES

The broader controversy around confidentiality clauses

14.63. Confidentiality clauses, sometimes known as non-disclosure agreements ("NDAs") or gagging clauses, have been the subject of public criticism and come under increasing scrutiny in recent years, principally in the context of cases of sexual harassment and bullying in employment.

14.64. As can be seen in the Rt Hon Nicky Morgan MP's letter of 26 June 2018 to Professor Griggs, referred to earlier in the Chapter, the confidentiality provisions of the settlements that resulted from the Customer Review were a concern. The SME Alliance told me that the confidentiality provisions of the settlements were perceived to have been designed to frighten people.

14.65. In my view confidentiality provisions have a valid role in settlements. They serve the useful and legitimate purpose of protecting commercially sensitive information and enabling parties to a dispute to create a clean break.[61] There is nothing wrong as a matter of law or broader principle with parties agreeing to keep their settlement (and the events leading to it) confidential.

14.66. The question for me is whether the confidentiality clauses in the settlement agreements struck the right balance between these competing interests and, in light of all the circumstances, are fair and reasonable.

Scope of confidentiality obligations in settlement agreements

Clause 4

14.67. The core confidentiality provisions in the settlements are contained in clause 4 (they are the same in both the Select Committee template and the other templates).

[61] See *ABC v Telegraph Group* [2018] EWCA Civ 2329, [2019] 2 All ER 684; *Mionis v Democratic Press SA* [2017] EWCA Civ 1194, [2018] QB 662.

14.68. The information that both of the parties must keep confidential is "the terms of this Agreement or the contents of the discussions and negotiations which have led up to this Agreement".

14.69. There is an exception in clause 4 if the other party gives prior written consent. The fact of settlement on confidential terms is not itself confidential. There are carve outs for disclosure: to officers, agents and insurers per the terms of the agreement or as required to carry it out; to legal and financial professional advisers; as required by applicable law and/or regulators and/or court orders; if the information is already in the public domain; of information disclosed to the party by a third party who is not in breach of confidence; and to financial regulatory bodies and HMRC.

14.70. Clause 4 is not especially onerous. The underlying fraud and its mistreatment of customers that led to discussions and negotiations are not confidential. The Bank confirmed this in letters to Mr Hollinrake MP dated 10 October 2018, and to Dame Linda Dobbs dated 6 November 2018. The former was a response to a letter from Mr Hollinrake MP, for the APPG, which included the following:

> "I would also like to query with [sic] the settlement agreement, a sample of which was sent to the Treasury Select Committee by Professor Griggs. We have had representations regarding section 4 of the agreement, which deals with confidentiality. There appears to be confusion with regard to the exceptions. It is our understanding that 4.2.3 allows the victims to still speak voluntarily with the police, regulators, MPs, etc about their case and concerns, and that they are able to do so without informing Lloyds. However, concern [sic] have been expressed that signatories would only be able to speak with police if presented with a court order.
>
> […]. Can I therefore have your assurances that any of the victims that wish to present information to any law enforcement agency, regulator, MP or parliamentary group may do so freely and without the need to inform the bank."

14.71. Both the Bank's response to Mr Hollinrake MP and letter to Dame Linda Dobbs stated that clause 4.1 was:

> "limited in scope […and…] only serves to keep confidential the without prejudice discussions and negotiations leading up to a settlement and the terms of the settlement itself".

14.72. The letter to Mr Hollinrake MP continued:

> "Because the clause is limited in this way, it does not restrict any customer from speaking to anybody (including the police, regulators, or their MPs) about their circumstances, their claims, their case or their concerns about HBOS Impaired Assets in Reading. The only information which customers need to keep confidential is (i) the terms of the agreement and (ii) discussions and negotiations which led to the agreement itself.
>
> In addition, although narrowly drawn, the confidentiality clause has a number of express 'carve outs' including the one you refer to in your letter in relation to disclosure

obligations (i.e. "to the extent required by applicable law…or pursuant to any order of court" etc). There is also a clause that explicitly allows any party to notify the FCA, PRA, HMRC or the FOS of the existence or terms of the agreement without requiring consent from the other parties.

I trust that this provides the assurances you have asked for."

14.73. As I have indicated, it is standard practice for parties to make their negotiations and the terms of any settlement confidential. Although the likelihood of getting consent from the other party for further disclosure might be small, the express possibility moderates these clauses even further. Were these the only confidentiality provisions of the settlements, I would regard them as reasonable and fair.

Clauses 2.2 and 2.3: non-assistance and covenant not to sue

14.74. These clauses appear within the "release" section of the agreements, not the "confidentiality" section. As explained above, their primary effect was to prevent claims by third parties such as the company, shareholders and creditors of the company. However, they also had the effect of restricting information-sharing between customers affected by the IAR fraud.

14.75. Thus, in one sample case, the effect of these clauses was to prevent former directors from sharing key correspondence with each other (where some but not all the directors had settled). That led one director to refuse the Bank's offer of redress. This potentially wasted time and resources for both the director and the Bank.

14.76. In another sample case, also dealt with in Chapter 10, the non-assistance clause meant that an individual whose parent (now deceased) had been affected by the fraud was unable to obtain information from the parent's business partners.

14.77. In addition to what emerged in the sample cases, a number of customers who came to see me complained about not being able to speak to former colleagues and that this hindered their ability to formulate their submissions to the Customer Review.

14.78. Despite the fact that the wording of clauses 2.2 and 2.3 in the other templates does not expressly refer to "confidentiality", as does clause 4, they effectively imposed additional disclosure restrictions on customers. In not drawing attention to them in Professor Griggs' letter to the Rt Hon Nicky Morgan MP, Professor Griggs and the Bank unintentionally did not provide the Treasury Select Committee with a full picture of the restrictions in the settlement agreements.

VI EXCLUSION CLAUSES

14.79. The settlement agreements contained clauses (which I will describe as exclusion clauses) which precluded reliance on any "representation, warranty, assurance, covenant, indemnity, undertaking or commitment which is not expressly set out in this Agreement". They also stated that:

"the only rights or remedies in relation to any representation, warranty, assurance, covenant, indemnity, undertaking or commitment given or action taken in connection with this Agreement are pursuant to this Agreement".

14.80. There was also an "entire agreement" clause, which has the effect of preventing parties from asserting that oral or written assurances were part of the contract.

14.81. The settlements contained further exclusion clauses preventing customers from relying upon any representation or advice in respect of the tax treatment of the outcome payments. That was despite the Bank providing standard-form "Outcome Payments Fact Sheets" following its discussions with HMRC, reassuring customers that payments in respect of distress and inconvenience payments, QCS fees and waivers of debts were not taxable. I should emphasise that no customers have raised complaints about these clauses but they also operated as exclusion clauses. For completeness my comments below apply equally to these clauses.

