HOUSE OF COMMONS

ORAL EVIDENCE

TAKEN BEFORE THE

TREASURY COMMITTEE

PROJECT VERDE

TUESDAY 29 OCTOBER 2013

BARRY TOOTELL

Evidence heard in Public Questions 486 - 671

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Oral Evidence

Taken before the Treasury Committee

on Tuesday 29 October 2013

Members present:

Mr Andrew Tyrie (Chair)
Mark Garnier
Stewart Hosie
Mr Andrew Love
John Mann
Mr Pat McFadden
Mr Brooks Newmark
Jesse Norman
Mr David Ruffley
John Thurso

Examination of Witness

Witness: **Barry Tootell**, former Chief Executive, Co-operative Banking Group, gave evidence.

Q486 Chair: Good morning, Mr Tootell. Thank you very much for coming to give evidence this morning.
Barry Tootell: Good morning.

Q487 Chair: You were chief financial officer of the Co-op Banking Group, from 2008 to 2011, and then chief executive. Is that right?
Barry Tootell: Indeed.
Chair: You were in a key position of responsibility for the whole of the period that we are looking at?
Barry Tootell: Yes.

Q488 Chair: Would you consider Project Verde to have been yours; that is, something that you primarily had responsibility for?
Barry Tootell: Given the significance of the Verde opportunity, it was, quite rightly, something that the group had a major hand in. The group board, together with the bank board, had concluded that it wished to pursue the opportunity that was represented by Verde.

Q489 Chair: Mr Marks tells us that this was a matter primarily for the bank and not for the group board. Who is right?
Barry Tootell: Mr Marks said it was primarily for the bank to decide whether it was able to complete the transaction. I think Mr Marks also said that he was a driving force behind it as he had the full support of the group board to consider the opportunity.

Q490 Chair: Where does primary responsibility lie for handling Project Verde?
Barry Tootell: Project Verde or the acquisition of a major new business is a matter reserved for the group board. As the shareholder of the banking group, the bank could not

acquire a major new subsidiary or a major new undertaking without the approval of the group board. However, it would be for the bank to decide whether it was able and wished to do the transaction. So primarily the bank, but if the bank wished to pursue the transaction it would have had to have sought approval from the group board.

Q491 Chair: We know the legal position here. We are trying to establish which individuals were driving the attempt to do this deal. Were you one of those?

Barry Tootell: I was, yes.

Q492 Chair: Were you uneasy about the deal?

Barry Tootell: I was concerned at various stages about the economic viability of the transaction, culminating in April 2013 when I recommended to my board and to Peter Marks as group chief executive, that we should not pursue the transaction because of the lack of capital strength to do so. As the group chief executive—given the key strategic importance of this initiative for the group—Peter Marks was also the key driving force behind us exploring the opportunity.

Q493 Chair: So you were uneasy about it at various points?

Barry Tootell: Rightly so. Given the size of the transaction, it would be—

Q494 Chair: When did you first become uneasy?

Barry Tootell: At the end of 2011, beginning 2012, we were going through the consideration of our indicative offer to Lloyds. We were very clear that we had to make this economically viable and we were doing a lot of analysis to make sure that it did do just that, and then, during 2012, we continued to have a debate with Lloyds about the do-ability of the transaction. That is not to say I was concerned and wished to pull the plug on the transaction, but it was quite right that I was concerned that it was the right thing for the group to do and I was challenging of our ability to do just that.

Q495 Chair: Did you discuss your uneasiness with Neville Richardson?

Barry Tootell: No, I did not. Neville had left the business in July 2011.

Q496 Chair: But you said you first had concerns towards the end of 2011. You never discussed it with him?

Barry Tootell: No. Could I just clarify, Chair?

Chair: He never had any influence over your views on this?

Barry Tootell: Absolutely not, no.

But to clarify what I mean there by "concern": concern that it was the right transaction for us to do; concern that we approach it with appropriate diligence to make sure it was the right transaction. That was not a concern that we could not do the transaction in 2011, it was merely a duty of care and detailed diligence over our capability. Concerns did emerge in 2012 about the economics of the business that we were acquiring and the cost of integrating that business into our business, because the bank would have been acquiring the undertakings of the Verde business. Our ability to integrate that, together with the economics of the business that we were acquiring, were a concern at that time and we had those discussions with Lloyds about our lack of willingness to proceed.

Q497 Chair: I understand. One further question. Did you leave of your own accord or were you eased or pushed out? I do not want to question with respect to employment law. I am asking you a question with respect to exchanges that you will have had.

Barry Tootell: That is fine. If I could clarify the terms on which I came into the role in the first place. I was acting chief executive from mid-2011 at the point when Mr Richardson left the business. I was brought into that role to consider whether the transaction of Verde was viable for the group, and then the group would have to decide who the chief executive would be going forward. So in a way I came into the role to assess the Verde transaction. In January 2013, I had a discussion with my chairman, and with my chairman of remco. I said I did not see myself staying on in the role even if we did not do the Verde transaction.

Q498 Chair: You had already decided to go.

Barry Tootell: I had had the conversation in January 2013. I would say the timing of my departure was as much in the hands of the new group chief executive—

Q499 Chair: Just remind us who that conversation was with.

Barry Tootell: I had three conversations. I had a conversation with my chairman in January 2013 about my medium-term future with the business. I had the same conservation at the same time with my chairman of the remuneration committee. Then in early May, after the arrival of the new group chief executive, Euan Sutherland, I had a similar conversation with Euan about his plans and my plans for the future.

Q500 Chair: By the beginning of 2013, you had made up your mind that you were looking to go?

Barry Tootell: At some stage. Yes.

Q501 Chair: I am not pressing this point. I am trying to clarify whether you were pushed out or whether you left on your own accord. You are giving us a very clear steer that you had already made up your mind and you were thinking about this for many months, perhaps up to a year, before you did go.

Barry Tootell: Yes, indeed, and I made that point clear with my chairman.

Q502 Chair: One last point before I hand over questioning to colleagues. In the overview to the Co-op's 2012 financial statement you said, "Our balance sheet remains strong". Were Moody's already in the Co-op by that time, looking at your papers?

Barry Tootell: Neither Moody's nor Fitch were ever in the business looking at our papers.

Q503 Chair: They never asked you for papers? They never asked you for any information in order to do their assessment?

Barry Tootell: Yes. They were not in the business. It is common practice for banks to brief the rating agencies on the—

Chair: I am using that metaphorically.

Barry Tootell: Okay, sorry.

Chair: They obtained briefings.

Barry Tootell: Yes, we had briefed the rating agencies.

Chair: On privileged terms.

Barry Tootell: Indeed.

Q504 Chair: I am asking you whether they were already engaged in those privileged briefings.

Barry Tootell: We had briefed them at the time of the March 2013 announcement of the 2012 results. We had briefed both rating agencies at that time and, when I say the balance sheet was strong, we had—

Q505 Chair: I just want to clarify this role of Moody's. They were already engaged with you at the time that you have said, "Our balance sheet remains strong", or not? That was on 20 March 2013.

Barry Tootell: Indeed.

Chair: They were?

Barry Tootell: They were engaged and they had been engaged for years gone by. This was not an immediate engagement.

Q506 Chair: This is not a continuous engagement by rating agencies, is it? At specific periods when they look at specific questions, they have a heightened level of involvement.

Barry Tootell: They do and they take the—

Chair: We will agree that they do. To say that they were continuously involved could have been misleading, but we have cleared that up.

Barry Tootell: Sorry, if I may clarify?

Chair: They were at a heightened level of engagement at the time?

Barry Tootell: At the time.

Chair: At that time, right.

Barry Tootell: Typically they would meet me and the chief financial officer every six months, and they did so in March 2013.

Q507 Chair: Six weeks later they downgraded you.

Barry Tootell: Indeed.

Q508 Chair: A £1.5 billion capital shortfall was exposed. Is that correct?

Barry Tootell: The £1.5 billion shortfall was announced by the PRA to the markets in June 2013.

Q509 Chair: Yes, so only a few weeks after that. Within a few weeks, not only had you been downgraded but the regulator had also said you needed a lot more capital—a huge amount more capital—bearing in mind your size in relation to your balance sheet, core tier 1. Is that correct?

Barry Tootell: Correct.

Q510 Chair: In retrospect, would you think that saying, "Our balance sheet remains strong" was misleading?

Barry Tootell: We continued to have a 9.2% core tier 1 ratio in March 2013. We had had 9.6% CT1 in year-end 2010 and 2011 from memory, but certainly 2011 was 9.6%. Despite the difficulties the business was facing, in terms of impairment emerging through the P and L and hitting the balance sheet clearly, CT1 remained at 9.2%. We were very careful not to mislead the markets by using words such as "strong' too glibly. Nevertheless, CT1 at 9.2% was regarded as being broadly consistent with the CT1 we had previously had, despite taking the hit.

Q511 Chair: I will quote another line, "The bank's underlying financial strength remains intact". It is a bit difficult to square with a £1.5 billion capital call, isn't it?

Barry Tootell: That was referring to the analysis of the business between core and non-core. If you look into the year-end financial statements, you will see the core profitability of the business remaining at a viable level and the losses essentially emerging out of the non-core business, which is the asset deterioration in the non-core portfolio, together with the one-off hit for the write off of the intangible assets and the provisions for PPI. The underlying business still remained profitable, and that was what that statement referred to.

Q512 Chair: While you say that that remark and the remark that, "The balance sheet remains strong", were carefully thought through—which is what you are telling me now—when you were doing that thinking through, you already had in mind the risk that there might be a downgrade and a need to handle the £1.5 billion capital shortfall. Is that correct?

Barry Tootell: It was, but it was not a £1.5 billion capital shortfall in the way in which the PRA announced it in June. What we had was a future capital requirement, which we had been discussing with the PRA during quarter one of 2013 as a medium-term requirement for us to achieve a certain level of capital for regulatory purposes. That is not a hole in the balance sheet in the year-end 2012. That is a requirement on us to increase our capital on a go-forward basis. At that time, certainly by March 2013, we had announced our intention to sell our general insurance business and we were already in the process of completing the transaction to sell our life and savings business. The capital from both those transactions was to be redeployed into the bank, and that was intended to offset the deteriorating capital base because of the non-core business.

Q513 Chair: You were already well aware of the things that Moody's might find and that the PRA were finding, but you felt that that was consistent with being able to say that your balance sheet remained strong?

Barry Tootell: Yes, but there was nothing for Moody's to find. We had been very open with the regulator and with rating agencies, in terms of the asset quality of the balance sheet. Moody's assessment of our credit rating was based upon their look-forward basis of assessing that asset credit quality and the means by which they thought we would accommodate that, and their judgment was a multi-notch downgrade of the business way beyond that which we anticipated.

Q514 Chair: I know I have asked this question before, but it will strike some as something of a surprise that saying that your balance sheet remained strong was not in any way misleading the market, bearing in mind that you have said you were already fully aware of the concerns that led to the £1.5 billion capital shortfall at the time that you made it.

