

MEETING OF THE COURT OF DIRECTORS

Wednesday, 11 December 2013

Present:

Sir David Lees, Chairman
The Governor
Mr Bailey, Deputy Governor – Prudential Regulation
Mr Bean, Deputy Governor – Monetary Policy
Mr Cunliffe, Deputy Governor – Financial Stability
Ms Hogg, Chief Operating Officer
Sir Roger Carr
Mr Cohrs
Mr Fried
Mr Frost
Mr Prentis
Lady Rice
Mr Stewart

In attendance:

Ms Hogg, Chief Operating Officer

Secretary:

Mr Footman

1. Minutes – 14 November 2013

The minutes of the meeting on 14 November were approved.

2. Matters Arising

The Governor referred to progress being made under the FSB's guidance to eliminating the "Too-big-to-fail" problem, where the threatened failure of a systemic institution left governments no option but to bail out with public funds. Court had seen the FSB paper to G20 leaders: this reported significant progress but further legislative changes were required in a number of jurisdictions and at the cross-border level. The key task over the next year would be completing the framework for gone-concern loss-absorbing capital. The Governor was chairing an FSB subcommittee to drive this work forward. The tools available for resolving banks were expanding from simple payout-plus-insolvency to include bail-in of creditors. Meanwhile capital positions worldwide were being strengthened.

The Chairman reported that a copy of Matters Reserved to Court have been sent to Mr Tyrie and had also been published on the Bank's website.

It was noted that Court/Oversight Committee would review the roles of the MPC and the FPC in the development of the Sterling Market Facility.

3. **Chairman's Business**

The Chairman asked that the Bank's Health and Safety Report be tabled for Court discussion in February.

Lady Rice reported on the most recent meeting of ARCO. The National Audit Office (NAO) had been present to discuss their approach to auditing the PRA. The NAO had confirmed that this would be a financial audit.

ARCO had reviewed the Quarterly Risk Report – now presented on a cross-enterprise basis – and was content with the assessment.

ARCO had also considered reviews of the Bank's insurance and tax management policies, and the Records Management Review (minute 10 below).

4. **Relationship between ARCo and the PRA Board**

Mr Bailey noted that ARCO was acting as the Audit Committee for the PRA as well as for the rest of the Bank, and PRA Board members attended its meetings. The PRA Board was required to publish separate accounts from the Bank, and had its own statutory responsibilities, but the PRA shared services with the Bank and governance of a number of its control systems lay within the Bank. Consequently a joint approach in ARCO had been agreed. The PRA Board was however signing off the risk and performance reports that were submitted to ARCO and to Court.

5. Executive Report

(i) FSR

The Governor reported on the launch of the November FSR, which followed the FPC's quarterly round of meetings. This drew together a number of strands, most relating to the housing market, and enabled the Bank both to act in a co-ordinated way and also to establish forward plans. The FSR had outlined the Bank's coordinated, graduated, and prudent response to guard against risks to financial stability, including from the housing market, and set out a range of additional steps that the FPC could take in the future but was not activating at present. At the same time, it was announced that the PRA would end its temporary capital relief on new household lending, and that the FLS would be focused only on the support of business lending. This last announcement had been agreed with the MPC, which had been the sponsor of the FLS, and with the Treasury which had joint ownership of the scheme with the Bank. Finally, the FCA had been recommended to consult the FPC on the appropriate interest rate stress to use in assessments of mortgage affordability.

The FSR had also reiterated medium-term policy priorities including the "steady state" capital framework for banks, steps to end "Too-big-to-fail", encouraging market based finance, and identifying risks from shadow banking.

Court noted an exchange of letters with Mr Tyrie on "Help-to-buy".

(ii) FX investigation

The Governor referred to regulatory investigations into apparent attempts by traders to manipulate foreign exchange markets, specifically around the 4.00pm benchmark. It had been suggested that the Bank had been aware of the potential for manipulation and that the matter had been discussed at the meeting of a market committee chaired by the Bank. The Bank initiated in October a full examination of records, with external legal assistance, and Court would be informed of the outcome.

(iii) PRA

Mr Bailey said that the PRA Board had approved the appointment of Lord Blackwell as Chairman of Lloyds Bank Group; and that the Treasury had announced that the PRA would

undertake an investigation into the affairs of the Co-operative Bank and the actions of all relevant authorities, the start of which was subject to any enforcement proceedings.

(iv) Strategic Planning exercise

Ms Hogg said that work was progressing on the Strategic Plan and VfM. The former was about half way through, and an EDCo awayday would be held the following week. Findings of the staff survey conducted as part of the Strategic Plan work stream had been received.