14.82. The Bank knew, as it was developing the Customer Review, that stakeholders objected to exclusion clauses. As early as 7 February 2017 the then chair of the APPG, Mr George Kerevan MP, had written to the Bank stating that:

"it is critical that you avoid blanket schemes like the current and defective one at RBS with regard to customers forced into the GRG unit. The latter has unacceptable exclusion clauses […]".

14.83. The use of exclusion clauses is controversial in banking contracts because of the inequality of bargaining power between banks and many of their customers. Exclusion clauses prevent a party from relying on an oral representation made by the other contracting party, regardless of whether that representation was false and regardless of whether they relied on that false representation when entering into the contract. However, in the cases that I sampled, I do not think they caused material unfairness or were unreasonable.

VII SETTLEMENTS FOR QCS FEES ONLY

14.84. As I explained above, the Bank's policy was to require any individual receiving a total payment of £2,000 or more to sign a settlement agreement.

14.85. Shareholders were not eligible to participate in the Customer Review. That I addressed in Chapters 11 and 12. Nonetheless, the Bank refunded an amount in respect of QCS fees to shareholders in some cases. In each case the Bank required these shareholders, as a condition of receiving their share of the QCS fee, to enter into a settlement agreement. Those settlement agreements were on the same basis as for customers who had been through the Customer Review.

14.86. The rationale for requiring individuals to enter into full settlement agreements, where they were only receiving QCS fees, is not obvious. For shareholders, the principles which the Bank had for settlements (set out above) were not applicable as they were not true participants in the Customer Review. In particular, it is difficult to see how "certainty" and "closure" are laudable aims in respect of claims that the shareholder has not been

permitted to advance, and the Bank has not considered. To the extent that the Bank had concerns about maintaining confidentiality regarding the payments made by way of refunds of QCS fees, the matter could have been dealt with by way of a short, separate confidentiality agreement.

14.87. The sole exception to the requirement for a settlement agreement was where the sum paid by the Bank was less than £2,000. Below that sum, shareholders countersigned an offer letter from the Bank that did not require them to release any claims, nor to maintain any confidentiality.

14.88. The Bank appears to have implemented the rule strictly. There were five cases in which the refunds of QCS fees were between £2,000 and £2,050, and in each case the Bank required the shareholders to sign a full settlement agreement, even in one case where the refund was paid to joint shareholders (and so their individual entitlements would have been below the threshold).

VIII CONCLUSIONS

14.89. The Bank had legitimate reasons for requiring customers dealt with in the course of the Customer Review to enter settlement agreements and to require them to agree to confidentiality obligations. In my view not all complaints by customers about the settlement agreements are justified. Moreover, the Bank made independent legal advice a precondition to customers signing the agreements, a policy which I have commended.

14.90. Nevertheless, I have concluded that the Bank's conduct in relation to settlement agreements, and some of the terms in them, were not fair and reasonable. Essentially it comes down to a failure properly to take into account the interests of customers, and a lack of sufficient transparency about the standard terms which were in use.

The different settlement templates

14.91. As I have explained, four settlement templates were used, with important differences. The Select Committee template was represented in Professor Griggs' letter to Parliament as "a sample", and this gave the wrong impression that the template was representative of the settlement terms upon which the Bank had offered redress to customers in the Customer Review. Professor Griggs and the Bank have explained to me how this mistake occurred.

Breadth of main release clause

14.92. I do not consider the breadth of the main release clause in the settlement agreements to have been fair and reasonable. However, as a matter of law there is nothing wrong with a broad release.

14.93. The scope of the Customer Review was limited. Customers, or the companies affected by the IAR fraud, could have had other potential claims surrounding the IAR fraud which the Customer Review did not address. Those claims would be covered by the main release clause and barred by the settlement agreements. However, customers would have

been aware of this if they took advantage of the legal advice made available by the Bank before signing a settlement agreement.

Confidentiality and disclosure

14.94. In my view clause 4, "Confidentiality", in the settlement agreements was fair and reasonable. As stated by the Bank in correspondence with Dame Linda Dobbs and the APPG, it was limited to the negotiations and the terms of settlement. It also had a number of carve-outs. This means that the confidentiality clauses in the agreements based on the Select Committee template, which had no other confidentiality terms, were also fair and reasonable.

14.95. On the other hand, I do not regard clauses 2.2 and 2.3 in the settlements based on the other templates as fair and reasonable. And those other templates were used in all but three of the 60 settlements I have seen.

14.96. These clauses had the effect of imposing further restrictions on customers. The effect has been to prevent information sharing between customers, which may have prevented customers from advancing their best case through lack of information. If the Bank had itself been more willing to disclose documents to customers, this might not have been a problem.

Exclusion clauses

14.97. For the reasons I gave given earlier, although somewhat controversial, the use of the wide exclusion clauses in the context of the Customer Review, did not cause any material unfairness in any of the sample cases nor was it unreasonable.

Settlements for QCS fees

14.98. Requiring those who received QCS fees to give up any claims that they might have in relation to the fraud was not fair and reasonable if they had had no opportunity to present those claims and the Bank was refusing to consider them. Imposing settlement agreements in such circumstances was a way for the Bank to buy, cheaply, immunity from claims, without having to consider them or pay any redress in relation to them.

PART E RECOMMENDATIONS

CHAPTER 15 CONCLUSIONS AND RECOMMENDATIONS

15.1. The Bank established the Customer Review in February 2017 to compensate the victims of the fraud committed at the HBOS Impaired Assets unit based at Reading and Bishopsgate, what in this report is called the IAR fraud. During the course of this report, I have sought to explain how the Bank went about the task. The explanation will assist customers in understanding how their cases were assessed.

15.2. However, I seek with the recommendations in this chapter to go further, and to remedy some of the shortcomings in the Customer Review. Before setting them out, let me begin with some general reflections, to provide a context for what I recommend.

I BACKGROUND OBSERVATIONS

Inconsistencies in the Customer Review

15.3. Standing back, I found that the Customer Review contained important inconsistencies. On procedural matters such as tracing customers, collecting relevant documents, and consistency checking, there was much to commend; but from the viewpoint of the customers I saw few, if any, were happy about the way they were treated, especially at the outcome meetings, due to the confrontational and, at times, forceful approach of the Bank. The Bank's message of its purpose at the launch of the Customer Review was clear (and welcome), to compensate the victims of the IAR fraud; yet the Customer Review's methodology and the reasoning behind particular offers for customers were decidedly opaque.