Barry Tootell: We were comfortable with that statement, yes.

Q515 Mr Newmark: That flows into the questions I want to ask you. You are a qualified person with respect to a financial services business. On the one hand you are saying you went out to the market and you said, "Yes, our balance sheet is okay", when clearly you were holed below the waterline in some way. I am curious, did you rely a lot on your accountants to make that judgment call, or where did that judgment call come from in terms of saying, "Our balance sheet is okay", when subsequently it was not?

Barry Tootell: The point refers to the balance sheet 9.2 status, which is the ratio of our core equity to our risk-weighted assets.

Q516 Mr Newmark: No, I understand that. But clearly there was a problem though, right?

Barry Tootell: There was a problem that we were addressing. This is the requirement for us to increase our capital still further, which we were doing, by divesting other aspects of our business within the broader Co-operative Banking Group and redeploying it into the bank to face off against what we saw as the deteriorating capital base in the underlying non-core business.

Q517 Mr Newmark: Who were your accountants at the time?
Barry Tootell: Our auditors were KPMG.

Q518 Mr Newmark: What feedback were you getting from them to give you the confidence to come out and say what you said with respect to your balance sheet? I don't want to tread on Mr Love's territory, but I am just curious.
Barry Tootell: Extensive discussion in terms of the wording of the statutory accounts for the year-end 2012. That review takes place within my finance community, in dialogue with the auditors, ultimately into the audit committee and to the board itself. It is a board statutory account approval process.

Q519 Mr Newmark: With the benefit of hindsight, do you think their advice in the end was a little dodgy or not at all?
Barry Tootell: No, there was discussion around the appropriateness of wording, as there always is in any statutory accounts process. We were comfortable that that statement, together with the plans that we had in place, was appropriate to address the go-forward capital requirements of the business. As I say, it reflects the fact that we had a 9.2% core tier 1 ratio for the year ended—
Mr Newmark: You keep repeating that.
Barry Tootell: It is very appropriate for the accounts that we were commenting upon.

Q520 Mr Newmark: But from the market's perspective, it did not subsequently address the fact that you had a huge problem with your balance sheet. No?
Barry Tootell: There is a difference between the year-end statutory accounts and the regulatory requirements that we had for the future that we were doing something about.

Q521 Mr Newmark: Neville Richardson's written evidence suggests that, in May 2008, Britannia was approached by David Anderson, chief executive officer of Co-op Financial Services, to broach the subject of a merger between the two organisations. Is this your recollection, namely that the Co-op was the activist partner in seeking a merger?
Barry Tootell: I know Mr Richardson has said that. My first recollection or awareness of the opportunity to acquire the Britannia business was David Anderson announcing to our executive committee that he had had a discussion with Neville. I honestly do not know who approached who.

Q522 Mr Newmark: Do you think that he was the driving force behind the merger or who was?
Barry Tootell: I think both parties were keen to explore the opportunity that the merger or the acquisition presented. I honestly don't know whether Neville approached David or vice versa.

Q523 Mr Newmark: In board minutes there was nothing in there giving any sense of which direction the pressure was coming from?
Barry Tootell: We could check, but I am not aware of such.

Q524 Mr Newmark: What was the rationale from the Co-op's perspective of seeking to merge with Britannia?

Barry Tootell: We were a £15 billion banking business with only 90 branches and, therefore, subscale in distribution reach, and subscale in balance sheet size in order to serve our customers and our members better. It was always the intention of the business to seek to expand its reach to our customers. Therefore, the 250-branch network of Britannia was of significant interest to us because it would broaden and deepen our reach within the UK. In addition to that, we were a clearing bank, but we had a relatively small savings and mortgage business, yet Britannia complementarily had a very significant mortgage and savings presence.

Q525 Mr Newmark: You reckoned between the two management teams you had the management depth to make sure that was all integrated and everything fine?

Barry Tootell: Indeed.

Q526 Mr Newmark: Who else within the Co-op was pushing for a merger between the two organisations, and was the group or the bank pushing more strongly for a merger?

Barry Tootell: It was an interesting opportunity that was presented to us. We were not trawling the market looking for targets. I believe it was through David Anderson's previous relationships with chief executives of building societies, given that he used to be the chief executive of the Yorkshire Building Society—so he knew many of his counterparties in the industry on the mutual side—that that meeting came about. It was not because we were searching for a target and who within our business was supportive—

Q527 Mr Newmark: It sounds like Mr Anderson was the one pushing a little bit more, in that it is sort of implicit from what you say.

Barry Tootell: I could not say. I am suggesting that they knew each other through that relationship.

Q528 Mr Newmark: No, I know that element of a relationship. We all know loads of people. But somebody is taking a more activist approach. I am trying to get to understand who was taking the more activist approach in this.

Barry Tootell: I am sorry, I could not comment. I don't know who was driving more so than the other. My understanding at the time was that both parties were keen to explore the opportunity.

Q529 Mr Newmark: Right. But they did not suddenly wake up one morning, each independently, and say, "Gee, it would be a great idea if we got together". Somebody must have approached one or the other.

Barry Tootell: Indeed, one of them must have made the first contact.

Mr Newmark: So who was it?

Barry Tootell: I don't know the answer to your question, I am afraid.

Mr Newmark: Come on. Okay, fine.

Chair: Are you sure about that?

Barry Tootell: Yes. I would have told you, Chairman, if I had known the answer.

Chair: Okay.

Mr Newmark: It would be interesting to see if there were any board minutes or anything.

Barry Tootell: Indeed.

Q530 Mr Newmark: I will let Mr Chairman figure out if we can get hold of those. Peter Marks told us that, while he voted for the Britannia deal as a non-executive director, he was not driving the Britannia deal. Is that the case and, if so, what does it say about group oversight of the activities of the bank?

Barry Tootell: At the time, the governance structure of the business was a little different. David Anderson did not have a direct reporting line to Peter Marks and Peter Marks was not as involved in the banking group business as he has been for probably the past two or three years. Yes, David Anderson was the driver of the transaction from within the banking group or from within the Co-operative group. You are right with your summary of the situation, which was that Peter Marks was supportive of the transaction as a non-executive of the bank. Indeed, he spoke in favour of the transaction, in his capacity as the group chief executive, in the group board meeting that finally made the decision to progress the transaction.

Q531 Mr Newmark: But based on information that he received during the board meetings as opposed to any other ambitions for the group or anything like that?

Barry Tootell: Indeed.

Q532 Mr Newmark: Or did it tie in with his ambitions for the group?

Barry Tootell: Strategically, it was the right thing for the banking group, and he supported it for that reason. He was not involved in detailed day-to-day conversations with David Anderson that I am aware of, in the way that he has been more recently with me in the context of the Verde transaction.

Q533 Mr Newmark: You would not say that, once he was sold on the idea, he was championing the deal in any particular way internally?

Barry Tootell: No.

Q534 Mr Newmark: How did Britannia react to the approach from the Co-op?

Barry Tootell: Again, I do not know whether Co-op approached Britannia. How did Britannia react to the opportunity? They were optimistic about completing the transaction and, again, from their point of view they thought that it was a very complementary transaction. If I look now at the Britannia business, what didn’t they have that they would benefit from by a transaction with the Co-operative? They did not have bank clearing capability. They did not have internet capability. They did not have the general insurance and life assurance manufacturing capability that we had. So the complementary nature of the transaction was appealing to both parties.

Q535 Mr Newmark: It might have been complementary, but do you think it was more of a rescue operation of Britannia or was it a merger of some sort of equals in your view?

Barry Tootell: An incredibly interesting question in the context of what we have seen happen over the past years with hindsight, but, no, at the time—

Q536 Mr Newmark: You thought it was a merger of equals, not a rescue operation?

Barry Tootell: We were very clear to make that sort of comment to the marketplace, and we genuinely believed that from within the bank and in all the discussions that we had with Britannia. There was no sense from Britannia or from our business that this was a rescue of Britannia. It was never discussed in our boardroom, and to my knowledge was never discussed in the Britannia boardroom and never discussed between parties and never discussed with the regulators. This was a bringing together of two businesses that were complementary.

Q537 Mr Newmark: In putting the two businesses together, there was nobody internally saying, “This is not a merger of equals; these guys could be in a bit of trouble here and we have leverage in this merger”? It was truly a sense of the merger of equals?

Barry Tootell: No.

Mr Newmark: No? Yes?

Barry Tootell: No as in, no, we did not think that.

Mr Newmark: No, you didn’t see it.

Barry Tootell: The only comment to that end is a comment made in the final group board meeting, when one of the directors noted, “Perhaps Britannia need this a little bit more than we do”. Apart from that passing comment, there was never any discussion.

Q538 Mr Newmark: I am curious, what led that person to make that comment?

Barry Tootell: Just the assessment of the relative capital strength of each business. Capital was slightly more constrained at Britannia, because at the time the FSA was encouraging them to improve their capital planning capability and was asking them to hold back capital because of that. So they were slightly more constrained. That was an issue that was removed on acquisition or merger because, under our capital planning oversight and stewardship, that capital planning issue was waived by the FSA. In standalone terms, perhaps Britannia needed the transaction slightly more because they were slightly more constrained, but this was never ever discussed as a rescue in any way, shape or form within the business.

Q539 Mr Newmark: So there was no pressure from the regulatory authorities or even the Government to encourage this—I view it as a rescue operation of Britannia—merger with Britannia? There was no pressure from either the regulator or the Government to do this?

Barry Tootell: Not at all to my knowledge. I did not have any such conversations with regulators or Government.

Q540 Mr Love: I draw the Committee’s attention to my designation as a Labour and Co-operative Member of Parliament. Mr Tootell, what role did you play in the due diligence that the Co-op conducted on Britannia?

Barry Tootell: The due diligence was undertaken under my area of responsibility as a CFO. It was undertaken by KPMG working with my risk officer who reported directly to me, so it was my responsibility.

Q541 Mr Love: When he appeared before the Committee, Peter Marks told us that the Co-operative Bank had relied very heavily on the fair value and due diligence work that was done on its behalf by KPMG. Would you agree with that statement and do you think you were overly reliant on the advice and work undertaken by KPMG?

Barry Tootell: That is a very interesting question, again, with the benefit of hindsight. If I refer to even more recent publications from the Parliamentary Commission on Banking Standards, which has a real focus on responsibility of officers and directors. I take responsibility for the due diligence that we had undertaken. I do not blame KPMG for any retrospective view of the shortfall in that due diligence work. Yes, we took comfort from it, but I do not believe that management abdicates responsibility by engaging consultants or advisers to assist them in their work. So, yes, we did take comfort from the KPMG work—

just as I took comfort from the work that my risk team and my finance team had done—but ultimately it was the board's decision to do the transaction based on that input.

