



BANK OF ENGLAND

News release

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Statement on SFO liquidity auction investigation announcement

The Serious Fraud Office (**SFO**) has announced today that it has closed its investigation into the conduct of liquidity auctions held by the Bank of England during the financial crisis in 2007 and 2008.

The SFO said that after a thorough investigation, it has concluded that there is no evidence of criminality in relation to this matter.

It has been a matter of public record since March 2015 that the SFO was investigating material referred to it by the Bank concerning the Bank's and auction participants' involvement in certain liquidity auctions in 2007 and 2008. The Bank had self-referred this matter to the SFO in November 2014 as the result of an independent inquiry which the Bank itself commissioned in June 2014. The SFO opened an investigation on 16 December 2014. The SFO's decision today takes into account all matters notified to it by the Bank.

The events which the SFO investigated occurred nearly a decade ago. The investigation focused on the conduct and operation of certain of the Bank's liquidity auctions at the height of the financial crisis when a number of systemically-important UK financial institutions were under unprecedented stress. The financial crisis exposed shortcomings in the Bank's frameworks for providing liquidity insurance, operating procedures and governance arrangements. In particular, the relevant Bank frameworks had not been designed to meet the extraordinary needs of markets and intermediaries at that time. They did not define a mechanism to support a banking system facing a sharp reduction in the liquidity of its key asset classes and a shortening in the term of its wholesale funding, and were also unable to stabilise overnight interest rates in these circumstances. This hindered the effectiveness of the Bank's response in the early phase of the crisis, and was overcome only through the commitment of Bank staff to innovate continuously in difficult circumstances to meet the liquidity needs of the banking system more effectively.

The Bank is proud of the dedication and professionalism displayed by its staff during the financial crisis. During the SFO's investigation, the Bank has provided pastoral support to staff involved with the SFO's investigation, and will continue to do so as is necessary.

After the SFO's decision to open an investigation, the Bank moved quickly to establish whether there was any other potential misconduct in any other key market operations during the financial crisis. The Court of Directors of the Bank commissioned a rigorous and comprehensive review of other key market operations during the financial crisis. The extensive review commenced in July 2015 and was conducted over 12 months by the Bank's Legal Directorate, with the assistance of external counsel. The review found no evidence of misconduct by any individual Bank employee. The review resulted in a number of recommendations which the Bank has now implemented. The Bank is today releasing details of the Court-commissioned review and those recommendations.

This review is a recent illustration of the Bank's commitment to greater openness and transparency. The lessons of the crisis and the results of Bank innovation are now embedded in a thoroughly overhauled and comprehensive framework for market operations. The Bank has completed a series of reforms to the Sterling Monetary Framework (**SMF**), including reforms made following an external report on the Bank's framework for providing liquidity to the banking system by Bill Winters in 2012. The Bank has changed the operational design of specific market operations, which has significantly reduced the ability of participants to manipulate Bank operations. For example, auction structures have been changed and the Bank's fee structures for policy operations no longer use submitted reference rates.

The Bank has also improved risk governance arrangements, established an internal Compliance function with a Charter and work programme approved by the Bank's Court of Directors, implemented a Bank-wide Code of Conduct and annual attestation process for staff, adopted a new escalation policy for Bank employees who become aware of information relating to potential improper conduct, and published the Market Intelligence Charter which explains clearly the terms of the Bank's engagement with financial market participants and its rationale for gathering market intelligence.

Since 2013, the Bank has also played a key role in addressing conduct and accountability issues in the wider financial sector. The Bank has worked to help to restore public trust in financial markets through initiatives such as the Fair and Effective Markets Review, engaging with market participants and external stakeholders in the Bank's Open Forum, and with the implementation of the Senior Managers Regime (**SMR**) to strengthen individual accountability and support a change in culture at all levels in banks, building societies and insurers. The Bank has also applied the core principles of the SMR to its own senior management.

Notes to editors:

Investigation into liquidity auctions

Liquidity auctions are a means by which the Bank can provide liquidity to the banking system. In a liquidity auction, the Bank will provide solvent counterparties with highly liquid assets, in sufficient size and at an appropriate term, in exchange for a wide range of collateral assets of good credit quality but lower market

liquidity. The Bank's willingness to provide liquidity insurance contributes to UK financial stability by promoting confidence in the liquidity of individual banks and the banking system as a whole.