15.4. Turning to substance, the Bank sought to cast the net wide in defining the cohorts in the Customer Review population methodology; yet, with individuals, it limited awards to directors, and it then interpreted that requirement rigidly, without regard to the methodology's purpose, with the result that some impacted customers may have been excluded from the Customer Review. The review was generous in legal assistance, interim payments, and the award of £35,000 for delay to everyone in the Customer Review, yet despite statements at the outset it was mean-spirited in funding financial advice and forensic accounting when customers requested it and felt it necessary to advance their case. The writing off of customers' outstanding debts with the Bank was both generous and welcome, yet it discriminated against those customers who had repaid their debts or refinanced them in the period between the IAR fraud and the date of the Customer Review. The Bank was innovative in the appointment of an independent reviewer to oversee the Customer Review, yet it put in place procedures which eroded his appearance of independence.

15.5. Inconsistencies lay, as well, in the making of compensation offers. The Bank had a low evidential threshold for customers for distress and inconvenience ("D&I") payments, yet its high evidential threshold for direct and consequential ("D&C") loss payments was unexplained and was coupled with a blanket policy of refusing access to documents in its possession when it was obvious that many customers would no longer have them, since their company had been dissolved. Its D&I methodology produced far larger

compensation offers for directors than would be available in litigation, yet that methodology was not premised on compensating loss from the IAR fraud but on interactions with the fraudsters. The D&C methodology was aimed at compensating for the IAR fraud, but its adversarial and flawed approach denied redress to every customer in the Customer Review. Finally, the Bank commendably funded legal advice for customers accepting a compensation offer, yet unnecessarily bound them through the settlement agreements they had to sign to releasing the Bank from a wide range of future claims and to restrictions on disclosure.

Detailed conclusions

15.6. In summary, despite the obvious merits to the Customer Review, there were serious shortcomings. I have set out these shortcomings in the conclusions to Chapters 10 to 14. They must be read as part of this chapter.

15.7. For the detailed reasons given in those chapters, and applying my Terms of Reference, I have reached the conclusion that the methodology and process of the Customer Review did not achieve the purpose of delivering fair and reasonable offers of compensation. Moreover, the examination of the sample cases demonstrated that the judgments made on individual customer cases have not always been fair and reasonable.

15.8. There is no need to repeat the detailed conclusions to Chapters 10 to 14 here. This report is already too long. But it is those conclusions, and the analysis underlying them, which lead to the recommendations below about admitting further individuals into the Customer Review, extending debt relief and remedying the flaws in the compensation awarded.

Approach to recommendations

15.9. Against that background, the issue becomes how to redress the shortcomings in the Customer Review. To do that, it is necessary to step back from the detail and consider their overall impact on the outcomes for customers. This is so that I can shape recommendations to provide real, workable solutions that will most effectively put things right. At this point I set out a number of key observations which provide the essential context for those recommendations.

15.10. My review has not been, of course, an appeals process. I have reviewed a limited number of sample cases. Whilst my teams considered what, in their view, the outcome in respect of these cases might have been, that exercise was for the purpose of testing the fairness of the Bank's assessment process across the Customer Review; it was not part of an appellate review in individual cases. The outcome of this analysis can therefore only assist in identifying a generalised pattern. It cannot produce a specific answer in any single case.

15.11. What follows are recommendations which aim to be workable, and at the all-important practical level, respond genuinely to the many shortcomings of the Customer Review where these caused results which were not fair and reasonable.

15.12. At the same time, I bear in mind the original, commendable intentions of the Customer Review, which included the need to be swift, and to avoid the need for customers to

engage in a lengthy, onerous or distressing legal process. These are intentions that I do not want to lose sight of. They remind me that there must be a practicality about my recommendations.

15.13. Where this comes out is that I have sought to devise recommendations that: (1) can provide genuine and real solutions to counteract the shortcomings of the Customer Review; (2) are, at the same time, practical, workable and realistic; and therefore; (3) provide swift results, without requiring customers to engage in a lengthy or onerous process; and (4) seek to take advantage of, and use, those elements of the Customer Review and the work undertaken in relation to it that I have not found to be unreasonable, or to have caused unfairness.

15.14. It is important to note that I have not made specific recommendations in response to every criticism made in this report. What I have sought to do is to step back from the detail of the various shortcomings, and take an overall view of their impact on customers. The purpose of my recommendations is to seek to address those shortcomings which most affected the overall fairness and reasonableness of the Customer Review process and customers' outcomes.

The key finding: D&C loss

15.15. Before turning to the details of the recommendations, however, let me say something at this stage about our key finding. It concerns the fact, as we saw in Chapter 12, that the Bank did not make a single award for D&C loss.

15.16. By contrast, when my teams examined the sample cases, they concluded that, on a proper approach to the documents on the files and the submissions of customers, there were a limited number of cases in which there may have been a good claim for that loss. It follows that a proper and fairly conducted D&C loss assessment, which fairly took into account the limitations of the Customer Review process, may have resulted in an award for D&C loss in these cases.

15.17. In other cases, my teams concluded that, even on a proper analysis, they could not say that a finding of no D&C loss was wrong. Taking a favourable view of the customer's evidence, and with a supportive banking team in place rather than the criminals, the outcome would likely to have been that the business would have failed, or rather not have been the success the customer believed.

15.18. Thus there is the key finding of the my review: that the failings in the Bank's assessment of D&C loss may well have deprived some, admittedly only some, customers, of redress for that loss.

15.19. The Bank's failure to acknowledge that the fraud had caused a single instance of D&C loss communicated that the failure of every single company was inevitable, and was not caused by the fraud.

15.20. Perhaps more damagingly, it also communicated (even for those companies that would have failed anyway) that none of the customers' financial suffering had anything to do with the actions of the criminals. By default, the message across the board was that all of

those failures and all of that suffering were of the customers' own making. This is an unacceptable denial of responsibility. It undermined the sincerity of the Bank's apologies for the IAR fraud, and portrayed the Bank as the only victim of the IAR fraud to suffer financial loss.

15.21. Even more hurtfully, it caused additional and fresh distress to some customers who had already had to deal with being made to feel like failures at the time of the IAR fraud, and (for some) with being rebuffed by the Bank in earlier attempts to raise a complaint and uncover the truth.

15.22. This must be redressed, and the consequences of the IAR fraud must be acknowledged. Even where the reality may be that the level of D&I redress paid exceeded any D&C loss caused, it is important that the Bank takes responsibility where D&C loss has been caused.

The D&I methodology

15.23. In the Customer Review what customers were compensated for was D&I loss, awarded under a non-legal process devised by the Bank. In Chapter 13 I explained that, whatever its artificiality, the compensation awarded under that label was, in two respects, generous. First, it resulted in sums beyond what a court would have awarded by way of damages for D&I. Indeed, in some cases the D&I redress figure appears to have been uplifted even further. That in some cases masked the reality that a payment in respect of D&C loss was being made.