If I could just comment for a moment, Chairman, on the content of that work or the timeframe within which that work was done. This was done in late 2008, when the level of arrears in the Britannia business was relatively low. We identified the areas of risk within the Britannia business and, notably, they were the non-conforming, self-certified mortgage books in the platform intermediary portfolio, together with the distressed books that they had acquired from General Motors or GMAC, together with the level of exposure that may sit within the corporate book. We made sure that we focused on those areas when we did the due diligence work and we assessed them based on our understanding of those areas. We stressed them based on our future economic outlook for the UK economy.

That future economic outlook accorded with Bank of England publications at the time in terms of where we as a UK economy thought the economy was going. The board assessed that and took comfort from that and, even in the board meeting where we finally made the decision to proceed with the transaction in January 2009, there was commendation for KPMG and the due diligence work by JP Morgan, for the thoroughness of the due diligence, the rigour within which we assessed the stress areas of the book and the capital planning of the business.

I look back with the benefit of hindsight and think that we have had a lot more credit risk exposure from the Britannia business than we ever thought possible. At the time we genuinely thought we had put appropriate fair value in place to protect ourselves. We put almost £700 million of fair value in place beyond that which the auditors of Britannia—which is PwC—and the Britannia management and board felt appropriate, based on their provisioning work that they would have done in the natural course of business. We put an additional £700 million away. With the benefit of hindsight, that has proved not to be enough. Do I think that KPMG let me down at that time? My personal view is, no, they did not. Based upon the economic circumstance at the time, I think they did a very, very thorough high-quality job that I took comfort from, as the chief financial officer, as did my board.

Q542 Mr Love: We will come to the emergence of impairments in a moment, but let me ask you this. You mentioned all the risky aspects of the Britannia balance sheet. I understand KPMG did all the work in projecting various scenarios, but did they throw up any concern that the level of risky assets on their balance sheet might cause problems in difficult economic circumstances?

Barry Tootell: Yes, because otherwise we would not have put £700 million of fair value protection aside to protect ourselves. They did not raise issues beyond that which we could afford within the capital plan for the combined business and, therefore, the business was a viable and attractive proposition for the Co-operative business. They raised several areas that were insightful and helpful to management in considering the transaction.

Interestingly, with all that we have seen more recently in terms of the emergence of significant losses from the non-core business of the Co-operative, which almost exclusively contains the Britannia assets—there is some Co-operative asset in there, but it is mainly Britannia assets—much of that exposure that has come out in 2012 and 2013 has related to the corporate business and not the intermediary business. At the time, we were much more concerned about the intermediary business and we did extensive work on that. That is not to say that we did not look at the corporate business, but that was not the major area of concern at the time. It was the intermediary business that was the major focus for us.

Q543 Mr Love: Who do you hold responsible for not looking at what turned out to be a very risky area? Do you accept responsibility yourself on behalf of the Co-op Bank or should KPMG, carrying out their functions as regards the due diligence, have thrown this up as a possible problem area? What I am trying to get to is that you accept that KPMG did the best it could. I am trying to figure out how reliant the Co-op was on the judgments made by KPMG in the negotiations over the merger with Britannia. That is what Peter Marks said, but you seem to be suggesting that the responsibility lay with the Co-op, rather than the advice given by KPMG.

Barry Tootell: To be clear, we did not blindly make a decision based upon the evidence of KPMG. We took comfort from KPMG's input to us. If I look back, do I take responsibility? I take responsibility as the CFO, with oversight of the due diligence process, for the support I gave to my chief executive and my board in an important decision. I took comfort, as my board took comfort, from the support of advisers. Do I look back and think of the economic circumstance at the time, and do I think that they missed something? They were working on the basis of economic projections that were consistent with Bank of England and market consensus; they were doing that assessment of the business only three or four months after the FSA conducted a supervisory review of Britannia and reaffirmed, give or take, a £30 million or £40 million—I think it was from memory—increase in their capital requirement. Broadly speaking, the FSA reaffirmed the capital requirements of Britannia, having done a thorough supervisory review process. As I say, we and KPMG did a review of the risk areas of Britannia, based upon current and stressed economic projections. I can think of no individual or committee or board or firm—in the sense of KPMG—that did not exercise the utmost professional care in pursuing what was an important transaction for the group. Were we right in hindsight? Self-evidently, no. As we have seen over the past three years, the level of losses from that business far exceeds that which we reasonably thought could come to pass.

Chair: We are going to move on, Andy. One very last quick question and a quick reply, please.

Q544 Mr Love: One last question. It is in relation to KPMG as auditor, which has very specific responsibilities. How important a role do KPMG have in relation to the statements that have been made through this recent period, where you have gone from having limited impairments to having significant impairments and a deterioration in the capital position? Did KPMG authorise all the statements that were made or did they advise that these statements might be inappropriate at any particular time?

Barry Tootell: No, we had no disagreement with KPMG in terms of our published financial statements.

Q545 Mr Love: As the auditor, they approved all the statements that were made?

Barry Tootell: Yes, they did. It is not really for them to approve, it is for the board of the business to approve. It is not for the auditors to approve, but they gave appropriate confirmation to the shareholders and the directors as a combination of their audit work on the accounts.

Q546 Mr Love: There were no discussions that the statements might be misleading the market from your auditors, KPMG?

Barry Tootell: No.

Q547 Jesse Norman: Mr Tootell, I am grateful for the clarity of your responses so far, thank you.

So KPMG were the auditors to the Co-op at the time of the Britannia transaction, PwC were the auditors to Britannia. Can you remind us who your financial advisers were?

Barry Tootell: The financial advisers for the transaction on the Co-op side were JP Morgan.

Q548 Jesse Norman: Yes, and who on the Britannia side?
Barry Tootell: I believe it was Citigroup.

Q549 Jesse Norman: Very quickly, what were the terms of the merger?
Barry Tootell: The terms of the merger were a zero consideration transaction. There was no payment made.

Q550 Jesse Norman: From the point of view of if you were a Britannia mutual member and you became a mutual member of the enlarged whole; if you were a Co-op member, you became a Co-op member of the enlarged whole, there was no other form of recognition of value as between the two groups?
Barry Tootell: Interesting perspective then, because members of the Co-operative are not members of the banking business. They are members of the group, so—

Q551 Jesse Norman: Yes, but you had that exposure to the banking business through the Co-op.
Barry Tootell: Indeed, but the Co-operative members do not become a member of the enlarged business. They remain members of the Co-operative Group. We enabled and accelerated a process by which all members of Britannia—and bear in mind that not all customers of Britannia were members of Britannia—were to become members of the Co-operative movement on an accelerated basis. The terms of paying a dividend to members was different from a Co-operative versus a Britannia. It was not a dividend in the Britannia world, but as a mutual they paid something called a Britannia Membership Reward, BMR. What we did was accommodate the members of Britannia with a transitional arrangement whereby we would enable them to earn a dividend within the Co-operative movement, which was no less than they would have otherwise earned as a member of Britannia. That was the only concession made.

Q552 Jesse Norman: From your point of view then, this has been a disaster from the Co-op members' side, because they have had an exposure to a Britannia book that has turned out to be vastly worse than anyone could have anticipated. Britannia members have done remarkably well, because they have come into the Co-op Group as accelerated mutual members of the whole. Is that right?
Barry Tootell: Yes, in broad terms.

Q553 Jesse Norman: Because otherwise the Britannia members would have been forced to have the share of their own mutual. They would have had to bear the full value of the £1.5 billion shortfall that we found in the Britannia balance sheet.
Barry Tootell: Yes. In hindsight, I find it hard to envisage what the future of the Britannia business would have looked like on the emergence of the losses from its commercial book, as we have now seen it. Then again, in isolation, neither can I predict what the management of Britannia would have done to accommodate that emerging issue.

Q554 Jesse Norman: But it is a reasonable assumption that Britannia would have been wiped out if it discovered the size of this without the capital strength of the Co-op to keep it afloat?

Barry Tootell: Or they would have sought other means of addressing their issues. If I may just diverge for one second, Chairman—

Jesse Norman: Very quickly, if you do not mind, because I have a very short period of time to ask questions.

Barry Tootell: If I look at what has caused the demise of the Co-operative business in the here and now, it has essentially come out of two major things, one of which is the cost of redress on PPI, together with the asset decline of the business, and a significant part of that is the non-core assets that I have discussed.

In terms of our means of accommodating those issues, there are two means available to a business. It is either to generate profits to increase retained earnings and, therefore, capital, or to raise new capital. As a co-operative, we cannot generate new capital because we do not have market access in the way others do. Interestingly, taking you back to the Britannia analysis, a building society does have market access because it can—as Nationwide has announced this year—issue CCDS as a means of raising capital. That is not available to the Co-operative.

Q555 Jesse Norman: Therefore, if anything, the Co-op board—both the board of Co-op Financial Services and the board of Co-op Group—was under a special obligation to ensure that there was nothing bad about the Britannia assets because they had limited other recourse to raising other forms of capital?

Barry Tootell: Yes. We have seen that the model of the Co-operative is very conservative, notwithstanding what you see as being the difficulties the business has just faced here and now, partly because of that, because it cannot raise capital.

Chair: Not conservative enough, though.

Jesse Norman: It is conservative enough to have been wiped out by this incautious acquisition.

Chair: Yes, exactly.

Q556 Jesse Norman: Mr Tootell, Neville Richardson stated to us that he opposed proceeding with the Verde transaction in July 2011. He said mounting pressures were facing CFS, putting it at unacceptable risk because the merger had not achieved full integration. Is that your recollection of events?

Barry Tootell: It was one of the transitional programmes that we would have to face as a business. Neville's main debate with the board—and I think he is on record in this Committee—was the Unity programme, but the Verde opportunity would have been yet another transitional or change programme that we would have had to face.

Q557 Jesse Norman: Did you share Mr Richardson's position that this was the right deal at the wrong time?

Barry Tootell: We had undoubtedly been busy, to say the least, considering the Verde opportunity, in and among managing the BAU business.

Q558 Jesse Norman: So you were being massively stretched at that time?

Barry Tootell: We were stretched, but that did not stop us doing the right thing by the business and at the same time considering the opportunity, and at the same time embracing the Unity programme.

Q559 Jesse Norman: Did he express concerns to you at the time about the Verde transaction and the Unity transaction?

Barry Tootell: We had no extensive debate on the Verde opportunity at that time. It was an interesting opportunity, which, by the time that Neville left the business; we had done very limited work on Verde. The main debate—and indeed, Neville is correct with what he said to this Committee—that he had in the boardroom was with regard to the Unity programme rather than Verde.

Q560 Jesse Norman: But he is overstating the concerns he had when he spoke to us about the concerns he had and was presenting to the board. He has overstated it, is that what is happening?

Barry Tootell: No, he mentioned both matters in this Committee room and he mentioned both matters in the boardroom, but of the two, his major area of concern was the Unity programme, at the same time as completing the integration of the Britannia business and commencing or completing the IT transformation programme.