Lord Grabiner QC was commissioned in June 2014 to conduct an independent inquiry into certain liquidity auctions which took place during the financial crisis in 2007 and 2008. The background to Lord Grabiner QC's appointment is set out more fully in Anthony Habgood's letter to Andrew Tyrie dated 17 March 2015:

- <https://www.parliament.uk/documents/commons-committees/treasury/150317-Anthony%20Habgood-Liquidity-Auctions.pdf>

Lord Grabiner QC's independent inquiry concluded on 18 November 2014 and the Bank referred the matter to the SFO on 20 November 2014.

The Bank and the SFO's press releases confirming that an investigation was ongoing, dated 4 March 2015, can be found here:

- <http://www.bankofengland.co.uk/publications/Pages/news/2015/037.aspx>
- <https://www.sfo.gov.uk/cases/bank-england-liquidity-auctions/>

The SFO's statement closing its investigation into the Bank's liquidity auctions can be found here:

- www.sfo.gov.uk/2017/06/23/bank-of-england-liquidity-auctions/

Given that the SFO has now completed a thorough and rigorous criminal investigation, it is not appropriate for the Bank to publish any further material.

Reforms to the Bank's market operations and safeguards introduced since the financial crisis

Given the Bank's commitment to openness and transparency and learning lessons from the past, the Bank has implemented a number of reforms in recent years to improve its governance and processes. The Bank has, for example:

- reviewed and introduced improvements to its record-keeping processes (2013);
- put in place a new escalation policy for Bank employees who become aware of information relating to potential improper conduct (2014);
- established an internal Compliance function with a Charter and work programme (2015);
- introduced a Code of Conduct for Bank staff and contractors (2015); and
- published the Market Intelligence Charter, which explains clearly the terms of the Bank's engagement with financial market participants and its rationale for gathering market intelligence, and introduced new training for staff in gathering market intelligence (2015).

These policies can be viewed here:

<http://www.bankofengland.co.uk/about/Pages/humanresources/default.aspx>

The Bank has also played a key role in addressing conduct issues across the financial sector and restoring trust in financial markets through, among other things:

- the Fair and Effective Markets Review, which was a comprehensive and forward-looking assessment of the way wholesale financial markets operate, aimed at helping to restore trust in those markets, and at influencing the international debate on trading practices (2015) (<http://www.bankofengland.co.uk/markets/Pages/fmreview.aspx>);
- the Open Forum, which brought together a wide range of stakeholders from the financial community and wider society aimed at catalysing change in the Fixed Income, Currencies and Commodities markets (2015) (<http://www.bankofengland.co.uk/Pages/openforum/index.aspx>);
- the implementation of the SMR to strengthen individual accountability and support a change in culture at all levels in banks, building societies and insurers, and the Bank has applied the core principles of the SMR to its own senior management team (2016) (<http://www.bankofengland.co.uk/pru/Pages/authorisations/smr/default.aspx>); and
- the UK Money Markets Code and Global FX Code, in which the Bank is playing an important role in setting out standards and best practice in the deposit, repos and securities lending markets, and to establish a single global code of conduct for the wholesale FX market and to promote greater adherence to these standards and principles (2017) (<http://www.bankofengland.co.uk/publications/Pages/news/2017/037.aspx> and <http://www.bankofengland.co.uk/publications/Pages/news/2017/032.aspx>).

The Bank has also completed a series of reforms to the SMF, including those made following an external review of the Bank's operating framework by Bill Winters. This report was commissioned by the Bank's Court of Directors in 2012. In particular, and as noted above, the Bank has changed the operational design of specific market operations, which has significantly reduced the ability of participants to manipulate Bank operations. For example, auction structures have been changed and the Bank's fee structures for policy operations no longer use submitted reference rates.

Notwithstanding the significant improvements and reforms already made, the Bank continues to review the effectiveness of its operations. The creation of the Independent Evaluation Office (**IEO**) in September 2014 was an important initiative of the Bank's 2014 Strategic Plan, and part of the Bank's broader commitment to enhance its openness and accountability. In 2017, the IEO will carry out a further assessment of the Bank's approach to providing sterling liquidity including facets of the Funding for Lending Scheme and SMF governance.