15.24. Secondly, the extension with some customers of the D&I redress scheme to non-fraudulent conduct (i.e. what I have called bad or aggressive banking) has resulted in their receiving significant sums. Again, these may have been beyond what a customer could have recovered as damages in a court process.

15.25. Under the D&I methodology the net result is that, although in some cases customers may have been under-compensated for their losses, in other cases their outcome overall will have been as good as, even better than, the outcome they might have received under a more rational and fair process. That does not mean that nothing need be done. Over-compensation for one person does not make under-compensation for another acceptable.

15.26. What it does mean, however, is that because the Bank never properly explained its methodology or its findings, customers were not given information to understand why they were (and were not) being compensated. For example, the failure to explain that the D&I redress scheme covered cases where no fraudulent conduct was found, resulted in some customers assuming that the receipt of a D&I award meant that the Bank had found that fraud had been perpetrated in their case for which it was not offering fair compensation.

15.27. It is a particular frustration to me that, for some customers, a proper and more transparent exercise would have meant that they understood that their compensation was not unreasonable when compared with what they would obtain in legal proceedings.

Moreover, the opaqueness in the process may have led some customers to decline offers and opt out of the Customer Review to their possible detriment.

An important note of caution

15.28. In reaching my conclusion that the Bank's assessment of compensation was flawed, and in recommending that customers have the possibility of a reassessment, I do not want to raise false hopes or unrealistic expectations in customers who have felt wronged. As I have said, my review was not an appeals process, and I have only reviewed a sample of cases. I cannot therefore comment on which cases may have had a viable D&C claim, let alone how such D&C claim would measure up to the D&I redress offered and in many cases accepted. Nor, obviously, can I comment on how any of those cases would have played out in court, had they been litigated.

15.29. Customers who were the victims of the IAR fraud have been through much and over an extended period of time. There has been a significant emotional and personal cost. I do not want to do or say anything which adds to that by encouraging them to bring actions that may have little merit. Nor do I want to lead customers to believe that they, specifically, have been deprived of a great measure of compensation when they may not have been.

15.30. However, I have reached the considered position that it is right that the shortcomings of the Customer Review need to be addressed. It is important that there should be real solutions. It may be that the working out of my recommendations does not result in a materially different outcome for many customers. The key difference will be that their claims will have been properly addressed, in an open and transparent manner.

II DE FACTO DIRECTORS/THOSE RUNNING A BUSINESS

15.31. In Chapter 11, I identified various deficiencies in the Bank's rules for identifying the Customer Review population. In particular I highlighted how, in determining whether individuals who were not formally appointed directors qualified for inclusion in the Customer Review population, the Bank placed significant weight on evidence of how HBOS regarded the individual at the time the business was in IAR.

15.32. Furthermore, the Bank assessed the individual's eligibility by considering its contemporaneous records and contemporaneous evidence provided by the customer. As I discuss in Chapter 12, an assessment focused largely on contemporaneous evidence was inappropriate in the context of the Customer Review.

15.33. In its early press releases, the Bank described those it was seeking to compensate in broad terms, those who "may have been affected by the criminal activities linked to [… IAR]", and those "impacted" by the IAR fraud.

15.34. In my view, consistently with what the Bank said, those who were actively involved in the running of the business at the time it was in IAR are persons who might have been "affected" or "impacted" by the IAR fraud.

15.35. Yet I noted in Chapters 3 and 11 that a number of individuals who were not formally appointed directors sought to be included in the Customer Review but were rejected by the Bank.

15.36. The Bank must revisit such cases. In deciding whether an individual was actively involved in the running of the business, it must take into account all relevant evidence, including the written statement of the individual concerned and the corroborative statements of others involved in the running of the business at the relevant time. HBOS' treatment of the individual at the time the business was managed by IAR is a relevant consideration, but must not be a determinative factor.

15.37. This is not simply a matter of applying a legal test as to whether a person was a de facto director. Where a customer was actively involved in the running of the business at the time it was in IAR, the individual should be treated in the same way as other customers who were included in the Customer Review population. That is, the Bank should perform the D&I matrix calculation and the customer will be entitled to a D&C assessment under the arrangements considered below.

15.38. Furthermore, in performing such D&I calculation, where the individual is a spouse or partner of someone who was a director of the business, I consider that the approach adopted by Professor Griggs should be applied. As explained in Chapter 5, Professor Griggs took a beneficial approach to spouse directors. This approach should be adopted in respect of all spouses and unmarried partners who are found to have been involved in the running of the business. This means that the Bank should give weight to the individual's statement about the extent of their involvement in the business and the impact of the criminals on their life. Where a business was operated by a couple, in the absence of evidence to the contrary, the spouse or partner should be considered to have suffered the same or similar distress to the customer included in the Customer Review.

Recommendation 1.1: The Bank must reconsider all cases where an individual sought inclusion in the Customer Review on the basis that they were a de facto director or were otherwise involved in the running of the business.

Recommendation 1.2: In determining whether an individual was a de facto director or actively involved in the running of the business, the Bank should take into account all relevant evidence, and give weight to the individual's written statement and any corroborative statements of others involved in the running of the business at the relevant time.

Recommendation 1.3: Where an individual who is found to qualify for inclusion in the Customer Review in this way is a spouse or partner of another director of the business, in the absence of evidence to the contrary, the Bank should consider each of them to have suffered the same or similar distress.

III WRITING OFF CUSTOMERS' DEBTS

15.39. As I explained in Chapter 10, the Bank's policy of writing off customers' remaining debts was laudable, but the way in which it was implemented discriminated, in effect,

against customers who had either repaid their debts to the Bank (often, as I have been told, at considerable personal cost to themselves and their families) or had refinanced their debts with another financial institution prior to the commencement of the Customer Review.

The recommendation in outline

15.40. Against that background I have concluded that the Bank should revisit this policy in line with the recommendations below, which are to be implemented retrospectively.

15.41. The Bank's policy on debt write-off should be amended on the following basis:

(1) Any customer who had a non-nil outcome and had outstanding indebtedness (of the type set out in sub-paragraph 2) at the relevant time (described below in sub-paragraph 3) is eligible for debt write off.

(2) The type of indebtedness covered should be consistent with that to which the Bank applied its policy during the Customer Review, i.e. mortgage debts, personal loans, business debts (in the customer's personal name), or outstanding personal guarantees for business debts.

(3) The relevant time for determining eligibility is the date at which the Bank's debt was either repaid, refinanced with another institution, or was demanded (by court enforcement process or otherwise), provided that such debt existed at the time of either (i) the business' exit from IAR; or (ii) the failure of the business.