Q561 Jesse Norman: But the point is you supported the Verde bid yourself?

Barry Tootell: Yes.

Q562 Jesse Norman: So you were in disagreement with your chief executive?

Barry Tootell: Yes.

Q563 Jesse Norman: That is why, when he presented his concerns to Peter Marks, he had to go, because he was not supported by his own management team and Peter Marks was driving the transaction from within group?

Chair: Is that correct?

Barry Tootell: I cannot speak to why he left the business because I was not in the boardroom when that debate was had by the board, at either the banking group board level or the group board level. I would not suggest—to repeat your words, Mr Norman—that he had to go because he did not have the support of management. I think Neville's own evidence to this Committee was that he left because he was in disagreement with the board in terms of strategic direction.

Q564 Jesse Norman: Right, but you then became chief executive, you disagreed, and you backed the bid. He did not have the support of his own chief financial officer. He was the man who had come with Britannia. You had been at the CIS before that. The Co-operative is deciding to reject this person who is not agreeing with their strategy.

Barry Tootell: It was not part of the debate as to Neville's departure from the business.

Q565 Jesse Norman: Was it your understanding that he stepped down because the CEO and the board of the Co-op Group did not accept his warnings about this transaction or Project Unity?

Barry Tootell: I do not wish to be pedantic, but I would reverse that sentence and put much more emphasis on Unity. The debate was not a severe disagreement on Verde. There was a much more severe disagreement on the ability of the bank to embrace Project Unity, but Verde was presented as another example of stretch and working on many fronts that Neville talked about.

Q566 Jesse Norman: A final question. You complete the transaction, by which the Co-op merges with Britannia in April 2009. By that time, you have already seen not merely the collapse of Northern Rock, but the disastrous results of the Lloyds/HBOS merger, which came out in February 2009. It now turns out that the assets you acquired were grievously compromised, to the extent that, had it continued with them, Britannia would almost certainly have been wiped out and had to seek some kind of emergency financing or partnership. Do you not feel that the writing was absolutely on the wall at that time? The combination of decline in the economy and decline in the financial sector, and the specific examples of the wreckage of HBOS and Northern Rock, should have given you pause as to the quality of the assets that you were acquiring?

Barry Tootell: You are absolutely correct to suggest that it gave us pause. Interesting insight, we were the clearing bank for Northern Rock, so we were unique in the UK marketplace in seeing just what happens with a run on a bank, so we understood exactly what that felt like.

Q567 Jesse Norman: Sorry, I am being delicate about it. It should have given you screaming cause for concern. You are responsible for this transaction and you are acquiring a bunch of assets while the asset quality all around you is being degraded visibly in front of you. Why don't you act on it? Why don't you call off the transaction and preserve that £1.5 billion of your mutual members' capital?

Barry Tootell: That would suggest then that no bank should do a transaction, as opposed to, if you are going to do a transaction, you make jolly sure that you do appropriate levels of due diligence to protect yourselves. We genuinely thought we had done the latter. We were absolutely aware of the consequences of hurried due diligence, and that was what the market perceived to be the issue with the Lloyds/HBOS transaction—there was not enough due diligence done on the HBOS assets. We genuinely thought we had done extensive due diligence.

As I say, it was commended in our boardroom in January 2009 just how much quality due diligence we had done. In Northern Rock's case, that was the consequences on liquidity management of a run on a bank and we were clearing that bank. We understood explicitly what that felt like and, again, modelled that extensively.

Q568 Mark Garnier: Can I take you to December 2012, when António Horta-Osório of Lloyds Bank told us that he first identified this capital shortfall with the Co-op, and he approached the Co-op to discuss their concerns about this. Peter Marks says he remembers the approach but does not remember any details of the conversation, and he also tells us that it was you who carried on these conversations with Lloyds Bank. Can you give us a flavour of what was going on in those conversations at the time?

Barry Tootell: Okay. I do not believe he said it was me who had that conversation, but I do recollect the conversations.

Q569 Mark Garnier: This is Peter Marks last week, "Barry Tootell, who was the chief executive of the bank and who I believe will be here next week, was the main person supervising the day-to-day running of the process".

Barry Tootell: Indeed, but that does not mean that I had the meeting. Let me tell you what happened. Peter was right in his suggestion that the meeting was not with him. We completed a three-year planning exercise that went through our board in November 2012, in which we projected forward the level of arrears that we were seeing emerging from our non-core portfolio. We had had a discussion with the regulator in late 2012 to suggest that the capital requirements for our bank were likely to increase. From that meeting, we imputed how much that might be. They did not give us a number at that stage, but we built that into our planning process.

Q570 Mark Garnier: How much did you think at the time? Were you identifying this £1.5 billion?

Barry Tootell: For me to answer that with specifics, I am going to have to disclose the internal capital guidance and capital planning buffer of the bank, which is market sensitive and a very private factor between the regulator and each individual regulated bank.

Q571 Mark Garnier: I will not press you. Presumably we should not press for market-sensitive information, should we, Chairman?

Chair: I cannot ask you for something that is still market sensitive.

Barry Tootell: Let me try to give you an answer that is more helpful.

Q572 Mark Garnier: What I am trying to find out is, at that point, did you know that you had a £1.5 billion potential shortfall in your budget?

Barry Tootell: No, we did not.

Q573 Mark Garnier: But Lloyds were beginning to come to this conclusion themselves?

Barry Tootell: To be clear, because we had an earlier discussion with the regulator and because we were seeing in 2012 a greater level of impairment from our non-core book, predominantly corporate, together with continuing provision for PPI, we were looking at a capital position for the bank that was tighter than it had been previously. We factored that into the plan. We rolled it forward appropriately, and we shared that with Lloyds on an open basis after the board had approved that in November 2012. So Mr Horta-Osório did not discover that we were having greater difficulty on capital; we shared it with António and his team.

As he has suggested to the Committee, he came back via one of his senior managers to one of my senior managers, who were the nominated people to have active, ongoing day-to-day dialogue on the deal. They raised their concerns. Why was that not a point at which we raised the flag and pulled the plug on the deal? It wasn't the appropriate time because we had a plan that suggested capital was tighter, and this brings me back to the point on the strong capital position in the year-end accounts. We had a capital plan that looked like capital was tighter and below the risk appetite of our own board, and clearly therefore not where we wished to be for the future, but we had plans to address it.

We were then determining the possibility of selling our general insurance business. We were already in the process of selling our life business, and we had committed in that planning process to deleverage more aggressively the corporate portfolio. Those three things gave us a capital position that would still make the deal viable; otherwise we would have pulled the plug on the deal. That was the emerging position that we shared with Lloyds in December 2012 that they raised their concerns about.

Q574 Mark Garnier: So Operation Pennine now became key. If I remember, this was a way to look at raising more capital. Operation Pennine was now key to this deal, going forward. I am trying to get a flavour of the dynamics that were going on, because certainly the impression that we have been getting in this Committee from the evidence so far is that it was Lloyds approaching you to say they were uncertain that you could go ahead with this deal and that absolutely the dynamics were that they were initiating this conversation. Now it sounds as if you are suggesting that that was not quite the case. It was a two-way dialogue and you were saying, subject to Pennine going ahead, that things were going to be fine, you as an organisation were less strong than they perhaps originally thought but, nonetheless, you were still strong enough to go ahead with it.

Barry Tootell: Indeed. Believe me, we were doing a lot of work to ensure that we were strong enough to operate on a day-to-day basis as well as undertake a transaction with the significance of Verde. We did not leap into action because Lloyds prodded us to do so. We were already working extensively on the capital plans to bring our capital to a position that the board had set as its risk appetite for the future.

Q575 Mark Garnier: You were telling the regulator about your findings as well?

Barry Tootell: Gosh, yes, the regulator was completely engaged.

Q576 Mark Garnier: What were they saying to you about this? Were they comfortable with what you were doing? Did they agree you had a problem? Did they say, "Don't worry, chaps. They are doing fine"?

Barry Tootell: They agreed we had a capital position to be worked upon. Andrew Bailey—apologies, I forget whether it was his evidence to the Committee or whether it was his written letter more recently—said that he had never approved the transaction. Indeed, they did not. They were never asked to approve the transaction, but they were consulted on our progress towards pursuing the transaction on a very, very regular basis, both in terms of the transaction itself but also in terms of our underlying capital planning for the underlying standalone business, so extensive conversations with them. Each of those conversations continued to reaffirm that the regulator was open-minded about considering the opportunity of Verde, provided we were putting in place the capital plan that would make that feasible.

In 2011, Andrew Bailey came to our boardroom and set out the things that he would expect us to address. That was in a letter to me I think in November/December 2011, reaffirmed in writing, and they were the things that the Committee went through in the weeks gone by. One of those was capital adequacy. Clearly, we had to maintain a level of underlying capital that demonstrated our strength as a bank before we continued to assess the transaction that was Verde. I am sorry, but a weak bank does not do a transaction like Lloyds in order to make itself a bit stronger. A weak bank that is a bit stronger is still a weak bank and, therefore, we were committed as a board that we would not consider the transaction unless we could convince ourselves that we had the adequate underlying capital strength to do so. Our board was very, very clear on that.

Q577 Mark Garnier: Did Lloyds interpret your financial modelling differently from the way you did?

Barry Tootell: I do not believe so. I never had such a conversation, nor am I aware of such a conversation with Lloyds.

Q578 Mark Garnier: It is quite an important point. You thought things were okay to go ahead and they did not at that time?

Barry Tootell: We had not shared with them the detailed options that we were considering, such as the general insurance disposal and so on, because that would have been market-sensitive information. We had shared more of an underlying plan without some of the remediating actions that we were considering.

Q579 Mark Garnier: Let us be clear about this. Lloyds were not aware that you were looking to sell the insurance services in this December 2012 conversation?

Barry Tootell: I do not believe so.

Q580 Mark Garnier: So at that point they were highlighting the fact that they did not think this deal could go ahead and they were seriously worried about it?

Barry Tootell: The choice of words is slightly different to the reality at the time. They wanted more information from us to evidence why we thought the capital of the combined business, and standalone, was appropriate.

Q581 Mark Garnier: This is not including the fundraising from Operation Pennine?

Barry Tootell: Yes. Project Pennine was not in progress at that time. There were certain events in 2013 that precipitated me establishing Project Pennine, which I can come on to if the Committee wishes me to.

Q582 Mark Garnier: I am still slightly confused by this. At the time of these conversations with Lloyds, you were not proposing to raise any money from the sale of the insurance services and the other stuff?

Barry Tootell: Yes, we were. That was in our plan.

Q583 Mark Garnier: That was in your plan, but you did not tell Lloyds about that?

Barry Tootell: I would have to check. I do not believe we did. The plan was presented in two parts. One was the underlying plan and then the mitigating actions and I don't think we shared the full detail of the mitigating actions with Lloyds. We shared the underlying planning assumption, the roll-forward of our business into the future, and on that basis the capital would have looked weaker without remediation.