Court-commissioned review

The Bank is today publishing documents relating to the review commissioned by the Court of Directors of the Bank. This was a rigorous and comprehensive review of other key market operations potentially vulnerable to manipulation during the financial crisis. The review was led by the Bank's Legal Directorate, with the assistance of external lawyers, and was conducted from July 2015 to July 2016. The review looked at approximately 100,000 documents relating to 37 liquidity auctions between May 2008 and April 2009. The Bank informed the SFO that it was undertaking this review, the scope of which did not overlap with the matters under investigation by the SFO. The review found no evidence of misconduct by any individual Bank employee.

On the advice of external counsel, the Bank did refer one matter, identified during the review, to the SFO. Between October 2008 and January 2009, the Bank used the discretion available to it under the auction framework then in force to grant one concession to a systemically important institution which was at the time in grave financial difficulty and in receipt of emergency liquidity assistance. As a result, the institution was permitted by the Bank, exercising its discretion, to commit a greater proportion of a class of collateral than envisaged under the standard collateral concentration rules then in force. This enabled the institution to place bids in the relevant auctions for a greater level of funds.¹

The review resulted in a number of recommendations which the Bank has now implemented. These recommendations build on the reforms to the Bank's market operations introduced since the financial crisis as described above. Today, the Bank is releasing:

- [a description of the methodology used to conduct the review;](#)
- [a summary of advice from Jonathan Laidlaw QC, the Bank's external counsel on the review, regarding whether the Bank should refer any matters to the SFO;](#) and
- [a summary of review's recommendations, and an update on the progress and completion of those recommendations.](#)

Legal costs

The Bank co-operated fully with the SFO throughout its investigation. The investigation was extensive and examined events dating back to 2007 and 2008. The SFO made a number of information requests to which the Bank responded comprehensively. In response to the SFO's information requests, from a pool of over 3.5 million Bank documents, more than 111,000 documents were reviewed and approximately 20,000 documents were provided to the SFO.

¹ The SMF Terms and Conditions in effect at October 2008 stated the Bank could amend or vary the Terms and Conditions and Operating Procedures at any time and that that provision might be used, for example, to enable the Bank to respond to a contingency, such as a major operational or financial disruption.
<http://www.bankofengland.co.uk/markets/Documents/money/documentation/080328full.pdf>

This work was led and coordinated within the Bank by the Bank's Legal Directorate, assisted by Travers Smith LLP and Jonathan Laidlaw QC (from March 2015 onwards). The Bank has incurred just over £4.7 million (including VAT) in legal costs in connection with the SFO's investigation. This includes fees of nearly £530,000 (including VAT) for legal advice provided to current and former Bank employees who were interviewed by the SFO as witnesses.

These costs were monitored by the Bank's Legal Directorate on behalf of the Bank's Court of Directors. Each line of each invoice was subject to detailed interrogation. Updates on costs were then provided to the Court of Directors at its meetings to facilitate rigorous and regular oversight. The Court of Directors discussed the investigation on 22 occasions from June 2014 onwards. Outside of these discussions, the General Counsel also provided detailed regular updates to the Chair of the Court of Directors and – separately – to members of the Bank's executive.

The fees incurred by the Bank in connection with the Court-commissioned review were nearly £1.1million (including VAT). Again, these costs were monitored by the Bank's Legal Directorate on behalf of the Court of Directors, with updates provided to the Court of Directors at its meetings.

The fees for the 2014 independent inquiry led by Lord Grabiner QC are set out here:

- <https://www.parliament.uk/documents/commons-committees/treasury/150317-Anthony%20Habgood-Liquidity-Auctions.pdf>

Engagement with the Treasury Select Committee

As the Bank is accountable to Parliament through the Treasury Select Committee, Andrew Tyrie – as the Chair of the Treasury Select Committee at that time – was informed of the Bank's original referral of this matter to the SFO in November 2014 and was kept regularly updated by the Bank during the course of the SFO's investigation up to the prorogation of the previous Parliament in April 2017.