15.42. Eligible customers should be compensated on the following basis:

(1) Where debt has been repaid, customers should be compensated for the debt outstanding at the time the repayment was made to the Bank, together with compensatory interest at 8% from that date;

(2) Where debt has been refinanced with another institution, customers should be compensated for the remaining debt outstanding (with that institution or any successor, in the case of multiple refinancings) at the commencement of the Customer Review, together with compensatory interest at 8% from the date that they received their final outcome letter; and

(3) Where debt was demanded or enforced (but neither repaid by the customer nor refinanced), customers should be compensated for the debt outstanding at the time the demand was executed or the enforcement process completed, together with compensatory interest at 8% from that date.

How debt relief will work

15.43. My financial advisers have not identified any simple and reliable way of identifying from the Bank documentation that they have seen all customers who would be eligible for this debt write-off. The best approach seems to be for the Bank to write to all customers who received a non-nil outcome under the Customer Review, explaining the revised policy and asking them to submit details of any debts which they consider would

fall to be compensated, together with supporting documentation (where available to the customer).

15.44. Where the customer does not have supporting documentation available (such as, for example, mortgage redemption statements or loan account statements), the Bank should adopt a sympathetic and pragmatic position in considering any corroborative evidence. This acknowledges the practical difficulties customers may have in locating relevant records given the length of time that has passed.

15.45. My financial advisers tell me that are a number of possible ways to calculate the compensation payable, particularly where the Bank's debt was repaid through the sale of personal assets. In formulating this approach, however, I have sought to maintain consistency with the treatment of customers who have had debts written off.

15.46. Applying 8% compensatory interest would maintain consistency with the Customer Review's methodology for compensating for D&C losses. It also aligns with the aim described elsewhere in this chapter of simple and swift outcomes for eligible customers, insofar as this is possible.

15.47. Any payments made under this recommendation will need to be taken into account as part of the revised D&C assessment (which I address below). This is because writing off customers' debts ultimately comprises a form of redress for D&C loss. There can be no double recovery and, where debts are repaid, the repayment will have to be taken into account in calculating any D&C outcome resulting from a revised D&C assessment.

Recommendation 2: In line with this approach, the Bank must reconsider customers' eligibility for debt relief payments where such debt existed at the time of the IAR fraud, and that debt was subsequently repaid or refinanced before the commencement of the Customer Review.

IV COMPENSATION

15.48. In Chapter 12 I concluded that the Bank's approach to the assessment of D&C loss was flawed: it failed to consider the evidence properly, failed to accommodate the limitations of the Customer Review, and took an incorrect legal approach in not considering the possible counterfactuals.

15.49. Then in Chapter 13 I concluded that the Bank's non-legal D&I methodology was also flawed. The upshot was that it produced illogical results.

15.50. Given those conclusions, what are the possible options? They would seem to be fourfold: (1) to do nothing; (2) to take a non-legal, but consistent, decision to provide some level of award across all cases; (3) to release customers from their settlements; and (4) to provide for some sort of reconsideration of assessments across all cases.

The four options

(1) Do nothing?

15.51. Except in one respect, I do not recommend that anything be done in relation to payments made to customers under the D&I matrix. It was not necessarily logical in its methodology or design, but the methodology was applied consistently across customers, and overall the sums awarded were more generous (intentionally so) than the level of damages that would have been awarded by a court for D&I. I would not wish to interfere with that outcome.

15.52. But a do-nothing policy is not appropriate in relation to D&C loss, even though as I have explained many customers may have received more D&I redress than they would have likely received in court proceedings. That was especially so in cases where the redress figure was subject to uplifts by Professor Griggs, triggered by settlement discussions, or because of concerns that there may have been a viable case for D&C loss.

15.53. The reasons for rejecting the option of doing nothing in relation to D&C loss are threefold. First, the fact that some customers have been adequately compensated does not make the under-compensation of others fair. Secondly, as explained in Chapter 12, the D&C assessment process was procedurally unfair. Finally, a do-nothing policy would fail to hold the Bank accountable for such D&C loss as the IAR fraud caused.

(2) Payment of a lump sum award

15.54. The second option is to recommend that, given the flawed D&C analysis, the Bank simply pay a further sum to each customer. This might either be a fixed amount across the board or, for example, calculated by applying a multiplier to the level of D&I redress already awarded.

15.55. There would be a number of advantages to such an option. First, simplicity; it would not entail any further customer input, and minimal further Bank effort. Secondly, there is a certain element of procedural fairness to it in terms of clarity and consistency. Thirdly, customers could have the additional payments in their pockets within weeks of the system being implemented.

15.56. However, it would not provide substantive fairness, either to customers or to the Bank. The system would not distinguish between those who have truly suffered D&C loss, and those who have not. It would not identify, within those who have suffered D&C loss, the differing magnitudes. To that extent it would not be transparent.

15.57. The mechanistic nature, which is what provides its simplicity and speed, also prevents any true acknowledgment of, or acceptance of responsibility for, the D&C loss caused by the IAR fraud.

15.58. Moreover, it would likely compound, rather than redress, the unfairness of the Customer Review. If the D&I redress payments cannot be logically justified, they cannot provide a reference point for calculating compensation for D&C loss.

15.59. That rules out the "multiplier" approach to calculating any D&C loss compensation, as there is no alternative simple or clear reference point for any such calculation. The alternative approach, a fixed payment, is too blunt an instrument. It would again compound unfairness.

(3) Release customers from their settlement restrictions.

15.60. The third option is to release customers from their settlement agreements. Knowing about how the Customer Review operated from this report, they would then be in a better position to pursue a legal claim for their D&C loss. A legal claim would mean the ability to obtain disclosure, make submissions, and fully understand, respond to and interrogate the other side's position. The claim could be mediated or litigated.

15.61. However, the option seems of no practical assistance to most customers. Litigation was (in theory) available to customers at the stage at which they settled with the Bank. Customers regularly emphasised to me that the Bank's approach of "take the offer or proceed to litigation" in reality left them with no option but to accept the outcome offer, as they had neither the finances nor emotional energy to undertake the legal process. This option is therefore the very option that the majority of customers have already rejected.

15.62. Of equal concern is that recommending this option could encourage expensive, lengthy and ultimately fruitless litigation, at least in its initial stages (even if the case ultimately settled). The view of my teams is that despite the fundamental problems with the Customer Review, in many cases customers may not have suffered the D&C loss that they believe they did. Should a court require any D&I payment to be off-set against any D&C award (a quite possible outcome), it could mean that any customer victories are pyrrhic. Customers might also face limitation issues.

(4) Reconsideration of the D&C assessment

15.63. It will be apparent, by process of elimination, that this is the option that I favour, and which forms the basis of the recommendations below.

15.64. In my view, it is the most principled option. The Bank got the assessment of D&C loss wrong. Consequently, that assessment must be re-done.