Q584 Mark Garnier: The remediation was selling the insurance services, that which then became known as Project Pennine?

Barry Tootell: There were three primary remediation points. One was deleveraging the corporate asset by taking risk-weighted assets off the balance sheet; secondly, it was selling the general insurance business; and thirdly, it was completing the life and savings sale. The L&S—life and savings—and general insurance sales would have allowed our parent company, which is Co-op Banking Group, to inject capital into the bank.

Q585 Mark Garnier: When you had the conversation with Lloyds, was there an assumption that you were going to inject? Were Lloyds aware that there was going to be an injection of capital one way or the other into the bank?

Barry Tootell: As I say, I do not recollect whether we told them about those remediating actions in December.

Q586 Mark Garnier: This is very, very important. There is an awful lot of sort of corporate amnesia about this. Having spoken to Peter Marks last week, he was amazingly—

Chair: Amnesiac.

Mark Garnier: Amnesiac, thank you, Chairman. I am slightly worried that this is catching among the board of Co-op, so I am going to press you on this. It is really important: did Lloyds know full well that there was going to be a capital injection or not? You must be clear about this.

Barry Tootell: I am sorry, I do not recollect, and I think your challenge is a little unfair.

Mark Garnier: I think it is very fair.

Barry Tootell: I have been extremely open with the Committee but—

Q587 Mark Garnier: This is the difference between a deal going ahead and not going ahead. This is the difference between a bank being solvent and effectively not being solvent. This is very, very important stuff. I genuinely cannot believe that you would forget the importance of that conversation at the time.

Barry Tootell: This was not a major milestone in the negotiation or the engagement of Lloyds.

Mark Garnier: Really? It was not a major milestone?

Barry Tootell: This was an ongoing sharing of information with Lloyds, an iteration. In the iteration that we shared with them in December, "There will be a level of capital, which is not an insolvent bank but is a bank that requires additional capital". The comment to Lloyds was, "and we are working on that" and we were continuing to do just that.

Q588 Mark Garnier: Can I summarise how this is coming over? So you run a full projection model and you realise that you have a problem with your bank. Part of your process of resolving that is to sell off a couple of assets and then inject capital into that bank. You have a general conversation with Lloyds. Lloyds say they initiated it but you say it was a general conversation—I do not want to be pedantic about those points, just leave it at that—and within that, Lloyds come out and say, "We are not sure that this is going to go ahead. We do not think you are capable of doing this deal". The one thing that is going to save that is this capital injection from the sale of other assets outside the bank itself and you forget whether you mentioned that or not. The one deal that is going to be able to bring Co-op forward and you, kind of, forget that you have two big transactions going on that are going to save this deal, which is incredibly important to the future of the bank. How do you forget that?

Barry Tootell: It was made clear that that would have included capital injection. I am not clear on whether we had told them which assets Co-operative Banking Group, or indeed our parent, may choose to sell.

Q589 Mark Garnier: You were being a bit woolly about this a bit earlier, so thank you for clearing that up. You are now saying that you definitely said there would be a capital injection from the parent company?

Barry Tootell: I was not in the meeting. I would expect so.

Q590 Mark Garnier: It is so important. I cannot believe that you guys who are running this bank cannot remember these really important details.

Barry Tootell: This is day-to-day liaison between managers—

Mark Garnier: No, it is not, this is a major strategic transaction.

Q591 Chair: Are you describing this huge deal as part of day-to-day liaison?

Barry Tootell: The particular meeting—

Chair: This was make or break for Co-op.

Barry Tootell: If we were not able to address the capital shortfall through the remediating actions, it would have been a showstopper for the transaction. Yes, I accept that.

Q592 Chair: But you cannot remember what was told to Lloyds?

Barry Tootell: The information that was provided, the detailed discussion of that at that point, bear in mind our teams were meeting several times a month, several times a week, sharing information, sharing plans. They were sharing plans with us; we were sharing plans with them. In one of those meetings, yes, we did agree we were going to share with them our underlying three-year planning assumption for the standalone business that was going to be part of the Verde transaction, but it would have shown—and it did show—a lower level of capital than the deal would require and there would have had to have been a capital injection. I am not clear on whether we said, "That will come from the sale of the GI business" because at that time we had not made the board decision to divest. That was not until quarter one 2013, but we were progressing our thoughts along those lines.

Q593 Chair: This is not long ago, we are not digging up something from a decade ago and there will be notes of comments that were or were not made, won't there?

Barry Tootell: Yes.

Q594 Chair: Have you made an effort to look at those before coming today?

Barry Tootell: I have not done, no.

Q595 Mark Garnier: There is a very important point to this, which is Lloyds' due diligence on how they go about this. If you are suggesting there is going to be a significant importation of capital from a mutual parent, quite justifiably, Lloyds would ask where that capital would be coming from. They would want to know where it is because, as a mutual, you do not have the easy ability to raise capital in the same way that a listed company would do.

Barry Tootell: No. It was clear that the only means we would have had to inject capital would be the divestment of assets of the group and more likely the assets of the banking group. So, yes, general insurance and life and savings were known businesses that we could divest if we chose to do so.

Q596 Mark Garnier: But you are saying you would not have told them what it was. As an organisation, Lloyds would have to take a massive amount of trust on what you are saying. Do you think they would do that? This is a huge deal. This is a very public deal with a publicly-owned bank, with the biggest mutual in the country, with huge amounts of importance on the whole of the transaction. You cannot remember what was going on. You are now telling us you were not prepared to reveal to Lloyds what the assets were that were being sold because they were market sensitive. Lloyds would have had to accept, on a massive amount of trust, the fact that as a mutual—which obviously has difficulty raising capital—you could raise this capital. Are you suggesting that in all these conversations in December, which seem to be the key conversations that were going on, you cannot remember what was happening then?

Barry Tootell: I cannot remember the specific of whether we said, "We are selling our GI business".

Q597 Mark Garnier: You did say earlier that you said you weren't.

Barry Tootell: Yes, but I did not say we did not tell them. I cannot recollect whether we told them specifically which asset we were considering selling.

Q598 Mark Garnier: You said you could not, because it was market sensitive.

Barry Tootell: Yes.

Q599 Mark Garnier: So what is it? You cannot remember whether you said it or you did not say it?

Barry Tootell: I apologise. I said before, I do not recollect. I do not know specifically whether we told them that we were selling our GI business and injecting it. I suspect we would not have done because it was market sensitive, but I do not know whether we shared that mitigating plan with Lloyds. I agree with your comment that Lloyds were taking the work that we were doing on trust, because we were asking them to wait while we developed our mitigating plans and then we would share the detail of that with them. During the process of engagement—we were meeting them regularly, day in, day out, week in, week out—we were sharing the emerging view of things with them.

Q600 Mark Garnier: Mr Norman asked you a bit earlier about who were the advisers on the Britannia deal, which for the Co-op was JP Morgan and for Britannia it was Citigroup. I believe JP Morgan and Citigroup were the advisers to the Project Verde deal.

Barry Tootell: Indeed.

Q601 Mark Garnier: Do you think they knew more about your business as a result of that link with the corporate advisers of that deal than you did at the time?

Barry Tootell: Did they know more about?

Mark Garnier: Because they had two advisers that had been party to the Britannia deal, do you think Lloyds had a better insight into what was going on in your business than you did, because they understood how to run your business better than you did?

Barry Tootell: I would suspect not. One could argue that because I had Credit Suisse and BarCap working for me, we would know more about them than they would have told us. To suggest any of those factors was true is to suggest that the strict confidentiality over any engagement of an adviser was breached, so I would suggest not.

Mark Garnier: Okay, fair enough.

Barry Tootell: As a corporate, JP Morgan clearly understood us in some detail.

Q602 Mr Ruffley: Mr Tootell, you have been very strategically forgetful in your last few answers, so I am going to help you along. In our hearing with Andrew Bailey in July this year—you have read his evidence, I take it?

Barry Tootell: Indeed.

Q603 Mr Ruffley: You have. Good. He says that towards the tail-end of 2011, he told the board of Co-op Bank that it was not clear to the regulator that the Co-op Banking Group had the ability to transform itself successfully and sustainably into an organisation on the scale that would result from acquiring the Verde assets. He then went on to say, "Then we set out five things, the five areas that they would have to deal with: capital, liquidity-risk management, integration, governance and management". That is obviously a pretty full set. He starts with that list of five things that the board would have to address as capital. What did he say about the level of capital, if anything, and what was your reaction to his flagging a capital shortfall, which is implicit in what I have just read out?

Barry Tootell: There was no implication or indication of a capital shortfall I think.

Q604 Mr Ruffley: What did he mean by "capital"? What was your understanding when he said "capital" in that list of five things I have recited?

Barry Tootell: That we had to evidence sufficiency of capital to do the transaction in order to proceed. He said that in July 2011. He reiterated that by one of his team writing to me, as I said before, I think it was November or December 2011, to reiterate those points. Those points were presented as the key criteria, the key heads that we would need to address in seeking any approval from the regulator to proceed with the deal.

Q605 Mr Ruffley: Let me just nail this down. I am not going to read it out again, but he said there were five things and capital was one of them. What was the response by Co-op Bank to that representation by the regulator when he says, "Areas to be addressed"? Describe to us, as best you can, what your response was. Was it in writing? What did you say to the regulator when the regulator pointed out capital as being one of the five areas of concern?

Barry Tootell: It was not raised with us as an area of concern. It was raised with us as an area that we would—

Q606 Mr Ruffley: Hang on, hang on. This is serious stuff, okay. The regulator is saying, "We set out five things, the five areas that they would have to deal with". What I am asking you, Mr Tootell, is how did you deal with it? I am quoting the regulator here. There is no point in smirking quietly to yourself.

Chair: No, steady on. Let us just—

Mr Ruffley: Let us have an answer.

Barry Tootell: It was not a concern about the business in 2011. It was Andrew Bailey being very clear with us as to which areas we would have to specifically address in order to proceed with the transaction.

Q607 Mr Ruffley: We understand. What was your response? Why can't you answer that? He asks you to deal with capital. What did you do or what did your colleagues do, to the best of your knowledge and belief, Mr Tootell? How did you respond to that capital issue? He asks you to deal with it. What did you do?

Barry Tootell: Capital is fundamentally important to the transaction. I could also argue that the capital, and perhaps all of this—

Q608 Mr Ruffley: You are waffling now. What did you do in response to the regulator, and I quote, "To deal with it"? What did you do? Did you write to him? What did you show him? What did you say to the regulator?

Barry Tootell: We had detailed dialogue on an ongoing basis with the regulator at all levels.

Mr Ruffley: On the capital, but what—

Barry Tootell: In addressing all five of those things and we updated them on our progress.

Mr Ruffley: No, let us stick with capital.

Chair: Hang on, Mr Ruffley; let us just hear what Mr Tootell has to say on that point.