6. Combined Quarterly Reports

(Messrs Coates, Fisher, Hunt and Ms Coffey in attendance)

Mr Coates summarised the financial report: income was likely to be £35mn below budget in the full year to February, mostly reflecting lower than expected FLS scheme participation and expenditure £8mn below budget because of headcount shortfalls especially at the PRA. This assumed that the gaps would be filled relatively quickly. Mr Bailey agreed that the assumption was optimistic. The PRA turnover rate, which had been unusually low at the time of cutover, had moved towards a more normal level (though still below the position at the FSA when he joined it). The Bank needed to recruit on a larger scale than it was used to.

Noting the sizeable underspend against budget in the PRA the Chairman asked about the budget commitment made by the Bank in relation to the PRA. Mr Bailey said that the Bank – and he himself at his confirmation hearing – had undertaken that the PRA would not cost more than the equivalent function as carried out in the FSA. The proviso was that if we gained new functions or activities then we would need to add their costs in as extra. And there were some new functions and activities: for example, ring-fencing, senior persons and licensing, and stress testing on a much more extensive basis. The PRA Board were certainly concerned, particularly about the ability of the PRA to undertake asset quality reviews. One approach was to commission more S166 reports outsourced to “skilled persons” to compensate.

7. **Banknotes**

(Mr Salmon and Ms Cleland in attendance)

(i) Historic characters on Banknotes

With reference to a minute of 17 July, Mr Salmon reported to Court the findings of the Review of the process for selecting historic characters to appear on banknotes. The Review had been conducted with input from other central banks and relevant institutions, and had focussed on the principles that should guide the choice, the process for delivering those principles and the relevance of the Public Sector Equality Duty.

The proposed principles set out more clearly and positively the Bank's aims in using historic characters on its notes.

The new process would involve, for each new note, an initial determination of the field of achievement to be celebrated; a period for public nominations; and a selection committee with external experts to prepare a long list for public consultation and subsequently a short list, from which the Governor would make a selection. There would be professional historical input and arrangements to ensure that the implications of the Equality Act were considered at each stage.

Court APPROVED the proposal.

(ii) Polymer Banknotes

Court noted that the consultation on polymer banknotes had elicited a very positive public response, especially from those who had been given an opportunity to see and handle them. The Bank would therefore proceed with the announcement that the next £5 and £10 banknotes, to be issued in 2016 and 2017, would be printed on polymer substrate. Subject to certain conditions, the sub-committee of Court that had previously been authorised to oversee the next Bank Note printing contract, had given its approval for the project to go ahead.

8. **Projects**

(i) *Collateral Operations*

(Messrs Salmon and Davies in attendance)

With reference to Minutes of July 2011 and November 2012, Court was asked for a further increase, of up to £2.3mn, to complete the project. The previous agreed budget had been £7mn. Functional testing had shown that completion would take longer than previously expected. The worst case for delivery was December 2014, although the central case was three months earlier than that. Given the uncertainty, the budget requested covered the period to December. It was intended to hold a review in the Bank's Project Group in March to decide whether the full funding should be released.

Court approved the extension but subject to holding, at its April meeting, a further review of the Project Group recommendation.

(ii) *Access LAN and Fibre Replacement*

(Mr Finch in attendance)

Court was asked to agree an increase in funding for this project, which replaces the local area networks and fibre estate across the Threadneedle Street building. VAT changes, foreign exchange movements and a previous underestimate of power requirements had driven the cost from £4.58mn to £5.33mn, above the threshold for Court's approval.

Court approved the increased project budget.

9. **Communications Annual Report**

(Mr Blythe in attendance)

Court noted a report from Mr Blythe on Communications. Directors observed that as the Bank's own MI was now highlighting communication as the most significant risk to the Bank and asked how the Communications Strategy was responding.

Mr Blythe emphasised the closer co-ordination between MPC members and the press team, and the increasing public awareness of the FPC and its role. This had reduced the risk of mixed

messages, and helped to promote more co-ordinated presentation of policies, of which the announcements around the November FSR, and the launch of Forward Guidance provided examples.

Court noted that there had been a significant increase in FoI requests over the year to date, partly reflecting the inclusion of the PRA.

10. Records Management Review

(Mr Brown (Internal Auditor) in attendance)

Court noted the management responses to the specific recommendations in the Internal Audit Review, which had been commissioned in response to the Treasury Committees Report on LIBOR (August 2012). These included acceptance of a journaling system for all emails entering and leaving the Bank. This would not be part of the Bank's normal records system, but would be available (and searchable) in the event of any dispute or formal investigation. Staff would still be encouraged to copy significant emails into the main record system.

Mr Brown confirmed that the Review represented his own independent view.

Court agreed that the Review should be published and that progress on its recommendations should be reported to Oversight Committee in the first half of next year.

The meeting of Court was closed.