The reassessment process

15.65. Precisely how this is to be achieved is not easy. The detail of any revised scheme must be carefully thought through. It must also be the result of a collaborative discussion with the relevant stakeholders. Some customers and their representative groups feel that they were not sufficiently consulted about the design of the Customer Review. The same mistake must not be made again.

15.66. Accordingly, I cannot provide the detailed structure of any revised D&C assessment. At Appendix 2 of the report I provide one possibility, an independent panel which would proceed in a non-legalistic manner to conduct the assessments. Its underlying principles should form part of any revised D&C reassessment process.

15.67. Certainly, the Bank should not conduct this revised D&C assessment. What is clear from the customer contact I have had is that customers have lost confidence in the Bank. A revised D&C assessment conducted by the Bank would lack credibility. Accordingly, it is vital that the revised D&C assessment process is conducted by an independent third party.

15.68. As with the Customer Review in the first place, no customer should or can be compelled to participate in the revised D&C assessment. A customer may not wish to participate, or even to have their case put through the revised D&C assessment at all. They may simply prefer to leave the status quo as it is.

Recommendation 3.1: For individuals, the Bank must arrange for the reassessment of D&C losses by an independent body, on an opt-in basis, after agreeing the arrangements with key stakeholders. The principles underlying the structure proposed at Appendix 2 must form part of the agreed revised D&C assessment process.

Shareholders

15.69. Shareholders claim their losses through their company. That means they will not necessarily have any influence over whether the business that their complaint concerns is included in the revised D&C assessment. The former directors of a company may not want to opt into a reassessment.

15.70. In my view if shareholders raised a complaint about company losses in the course of the Customer Review, a revised D&C assessment should be conducted for the business. As all companies received a nil outcome letter, they did not sign a settlement agreement (save, possibly, in respect of only QCS fees, which I address below), so there is no difficulty in the business-level assessment for D&C losses being repeated. Further shareholder input should not be necessary.

Recommendation 3.2: For a business, if any of its shareholders sought to make a claim in the course of the Customer Review the Bank must arrange for the independent body (constituted in accordance with Recommendation 3.1) to conduct a D&C assessment.

Direct claims by shareholders, creditors and guarantors

15.71. As concerns third parties who might have direct claims (e.g. shareholders with personal claims, creditors and guarantors), to bring them into the Customer Review at this stage would require starting that process for them from scratch. That does not seem to me to be practical. Such individuals are not bound by any settlement agreement (save possibly in respect of only QCS fees, which I address below). They are (and, save for the few subject to QCS fee settlements, have always been) free to bring legal proceedings if they consider it appropriate to do so. Accordingly, I have decided not to make any recommendations in respect of such potential claimants.

V SETTLEMENT AGREEMENTS

Those receiving QCS fees

15.72. I concluded in Chapter 14 that it was not fair of the Bank to require signature of a settlement agreement where the signatory was only receiving a refund in respect of QCS fees. That is not to say that they have a claim against the Bank. It is simply to recognise that requiring settlement of all claims merely for receiving a QCS-fee payment was unreasonable.

Recommendation 4.1: The Bank must release non-director shareholders (or any other third parties, including the companies themselves) who only received a QCS-fee refund from their settlement agreements.

Clarification on use of templates

15.73. I set out in Chapter 14 the circumstances in which an apparently little used settlement template came to be provided as "a sample" to the Treasury Select Committee, and the confusion and ill feeling that this created among customers.

Recommendation 4.2: The Bank must write to the Treasury Select Committee providing an accurate picture of the use of settlement templates in the course of the Customer Review.

Release and confidentiality provisions

15.74. Where customers opting into a revised D&C assessment need a formal release from the provisions of the settlement agreement in order to do so, the Bank should grant it.

15.75. As explained in Chapter 14, Clauses 2.2 and 2.3 operate as additional limits to the confidentiality clause, clause 4, on what customers can disclose. That was in addition to their functions within the release clause. In that chapter I concluded that that was not fair and reasonable.

15.76. In the face of customers' concerns, the Bank gave public assurances that the only confidentiality-type provisions of the settlement agreements were at clause 4, which as I have said were fair and reasonable.

15.77. The Bank must stand by its assurances as to the confidentiality provisions and not seek to rely on clauses 2.2 and 2.3.

15.78. Two recommendations follow from this. Beyond that, I do not recommend any wider release from settlement agreements. Finality is important, and customers were entitled to legal advice before they signed the settlement agreements they did. In combination, the recommendations that follow should redress the most significant shortcomings of the Customer Review relating to settlements. I leave it to the Bank to consider on a case by case basis, in light of my comments in Chapter 14, any other specific requests to be released from the settlement agreement by customers, and if so on what terms.

Recommendation 4.3: The Bank must release customers opting into a revised D&C assessment under Recommendation 3.1 from the relevant provisions of their settlement agreement.

Recommendation 4.4: The Bank must undertake (i) not to bring or threaten to bring any breach of confidence claim under any clause in the settlements other than clause 4; and (ii) not to bring or threaten to bring any breach of contract claim in respect of customers sharing information under clauses 2.2 and 2.3 (save to the extent that the same would constitute a breach of clause 4).

APPENDICES

APPENDIX I TERMS OF REFERENCE FOR CRANSTON REVIEW

Aim

The aim of the assurance review ("Assurance Review") is to consider whether:

- The methodology and process developed for the Customer Review has achieved the purpose of delivering fair and reasonable offers of compensation and has been consistently applied in accordance with established principles of Treating Customers Fairly.
- The judgements that have been made on individual customer cases are fair and reasonable, including in relation to the assessment of direct and consequential losses.
- The overall level of compensation to customers has been fair and reasonable when compared to the damages likely to have been available through a court process.
- Professor Russel Griggs ("Professor Griggs") has exercised appropriate levels of independent challenge over customer outcomes, ensured that offers to customers have been reasonable and was able to properly perform his role.

Phase 1

Through a review of the methodology, to determine whether it provides a reasonable basis on which to deliver fair outcomes and offer swift and generous compensation, taking into account:

- **Approach to building a case file** including the opportunity for customers to provide input, with the benefit of independent legal advice, and LBG's process of gathering and collating documentation from LBG records;
- **Approach to assessing a case** including the 'heads of loss' considered, the approach and basis for establishing loss and ensuring consistency in assessments;
- **Approach to compensation** including consideration of direct losses, consequential losses and personal impacts, as undertaken by both LBG and the Independent Reviewer
- **Approach to communicating with customers** including the clarity of the process and the time provided for customers at each stage of the Review;
- **Approach to disclosure (in the context of a without prejudice voluntary review)** including the provision of available information to Professor Griggs and customers, the explanation of outcomes and redress to customers (both in writing and through face to face meetings), the explanation of how the level of compensation was arrived and whether customers were able and had the opportunity to challenge LBG's view;
- **Approach to supporting customers through the Review** including the reasonableness of decisions in relation to professional advisor costs;
- **Approach to additional information from customers** including the opportunity for customers to provide additional information for consideration by LBG and Professor

Griggs if they disagreed with their outcome at first instance and their ability to provide it so that the LBG's view could be challenged;

- **Approach to Settlement Agreements** including the requirement that customers take independent legal advice prior to releasing claims and whether the terms and conditions included within the Settlement Agreements were fair and reasonable.