Barry Tootell: We updated them on a regular basis with our progress towards addressing the five areas that they were expecting us to evidence sufficiency or progress around in order to do the transaction. These were not challenges of things that we had to fix in 2011 because the business had a problem. These were very clearly things that the regulator was saying, "If you are going to do a transaction the size of the Verde transaction, these five things are fundamentally important". We completely agreed with those five things and we were working tirelessly—

Q609 Mr Ruffley: I have been asking about capital, not the other four, but I think the record will show that you are trying to slide away from that. Never mind.

Was a potential capital shortfall ever expressed to you or any of your colleagues by Mr Bailey or any of his colleagues at the regulator, yes or no?

Barry Tootell: No.

Q610 Mr Ruffley: In relation to the tail-end of 2011 discussion?

Barry Tootell: No.

Q611 Mr Ruffley: Andrew Bailey told the Treasury Committee that he asked you to make clear his concerns to Lloyds Banking Group. Peter Marks claims that you did this.

Barry Tootell: We did.

Mr Ruffley: You did it, did you?

Barry Tootell: We did.

Mr Ruffley: Sorry, you personally?

Barry Tootell: I do not know whether it was a letter signed by me, but we briefed Lloyds on the conversation we were having with the regulator and the key areas.

Q612 Mr Ruffley: When did you do this?

Barry Tootell: I do not know the date of the letter.

Mr Ruffley: You cannot remember?

Barry Tootell: But we absolutely briefed the Lloyds team.

Q613 Mr Ruffley: What date approximately? Give us a month.

Barry Tootell: It was December 2011, because the letter formally came to us—

Mr Ruffley: December 2011. No, we have that.

Chair: Just let Mr Tootell reply.

Mr Ruffley: He has replied.

Barry Tootell: The letter came to us in November or December 2011 and it would have been very quickly thereafter. It may have been as early as November 2011. It was no later than December 2011.

Q614 Mr Ruffley: Was a capital shortfall one of the concerns you relayed to Lloyds in late 2011?

Barry Tootell: Again, it was not a capital shortfall, but it was the list of things that the regulator needed us to evidence in order to do the transaction. It was never voiced as a capital shortfall.

Q615 Mr Ruffley: Fine, okay. You are rejecting the words "capital shortfall". Let me try this one on you. What did you say about capital to Lloyds towards the end of 2011? I am not using the word "shortfall", by the way. What did you or any of your colleagues say in writing or verbally about the capital issue? I am not using the word "shortfall"; what did you say to them, Mr Tootell?

Barry Tootell: But again, it was not a capital issue. It was evidencing—

Q616 Mr Ruffley: What did you say about capital then?

Barry Tootell: We said that there are five key areas of focus for the regulator that we will be evidencing and spending—

Mr Ruffley: No, capital. Not the other four issues, capital, Mr Tootell. Please do not slide away to the other four issues. I am focusing on capital. What did you say about the capital position and your expected capital position to Lloyds in late 2011, Mr Tootell? What is the answer to that question?

Barry Tootell: We told them specifically that, among four other things—

Mr Ruffley: Oh dear.

Barry Tootell: —but on capital as one of those things, but capital was a key area of focus for—

Q617 Mr Ruffley: What do you mean "key area of focus"?

Barry Tootell: The regulator demanded, as we would demand of ourselves, that we evidence that we have sufficient capital to do the transaction and that was a natural thing for our board to accept. We did not need telling that by the regulator. That was absolutely what our board would have evidenced to itself before it even considered the transaction.

Q618 Mr Ruffley: How was it proposed to evidence that?

Barry Tootell: Probably since 2011 we have been running with a board risk appetite, which was to have a minimum level of core tier 1 of 10% in order to satisfy ourselves on our capital position for the future. We accepted it was a timeline to get there and it wasn't going to be an overnight fix, but 10% was our board appetite for capital adequacy. That was the plan that we were working towards on a standalone basis. That was also one of the underpins in considering the Lloyds transaction. That was our board's view. Therefore it accorded with the regulator's view that capital is key, and we agreed and we told Lloyds that.

Q619 Mr Ruffley: Finally, let's move on to the second half of 2012, the regulator again. Let us see if you can do any better with this. Andrew Bailey told this Committee that the FSA's stress-testing in the second half of 2012 confirmed the suspected capital shortfall in Co-op Bank. Did the regulator express fresh concerns to you about Co-op's Verde bid in response to this?

Barry Tootell: No, it did not.

Mr Ruffley: It did not.

Chair: Okay.

Mr Ruffley: I am not quite finished.

Chair: We will take one more question and then we must move on.

Q620 Mr Ruffley: The chief executive of Lloyds told this Committee that Lloyds was "not approached by the Co-op Bank or the Co-op Group board" regarding the confirmed capital shortfall in December 2012. Why not, Mr Tootell?

Barry Tootell: There was no capital shortfall in 2012. There was an increasing level of capital that was being—

Mr Ruffley: No capital shortfall. Nonetheless—

Barry Tootell: In 2012. The capital shortfall emerged in 2013, which was the addition of future capital requirements on top of the underlying capital guidance requirements of the FSA. What we built into our planning process was the direction of travel for the capital guidance, which the regulator sets for all banks individually. I am afraid I cannot share it with you because of market sensitivity.

The issue that became the capital shortfall, which ended up getting announced in June 2013 by the PRA, was the requirement of the FPC and the PRA that all banks build into their future capital projections the ability to achieve a level of capital requirement under Basel III arrangements but adjusted for known areas of future emerging exposure. That was announced in June 2013. We had the first indication of the scale of that in early 2013, and that created the heightened concern beyond what we were aware of in December 2012. December 2012 was about our capital guidance figure, not around future capital requirement, which was crystallised in the June 2013 announcement.

Q621 Chair: Just to be clear there. As I understand it, what you are saying is that the goalposts were changed slightly by the regulator. They were tightening your capital requirements.

Barry Tootell: Yes, not just for us but for the whole marketplace because the regulator and the FPC were looking for banks to—

Q622 Chair: I understand. Therefore, because you had little margin for error—you did not have much of a cushion—this hit you particularly hard. Is that what you are saying?

Barry Tootell: Indeed. As I alluded to before, that was the trigger for Pennine in early 2013. We had done a plan based on what we thought the capital requirements were going to be, as crystallised within the individual capital guidance for the bank, and we were doing mitigating action to that end. Then in January 2013, we had the first indication of the heightened level of capital, which, broadly speaking, was consistent with the FPC and PRA announcement in June 2013. But it was that heightened level of capital requirement that caused Project Pennine to be initiated.

Q623 Chair: You would agree, though, that that does sit slightly oddly with your comment in March that "our balance sheet remained strong"?

Barry Tootell: Indeed. That is why we were doing Project Pennine to remediate the action.

Q624 Chair: I am being pretty gentle about it in saying it sits oddly. Going back to the conversation with which we began this hearing, you would agree with that, would you?

Barry Tootell: The accounts as a whole have an extensive area in them of risk assessment, considering not only our view of risks to the business—that was very clear on the scale of risks—but effectively to support the going concern opinion of the business. There was an extensive section there on the potential risks and mitigants to emerging risk. It was the combination of all of those that allowed us to make a statement about the balance sheet at the end of 2012 as being still at 9.2%.

Q625 Chair: The key point is that you were right up against these limits already. You were sailing close to the wind, and when some further demands were made of you, that was too much.

Barry Tootell: Indeed.

Q626 Chair: Therefore, it does sit oddly to say that your balance sheet remained strong because it wasn't very strong. A puff of wind could blow you over.

Barry Tootell: It was adequate at 2012 year-end. We were looking not so far as our own balance sheet standalone was concerned in December 2012, but looking generally to what the markets and the regulator were going to look to banks to address off into the medium-term future. It was that that gave us the significant challenge rather than the position of the year-end December balance sheet. But I think the combined package of the going concern review, together with the risk assessment, was an adequate packaging of the statutory accounts.

We were working extensively on remediating the difficulties this was going to cause for the bank and, from January onwards, we were doing the plan that was referred to by the FPC and PRA in June. All banks were doing their capital plans to address the future requirements—not a black hole, but the future requirements for the banking industry, and we were doing our own. The tipping point then for the transaction was that beyond February/March, when we were concluding our accounts process, but into April, it was me reaching the conclusion that—off the back of the capital planning work that we were doing to address the FPC/PRA papers for June—we were not going to put sufficient remediating actions in place to address the future capital requirements. It was on that basis that I concluded that we should not pursue the Verde transaction.

Q627 Chair: But given that you were already sailing so close to the wind, would it not be right to characterise the attempted deal with Lloyds as a rescue operation?

Barry Tootell: I think very clearly, no. Even though we had emerging or growing concerns around our future capital requirements and the demands placed upon us, we were very clear that—and I was very clear with Andrew Bailey, as early as January 2013—notwithstanding the fact that the deal could make us a little bit stronger, this was not a deal to go into if we were not strong enough to do it. Therefore, we could not countenance it as a rescue because we needed to be convinced as a board that we had enough capital strength to go into it.

If I take you to the 2011 comments and the letter from the FSA, the one of the five key things that they set for us was capital. It was very clear to us and to the regulator that going into the deal as a rescue was not going to work. We would not have done it anyway, but it was not going to work because we needed to demonstrate capital sufficiency to do the transaction in the first place.

Chair: I have three more colleagues who want to come in. We had intended to hear from Mr Flowers as well this morning but we hope that that will be rescheduled for tomorrow afternoon. I am going to bring in the remaining three colleagues for this hearing.

Q628 Mr McFadden: Thank you, and thank you for clarifying about tomorrow, Chair.

Mr Tootell, I want to turn to a slightly different area on these critical decisions we are taking in this structure of Co-op Bank or Co-op Financial Services with a parent Co-op Group sitting on top of it, which wholly owns Co-op Financial Services. In his evidence last week, Peter Marks explained to us that he did not sit on the board of the Co-operative Group, which was an elected board, but that he chaired the executive committee of the group. Sitting from where you were, what did you regard as the key decision-making body in the Co-op Group? Was it the executive committee or the group board, given the structure?

Barry Tootell: It was very clearly the group board in overall terms. Peter Marks attended each board meeting as the chief executive and, therefore, primary officer of the group. He was not a member of the board itself but he attended these board meetings. So, yes, he was a chairman of the risk management committee, but I would regard the primary decision-making forum as being the group board.

Q629 Mr McFadden: When it came to recommend going for the Verde transaction in the first place, who is taking that decision? Who is the key decision-maker when the bank decides to do that?

Barry Tootell: The group board needed to make the decision to support the continuation of exploring the opportunity. As with any board, if the chief executive is not able to support a decision or a transaction, that will be a significant issue for the board. The board will be very minded of the opinion of the chief executive. Peter Marks would clearly have been a significant influential character in that process, but the board is the decision-making body that would have allowed us to proceed or not with the transaction.