Phase 2

Through a representative sampling approach, to consider whether:

- The methodology of the Customer Review has been applied as intended and learnings have been adopted during the Customer Review
- Customer claims have been assessed across the 'heads of loss' consistently
- Customer outcomes have been fair and reasonable, and are in line with the objectives and methodology of the Customer Review
- Customers have had reasonable advice costs paid and have been provided with sufficient time and professional support to make informed decisions

Method

To achieve its aim conduct of the Assurance Review will involve:

- Meeting with LBG and Professor Griggs
- Seeking input from external stakeholders (including but not limited to FCA, SME Alliance, APPG on Fair Business Banking and Treasury Select Committee)
- Reviewing LBG methodology for the Customer Review
- Reviewing LBG processes for the Customer Review, including customer communications
- Reviewing customer cases through a representative sample.

Timeline

The current planning assumption is that the Assurance Review will be completed by 30 September 2019.

APPENDIX II MODEL ASSESSMENT PANEL

1. Nature of panel

Proposition 1: The panel is to have legal and financial expertise

Comment: A number of different areas of expertise will be required. Legal expertise will obviously be needed, as will financial expertise. Potentially, also, expertise in business banking and SMEs may be of assistance. As such, a panel may be more appropriate than an individual adjudicator.

The constitution of a panel of several individuals with different expertise would provide balance. In any event independent analysis must be the foundation of assessment, not a bolted-on accessory to it. The panel would not be a replication of a legal process.

2. Inquisitorial not adversarial

Proposition 2: The panel process is to be inquisitorial

Comment: An adversarial process would require starting from scratch. It would duplicate the good work that has already been undertaken in the Customer Review, and waste the costs already expended on legal advice for customers.

It would require new work, requiring customers to undertake complex document review, produce evidence to essentially legal standards, draft submissions addressing legal tests, and advance their case in an adversarial forum. That could not realistically be done without customers being given further access to legal representation and further opportunities to present their complaints.

3. Using existing work

Proposition 3: Aspects of work already undertaken should be utilised

Comment: Existing work provides a base around which the structure of the revised D&C assessment should be built. In particular, use can and should be made of the material produced by way of customer submissions, legal representation and the file build without significant replication of these steps.

An inquisitorial process would mean that fair outcomes would be possible largely on the basis of the evidence already collated and customer submissions made to date. With a properly sensitive approach to reviewing the files, the current material and customer submissions should be sufficient for an independent panel to assess and reach fair decisions. The one exception to this pertains to expert financial assessment.

4. Evidential and legal standards to be applied

Proposition 4.1: Customer submissions should be given due evidential weight

Comment: This includes the corroborative value of submissions of different individuals, where they relate to the same business.

Proposition 4.2: It would not be appropriate for the panel to reject submissions solely because they do not accord with the documentary record

Comment: Customer submissions must be assessed on the proper "balance of probabilities" test. Where they are not expressly underpinned by the documentary record, this means that the assessment must consider the circumstantial evidence, other witness evidence, commercial common sense, the acknowledgment that fraudsters will not deliberately record their fraudulent conduct, and any other relevant matters.

Proposition 4.3: Allowance should be made for any incompleteness of the file build and for the potential unreliability of the documentary record as a result of the fraud

Proposition 4.4: A common-sense approach should be applied to proof of causation and loss

Comment: In the Customer Review the Bank dissuaded customers from treating the process as a legal process, so a common-sense approach should be applied to proof of causation and loss.

Proposition 4.5: The panel should apply a sensible approach to what it is fair to expect customers to have produced by way of evidence

Comment: A sensible approach must be applied to what it is fair to expect customers to have produced by way of evidence, in particular when hypothetical counterfactuals are in question such as contentions of loss of earnings and alternative opportunities. A contention should not be dismissed on the grounds that it is bare assertion without exploring the matter further with the customer.

5. Customer submissions and legal representation

Proposition 5.1: The panel process should avoid the need for significant (if any) further customer input

Comment: None of the benefit of the work done by customers and their legal advisors in the Customer Review should be lost. The process must avoid the need for further customer input, if possible, for reasons of speed and because of the emotional energy customers have already expended. It may be, however, that the panel will find it helpful if customers were to make short, oral submissions to the panel.

Proposition 5.2: The panel should formulate requests for further customer input in a manner not requiring professional assistance

Comment: The intention of this proposition is obvious, to enable further input from customers but without the need for further expenditure on professional assistance.

Proposition 5.3: There should be no need for input from lawyers on either side

Comment: There should be no need for legal representation in the Panel process for either side. The Bank must not employ external legal assistance to interact with or otherwise make submissions to the panel. That would perpetuate the inequality between the parties. If the Bank considers such advice necessary to assist it in the process, it cannot argue that customers should not be entitled (and funded by the Bank) to access the same.

6. File build

Proposition 6: The Bank is not required to undertake further document collation

Comment: The Bank has already collated for the Customer Review a significant number of documents in relation to each customer file. This work should not be wasted. The panel process does not require the Bank to commence the sort of document-collation exercise that it would have to undertake for a disclosure process in litigation. That means, however, that the assessment process will need to take account of the limitations on the documents available.

7. Disclosure

Proposition 7: Disclosure at the same level as in litigation is unnecessary

Comment: As an inquisitorial process, the panel will take on the burden of investigating the truth. It will have access to all available information and give proper weight to each party's evidence.

8. Financial expert analysis

Proposition 8: Financial expert analysis should be available to the panel

Comment: Financial expert input is needed across the board. It has not been obtained consistently by either the Bank or customers. One approach would be for the parties to instruct experts but that would be time consuming and costly, and more suited to adversarial proceedings. Instructing a joint expert is likely to require professional assistance.

A financial expert on the panel would be jointly appointed, owe their duties equally to both the Bank and the customer, and would undertake an impartial review of the evidence available. The financial expert could seek any further information from the Bank and the customer if it was considered necessary.

9. Reasoned decision

Proposition 9: The panel should publish a reasoned decision to the parties

There should be a reasoned decision explaining the basis on which the panel has reached its conclusions. It should be provided to both the Bank and the customer.

10. Application to fraud

Proposition 10: The panel should make awards for cases of fraudulent loss only

Comment: The Customer Review was to compensate for the IAR fraud, although the Bank extended D&I redress to some customers beyond fraud. Consistently with its purpose, fairness does not require that the Bank also compensate them for D&C loss, other than loss caused by the IAR fraud.

Thus while all customers in the Customer Review would have access to the panel, the first thing it should do is to assess whether the file shows any fraudulent activity. If it does not, no redress for D&C loss would be awarded.

The consideration of and findings as to fraud (or a lack of fraud) must be explained as part of the panel's decision.

11. Appeal

Proposition 11: There should be no appeal from a panel award

Comment: The interests of finality, speed and simplicity are against an appeals process. Appeals require further submissions, be they written or oral, and that, in turn, generates both additional cost and the potential need for professional representation. Access to an appeals process is not an intrinsic requirement of fairness.

12. Set off against panel awards

Proposition 12: There should be a set-off against any panel award of sums the Bank paid customers in the Customer Review other than (i) the original Customer Review outcome offer and; (ii) the £35,000 ex gratia payment

Comment: There are at least three possibilities:

(i) At one end of the spectrum, customers seeking awards from the panel should forgo their D&I payments. That would most likely mirror the set-off which a court would require: if it made a D&C award, any D&I payments would be set off against it.

(ii) At the other end of the spectrum, the Customer Review presented generous D&I redress as separate to the Bank's D&C assessment. In those circumstances, there is nothing wrong in allowing D&I redress payments to remain in place in addition to panel awards.

(iii) The middle course is for some set-off as in Proposition 12 above: since uplifts in the original D&I awards in the Customer Review were sometimes used as a vehicle to compensate for D&C losses, any uplifts made subsequently to the original outcome offer should be set off against any panel award. Other payments the Bank made, such

as those for QCS fees and debt relief, also had the flavour of D&C compensation. Adding panel redress on top of D&I compensation carries the risk of double recovery and therefore some set-off of these amounts is justified.

The middle course in Proposition 12 would mean that if the panel award is higher than the combined sum of any uplift (over the original outcome offer), QCS fees and written off debt (but excluding the £35,000 ex gratia payment), the customer would benefit.

On the other hand, if the panel award results in a lower payment than those sums, the customer can keep the higher amount.

The overall result is that a revised D&C assessment by the panel would not lead to customers losing any sums received under the Customer Review, but it would not necessarily result in the customer being awarded further redress.

13. Binding nature of panel process

Proposition 13: Customers choosing a panel assessment must abide by its decision, as must the Bank

Comment: Processes such as arbitration are entered into by agreements in which the parties agree to submit their dispute to the arbitrator and to be bound by the arbitrator's decision. The same should apply to decisions of the panel.

For customers the after-effects of the IAR fraud have gone on long enough, and there must be finality for them. Likewise, the Bank cannot be expected to continue funding risk-free assessment procedures for customers without some assurance of finality.

Thus a customer opting in to a revised D&C assessment by the panel and the Bank should agree to be bound by the outcome, and required to sign a suitably drafted "opt-in" agreement to that effect.

That agreement would need to address the impact of participation in a panel assessment upon an existing settlement agreement entered into as part of the Customer Review.

GLOSSARY

3VB	3 Verulam Buildings, Gray's Inn, London (barristers' chambers of which Sir Ross Cranston is an associate member)
Additional information	A submission made by a customer after receiving an outcome letter in the Customer Review
Administration	Insolvency process as described in the Insolvency Act 1986
APPG	All-Party Parliamentary Group on Fair Business Banking
Bank	Includes HBOS and Lloyd's Banking Group and its subsidiaries
BOS	Bank of Scotland (a subsidiary of Lloyds Banking Group)
CBI	Confederation of British Industry
CFCP team	Corporate Financial Crime Prevention team
Cranston Review	The 'Independent Assurance Review' as announced by LBG on 7 May 2019, led by Sir Ross Cranston
Customer Review	The compensation scheme set up in 2017 by Lloyds Banking Group and overseen by Professor Griggs to compensate customers impacted by the IAR fraud
Customers	Includes the directors and others associated with the business customers of the Bank
D&C (loss/redress)	Direct and consequential (loss/redress)
D&I	Distress & inconvenience
D&I matrix	The part of the Bank's methodology for calculating D&I redress payments
Dobbs Review	The review led by Dame Linda Dobbs DBE into whether the Bank properly investigated and reported the IAR fraud
Entity	A business customer of the Bank
EY	EY LLP
FCA	Financial Conduct Authority
FCA final notice	Final notice issued by the FCA on 20 June 2019 fining HBOS for regulatory failures in relation to the IAR fraud
FSA	Financial Services Authority (predecessor of FCA)
FSMA	Financial Services and Markets Act 2000
FTI	FTI Consulting LLP
HBOS	Halifax Bank of Scotland (a subsidiary of Lloyds Banking Group)
HMRC	Her Majesty's Revenue & Customs

IA	Impaired Assets
IAR	Impaired Assets Reading
IAR fraud	The fraud that occurred at HBOS IAR, which resulted in the convictions in 2017 of two HBOS bankers and four persons associated with QCS
IBR	Independent business review
Independent reviewer	Independent reviewer (Professor Russel Griggs OBE)
LBG	Lloyds Banking Group
Methodology	Rules the Bank designed to govern the Customer Review
MP	Member of Parliament
Operation Hornet	Thames Valley Police's investigation into the IAR fraud which commenced in 2010 and ended in 2017 with the criminals' conviction
Outcome letter	Letter from the Bank communicating redress a customer would receive (if any) under the Customer Review
Outcome meeting	Meeting between a customer and the Bank and/or the independent reviewer after the Bank made an offer of redress in an outcome letter
PA	Project Associates, the strategic communications consultancy which assisted Sir Ross Cranston in the Cranston Review
Pre-pack sale	Sale contract in which a company arranges to sell all /some of its assets to a pre-determined buyer prior to the appointment of an Administrator to facilitate the sale.
Project Lord Turnbull Report	Report by Sally Masterston, an employee of the Bank
QC	Quality Control
QC Panel	Senior bank personnel designated to approve customer redress awards as part of the Customer Review
QCS	Includes Quayside Corporate Services Limited, Richard Paffard Consultancy (an organisation affiliated to QCS) and Sandstone Organisation Ltd
Questionnaire meeting	Meeting between a customer and the Bank and/or Professor Griggs before the customer made written submissions to the Customer Review
RM	Relationship manager

RPC	Richard Paffard Consultancy, an organization affiliated to QCS
Skilled person's report	Report into the IAR Fraud under section 166 FSMA
SME	Small and medium sized enterprise
SME Alliance	A stakeholder group formed in 2014 to support businesses affected by bank misconduct
Terms of Reference	Where capitalised, the terms of reference for the Cranston Review
Treasury Select Committee	Parliamentary select committee of the House of Commons covering financial matters
VAT	Value Added Tax