Q630 Mr McFadden: My colleague, John Thurso, when he was questioning Peter Marks on this kind of area last week, used the analogy of a Government and a Parliament, with the executive committee being the Government and the board being the Parliament. Do you think that is a fair way to sum this up?

Barry Tootell: If we are talking about the executive committee and the board of the group, yes, that would be a fair way to sum up the way in which the broader group or the trading aspects of the group operated, but not its oversight over the banking business.

Q631 Mr McFadden: Again, going back to Verde, would this have been a recommendation made by the executive committee of the group, which then goes to the board for approval, or would it have been something that originated within the board as being a good thing for the group to do?

Barry Tootell: No, we did recommend to the board that they allow us to continue with this opportunity, and they approved that course of action. In terms of the decision-making bodies below the board and the support that that gave to the process, Peter and I were pretty clear that if it did not have the unanimous or broad support of the executive committee of my banking group, and, similarly, if he did not have the broad support and unanimity of the group executive, it would not be something that he and I would be willing to take to the group board for decision. Unless the business underneath the board is supportive of the transaction, it would not be helpful for the board to be asked to approve something knowing that the management do not agree with that transaction.

Q632 Mr McFadden: Apart from Neville Richardson, is there any senior figure, in either the Co-op Bank or the executive committee of the group or the board of the group, who disagreed with going for the Verde transaction?

Barry Tootell: I would have to look back at the group board minutes. As I say, I am not a member of the group board either but we could look at the board minutes to check on the voting. Oftentimes it is consensus and oftentimes it is a vote. We did have a vote for the group board decision to proceed with the transaction or otherwise. On some of those votes, we have not had complete unanimous support. There have been abstentions but we have the vast majority of the board in favour of the transaction. I do not recollect whether that complete unanimous approval, versus the split but generally majority decision, was in relation to the heads of terms that we signed in mid-2012 or the initial decision to proceed with the transaction.

Q633 Mr McFadden: I am trying to get to the bottom of that. You are saying there were other voices on the group board that were uncomfortable with the Verde transaction? It was not a unanimous decision?

Barry Tootell: There was not a unanimous approval at all times. Quite validly and quite rightly, there were questions and concerns about the capacity of the group to do the transaction. Essentially, that was not a concern about the transaction itself. There was a concern about the financial capacity of the group to fund the transaction because the transaction consideration was £350 million up front, which would have been financed by the group injecting capital into the bank and the bank utilising that to buy the business we were acquiring. The group would have to encumber itself to the tune of £350 million, and that was a major area of focus for group board directors.

Q634 Mr McFadden: They were asking, “Can we afford this?”

Barry Tootell: They were, absolutely. You would expect them to do so and, yes, they did. It took a lot of input from the group finance and group audit committee in that deliberation, and you would expect them to do just that.

Q635 Mr McFadden: You had a long-term involvement both as CFO and then CEO of the bank. In that time, how much involvement did the Co-op Group board have in the running of the bank?

Barry Tootell: Relatively limited. They were the shareholder and therefore responsible for their investment in the group. They did not oversee and interfere, let’s say, with decision-making within the banking business. The banking business was set up with some representatives of the group board on the banking group board. Then importantly, we recruited from the market place independent, professional non-executives with industry skills and experience in order to run the bank as a bank needs to be run. They relied and took comfort from their professionalism and did not override or dabble in the decision-making of the banking group. There were occasions when the banking group needed to go to the group board for approval for certain matters because there would have been matters reserved for the group board itself—as I said before, major acquisitions and disposals. For example, the decision to sell the life business needed to be approved at the group board level.

Q636 Mr McFadden: When we have this—I guess you could call it—eclectic group board of these 20 elected members from various backgrounds, what you are saying to us is when it came to the running of the bank, most of the time they were pretty hands off? I am not trying to put words in your mouth, you use your own.

Barry Tootell: They were reasonably hands off. I attended the group board each month to account to my group shareholder representatives, effectively, as to how the bank was performing, talking about the major risks, talking about the major opportunities and talking about the day-to-day performance of the banking business. So there was accountability and there were appropriate and challenging questions on key issues from time to time, but there was no detailed involvement in decision-making.

May I say that is consistent with other businesses within the group? There are three subsidiary boards within the group. There is one for food, one for specialist businesses and one for the bank. There is a similar approach for non-executives to be recruited from the marketplace to support each of those boards in turn.

Q637 Mr McFadden: Yes. This is important because I want to get to how the overall Co-op Group and these subsidiaries work. Sticking with the bank, when it comes to setting strategy for the bank are you saying that is done by the bank itself or by the group?

Barry Tootell: It is done by the bank. We have a strategy session that starts in July, which is more high-level strategic, culminating in November of each year with a lower level of granularity and rigour, financials, capital and so on. That in turn is used to inform the group board as part of group-wide strategy settings. The group strategy would have been the sort of discussions that Peter Marks alluded to in this room, in terms of the diversity of interests of the group. For example, which businesses are we in? That is the sort of level of decision-making the group would get into in group strategy setting. Not the detailed strategy plans of each individual entity.

Q638 Mr McFadden: I will slightly change tack here and ask you one further thing following on from Mr Ruffley's questions about Andrew Bailey's list of five concerns. In his evidence last week, Peter Marks said several times that he saw proceeding with Verde as the answer to three of those five, including the capital question that Mr Ruffley asked. You seem to be giving us a different emphasis, which is, "These are five things that we have to show we have answers to before we can proceed with Verde". Which is right? This is an important difference. Was Verde the answer to Andrew Bailey's list or was this a list of things that had to be satisfied before Verde could be contemplated?

Barry Tootell: No. To be clear, these are things that we would have to address for ourselves in order to do the transaction and not looking for Lloyds or Verde to do it for us. Very clearly so.

Q639 Mr McFadden: Therefore, Verde is not the answer to Andrew Bailey's list. The answer has to come before Verde can proceed.

Barry Tootell: Indeed. If I take capital as an example. We had to demonstrate capital sufficiency before we considered the transaction. By the same token, the transaction itself will have to be complementary to that, it cannot erode. Therefore, the Verde opportunity will have to help rather than hinder. There is a primary position, which is that the bank needs to evidence sufficiency of capital first. We cannot look to the Lloyds opportunity to fix the five challenges that came from Andrew as part of the transaction.

Q640 Mr McFadden: That is important for us. Finally I will end with this. When it came to the decision to pull the plug on Verde, who took the decision?

Barry Tootell: Ultimately it is a board decision. It was my recommendation. It was my judgment as the chief executive. I cannot remember the sequence, whether I told my chairman first or Peter Marks first. But I told both parties that in my opinion this deal could not proceed. I told the chairman and Peter Marks, and that decision was supported by both parties. It was my judgment.

Q641 Mr McFadden: You told them and then the group executive goes to the board and says, "We don't think we can proceed with this", is that how it worked?

Barry Tootell: Peter and I informed the group board that it was no longer the recommendation of management that we could continue with the transaction. By the same token, I did the same thing with my board.

Q642 Chair: You have had much the same problems as an institution that most other banks have had. You also had a risk management committee structure in place. Were you sitting on those committees and were they flagging up concerns?

Barry Tootell: I was not sitting on the committees because, in line with the pursuit of greater governance—

Chair: You would be in attendance. Sorry, I should have used the words "in attendance", you are quite right.

Barry Tootell: I attended, yes. For example, my risk officer had a direct reporting line to the chairman of the risk committee. They were challenging meetings. We absolutely did not have an easy ride—and nor should we—with our risk committee and our audit committee in the management of the business on a day-to-day basis.

Q643 Chair: Were they flagging up the risks on the commercial lending you were doing?

Barry Tootell: No more so than we were briefing them upon. We got challenging and searching questions.

Q644 Chair: That does not sound very challenging if you brief them to ask certain questions and then you reply to them.

Barry Tootell: No, they were asking us challenging questions on the detail that we were presenting. I am suggesting that they did not unearth something we had not spotted. But the insightful and searching questions that we received from those committees were very challenging, and very appropriately so.

Q645 Chair: But much like other banks it did not stop this exposure developing, did it?

Barry Tootell: It did not stop the exposure emerging. If I take us back then to 2008-09 when the now fateful decision was taken to acquire the Britannia business. Everything that has ensued thereafter has been the consequence of having done so. From mid-2009, when we completed the transaction on 1 August 2009, in a way the die was then cast because we had the PPI exposure in the underlying co-operative business. We then had the exposure in the non-core business, predominately Britannia assets. Therefore, the challenge thereafter was one of management and mitigation and monitoring the emergence, but importantly, seeking to do something about it rather than simply watching the issue emerge. These were not new issues but these were a growing—

Q646 Chair: I want to ask one other question with respect to what was going on in early 2013. Did you have to give assurances to your auditors in 2013 to achieve the going concern signoff?

Barry Tootell: Yes, we did, but then—

Q647 Chair: What were they? What were the assurances that year?

Barry Tootell: We shared capital plans with the auditor to enable them to pass their opinion on the accounts.

Q648 Chair: What opinion did they give? What were they most concerned about at that time?

Barry Tootell: They were concerned about the eroding capital position because of capital risk weights.

Q649 Chair: The same eroding capital position that was taking place as you said that your balance sheet remains strong?

Barry Tootell: Yes. But it is a future ongoing emergence that needed parallel mitigation in order to accommodate. That is what the plans said we were doing. Those are the plans that we shared with the regulator in April 2013.

Q650 John Thurso: Can I go back to 2008, and first just clarify your own background. You are a banker by profession with fairly extensive experience in a number of commercial banks at a divisional CFO level?

Barry Tootell: Indeed.

Q651 John Thurso: When exactly in 2008 were you recruited?

Barry Tootell: I joined on 17 December 2007.

Q652 John Thurso: In other words, before anybody mentioned Britannia?

Barry Tootell: Yes, indeed, I joined on an interim basis, and I joined on a permanent basis on 1 April 2008.

Q653 John Thurso: Coming from a background in normal—it is the wrong word—but non-mutual banking, if I can put it like that, what were you recruited to do and what were your thoughts about the business you were going into?

Barry Tootell: I was recruited specifically to strengthen the finance team and our finance capability in a challenging external world, where the challenge to banks to perform with greater rigour and the desire for finance communities to play a more significant role in the stewardship of the business was something that the Co-op had absolutely embraced and had specifically looked for me to join the business and help them achieve.

Q654 John Thurso: The reason I ask that is, of course, because my memory of that year is very clear, having sat on this Committee with the report into Northern Rock. I remember very well going to events in the City, in June and July of 2008, where the then HBOS were complaining bitterly about being shorted and they were a very strong institution. Of course, it was not until the meltdown in September/October 2008 that the real crisis started, and it did not manifest itself in corporate lending until 2009. What I was trying to get at is the interesting view that you would have had at the very beginning, because it is pre-crisis, of "What is this business I'm coming into and what is it I'm being hired to do?"

Barry Tootell: It was a business that had historically operated with a high degree of competency. I was quite impressed in joining the Co-operative that not only did they have a culture within the business that was hugely collaborative and very, very open and non-political and a great place to work, but also with very high calibre people recruited into some of the key roles. I was quite pleased when I joined the business that they were not—it is a slightly disrespectful view—sleepy and backward looking as I might have thought they were; because I was brought in to help them get better. I was pleased that I was trying to help them get better from quite a high starting point.

Q655 John Thurso: Because in his note on the background to the Britannia merger Neville Richardson says, "CFS had a current account, corporate bank and insurance business. It lacked distribution and was badly in need of replacement IT systems, the cost of which would be difficult to recover over CFS's small distribution base". The point being that that is quite a significant identification of weakness in CFS at that time. Was that something you would agree with?

Barry Tootell: I would agree with it. It was not the reason for the transaction with Britannia but it is a fair assessment of where the Co-operative was at the time. We did have a small balance sheet size and a small distribution network, and we did have—consistent with other banks in the UK marketplace—quite old systems that needed more work to make them more resilient. You have seen that play out in the past year or so. We were no different from many other institutions and we were keen to replace or enhance our IT systems. Neville's comment would be correct, that our capacity to do that major infrastructure project with the scale of bank that we were would have been stretching or penal for us. Doing it once for a much bigger business would have been economically more doable. I would then suggest Britannia were in a similar position—that they also had IT systems that required work.

Q656 John Thurso: Not the new IT systems that Mr Richardson described in the note?

Barry Tootell: They had a more modern mortgage platform than the Co-operative. It was the same mortgage platform as the Co-operative, but it was a slightly newer version of it.

Q657 John Thurso: David Anderson, who was then the CEO of CFS—and tell me if this is wrong, just because it is in evidence from somebody does not mean it is right—the evidence given is that David Anderson asked to meet Neville Richardson, who was running the Britannia at that time, and pointed out the synergies and the strengths that would accrue within a merger. Was that an accurate picture?

Barry Tootell: I completely agree with the evidence that has been presented in terms of the complementary nature of the transaction. As I said before, I do not know whether David approached Neville or the other way round.

Q658 John Thurso: There is another way of looking at this, which is that the Co-op was in a degree of trouble going forward, with difficulty in growing. In looking to Britannia as a merger that gave strengths and solved quite a lot of problems, it would be fair to say that it was not a question of Britannia being taken over or rescued in any way by Co-op, it was

CFS seeing in Britannia a solution to its problems and a counterweight to some of the weakness that had been identified.

Barry Tootell: I completely disagree. Aside from the fact that the IT replacement would have been economically more viable if we had done it from a much larger business perspective, the future of the Co-operative, if we had not expanded, would have been a more niche operator than we thought was the right thing for our members and our customers because we had insufficient reach.

In terms of the capital strength of the Co-operative at the time, and in terms of the emergence of the issues thereafter, or up until today, PPI has been a significant issue and it is probably circa £400 million of costs that the Co-operative would have had to have accommodated. Looking at the capital base, and the profitability of the Co-operative, that would not have been an issue for the Co-operative.

John Thurso: Let me just get this straight, because a view that has been expressed today is very much one that the Britannia had all these hidden toxic assets and the Co-op went along and very nicely took it over and then suffered grievously as a result. Neville Richardson's evidence would seem to present that these are two mutuals that have a complementary set of problems, and a complementary set of assets that, if put together, would provide a stronger thing. It is then the CEO of Co-op who is approaching Britannia and who takes it on both sides through the relevant July strategy days. You seem to agree with the proposition at one point and then radically disagree with it afterwards. But is it not the case that it was clearly in CFS's interests to grow and to do the deal?

Barry Tootell: I think I am correct in suggesting that the only problem that you have alluded to there was the affordability of the IT investment for the scale of bank that we were. We would have been able to accommodate it, but it would have been more economic if we had done it from a larger base. That was the only issue that we were facing at the time. There would not have been the issues that we have today, if the only extra thing we had to accommodate was the emerging cost of PPI and the underlying heritage Co-operative business.

Q659 John Thurso: So Co-op would have been able to deal with PPI on its own?

Barry Tootell: Yes.

Q660 John Thurso: This is now close to April 2008, so you were the full-time chief financial officer. The relationship between a CEO and CFO is the tightest in any organisation, usually. So you would have been heavily involved in this. At what point did the internal CFS discussion about "This is a good thing to do" move to being first of all one that the CFS board started to talk about and then the board of Co-op were brought into?

Barry Tootell: I believe it was as early as July 2008.

John Thurso: For the CFS board or the Co-op board?

Barry Tootell: Both the CFS board and the Co-op Group board.

By August 2008 we had engaged advisers to proceed with the exercise. Then in January 2009 we had announced to the market that we were progressing towards the deal.

Q661 John Thurso: At the time, given the expanding size and your professional knowledge of the regulatory requirements, were you content with the corporate governance structures that were in place?

Barry Tootell: Yes. The quality of the non-executives that I had on my bank board at the time was impressive and they remain so today. So, yes, I had a very strong board back in 2008.

Q662 John Thurso: Sorry, because I just do not know this, how many of those non-executives were from a banking background?

Barry Tootell: I think we had five external non-executives.

Q663 John Thurso: That is not the Co-op non-executives, but the externals?

Barry Tootell: The external non-executives, the IPNEDs: the independent professional non-executive directors. I think two of them were. Bearing in mind we were also a multi-disciplinary business—we were a general insurance, life assurance and banking business—we had directors that covered each of those areas of our business.

Q664 John Thurso: Do you consider that to have been an adequate structure now that you know what has happened?

Barry Tootell: Yes. That is not to say we were complacent at the time. I think we have shown our desire and willingness to strengthen still further over the time that has ensued thereafter. Today we see greater banking expertise than we had at the time. That is not to say we did not have adequate banking expertise back in 2008.

Q665 John Thurso: You intimated earlier that you had had an opportunity to read the Banking Commission's reports. Did you read the one on HBOS entitled: *An accident waiting to happen*?

Barry Tootell: I did.

Q666 John Thurso: Did you notice any similarity between the composition of the boards, your own and that of HBOS?

Barry Tootell: No. The composition of the board, at both executive and non-executive levels in the bank, and the broader financial services business benefited from the detailed skills and experience from the broader marketplace. I thought you were going to ask was there a similarity between the issues that emerged. The answer to that would have been "yes", because clearly what was identified through the due diligence process proved not to have been sufficient to identify the problems that then ensued, with the benefit of hindsight. At the time, we genuinely thought we did an incredibly professional job.

Q667 John Thurso: The point behind this is that you had variously 16 to 17 people on the bank board, not the main Co-op board, of who roughly one-third are from the Co-op board, who broadly do not have any financial services experience?

Barry Tootell: Indeed.

John Thurso: You obviously have your executive members who clearly do and you had two out of five of the non-execs who had some experience. That falls very considerably short of all the recommendations made by the Banking Commission on the balance of a board in terms of the balance between professional banking and other experiences. Yet you are telling us you think it was hunky dory and no problems at all.

Barry Tootell: It was felt that it was a strong board at the time, in 2008. Since 2008 we have continued to strengthen it still further. If I look now in 2013 at the Parliamentary Commission's findings on the matter, I would say that today we have much stronger banking representation in our non-executive directors than we had then. We have continued to strengthen over the time that has ensued thereafter.

Q668 John Thurso: Ultimately the board you had in 2008 was as weak as the boards of a number of other banks. So at what point does the advantage of the culture of the mutual that owns the bank—but the bank is a share-structured and regulated equity-based company—become outweighed by the weaknesses of the structure that was put in place?

Barry Tootell: I think we have genuinely benefited from the diverse opinions that we see in our boardroom. We have the represented views of the broader membership of the group sitting in our boardroom and playing a part in the debate that we have as directors. Whether that be bringing the ethical card to bear or whether that be representing the broader view of the membership, it is a helpful check and balance to some of the decision-making that we have undertaken. I do not think we have fallen short by having that broader democratic representation in our boardroom.

John Thurso: I am having difficulty with this. You are no longer there, but the Co-op Bank—something a lot of us would like to support, both in concept and reality—is now likely to end up as a listed company, with 30% of its equity owned by the Co-op board. It is going to have to be run in the way of companies listed on the market with all the good and bad that come with that, and it has probably set back the concept of mutuality in finance for some considerable time. I am looking to see what could or could not have been avoided in the corporate governance structures, and you are telling me—notwithstanding the sort of cluster what-not that this has become—that it was all fine. Why should I take that as a credible piece of evidence?

Barry Tootell: It wasn't all fine. We made the decision to acquire assets from Britannia in 2009—decision-making at the end of 2008 into early 2009—based upon the economic data that we had at our disposal and shared extensively with the triumvirate of the regulators, which were HMT, Bank of England and FSA at the time.

We put it through a rigorous challenge in the boardroom and we acquired assets. Previously, in the late 1990s, early 2000s, we had sold PPI products. Those two things are essentially what have brought the business essentially to the position it is in today. So the governance of the business in the here and now or even back in 2008—bearing in mind we made that acquisition based on the available information about the future projections for the economy—I can point to no decision that was made at that time that was not made with the utmost care and professionalism.

Could there have been more banking directors on the board? Yes, there could. Would it have changed the decision? I am not sure that it would, based on the information we had at our disposal in 2008/2009.

Q669 Chair: Your evidence there is suggesting that you were happy with the non-executive structure and with the scrutiny on risk provided from that structure of corporate governance. Having heard what John Thurso and others throughout the hearing this morning—and it is now this afternoon—have been saying, is there anything in retrospect, with respect to the corporate governance structure, that you would want to have changed?

Barry Tootell: Both for its own benefit and to respond to challenge across the marketplace, the business has to continue to evolve and strengthen its governance still further. It is continuing to bring greater banking expertise to the fore and is actually reducing the level of group democrats.

Q670 Chair: That is a question about the institution now. I am asking you a question with the advantage of hindsight, and I will have one more go. In retrospect, at the time that all these things started to go wrong, or a little prior to that, are there things with respect to corporate governance, ways in which this institution was being run, anything at all that you feel you would like to have altered?

Barry Tootell: I do not believe so.

Q671 Chair: Nothing whatsoever?

Barry Tootell: I have benefited from a degree of—

Chair: It is a clear answer.

Barry Tootell: —expertise from my non-executive directors that helped me and challenged me in the running of the business. That had been the case since 2008 and all the way through to 2013. Is it continuing to evolve and get even stronger? Yes. Was it inadequate then? I would not suggest it was, no.

Chair: I think we will leave it there. Thank you, Mr Tootell; it has been an extremely illuminating session. It has left many questions unanswered, as often the best pieces of evidence do in their way. You will understand if we do find aspects of the evidence you have given today disappointing. Of course it is describing a story that is itself tragic, bearing in mind what has happened to the Co-op.