
FINAL NOTICE

To: **The Co-operative Bank plc**

Firm

Reference
Number: **121885**

Address: **1 Balloon Street
Manchester
M60 4EP**

Date: **10 August 2015**

1. ACTION

- 1.1. For the reasons given in this notice, the Authority hereby, pursuant to sections 91 and 205 of the Financial Services and Markets Act 2000 (the "Act"), publishes a statement to the effect that the Co-operative Bank plc ("Co-op Bank") has contravened regulatory requirements.
- 1.2. The serious failings in this case merit a substantial financial penalty. However, in the circumstances of this case, the Authority has decided not to impose a financial penalty. The Authority has given serious consideration to the impact of a substantial financial penalty. This includes, in particular, that Co-op Bank is currently engaged in a turnaround plan with the aim of ensuring that it meets its Individual Capital Guidance on a sustainable basis and has adequate capital to withstand a severe stress.
- 1.3. The Authority considers that it is of great importance that this plan is successful and that Co-op Bank's capital resources are directed towards improving its

resilience. In the exceptional circumstances of Co-op Bank, a public censure is considered appropriate and proportionate.

- 1.4. The public censure will be issued on 11 August 2015 and will take the form of this Final Notice, which will be published on the Authority's website.

2. SUMMARY OF REASONS

- 2.1. For the period 21 March 2013 to 17 June 2013 Co-op Bank breached the Authority's Listing Rule 1.3.3R (misleading information not to be published). This was as a result of the statements made on its capital position in its financial statements for the year ending 31 December 2012. In addition, from 25 April 2012 to 9 May 2013 Co-op Bank also breached Principle 11 by failing to notify the Authority of intended changes to two senior positions (and the reason for those changes).
- 2.2. The UK listing regime relies on disclosure and transparency to allow investors to make fully informed decisions. It is of fundamental importance to achieving the Authority's objective of making the relevant markets work well that market disclosures by listed companies are not only timely but also accurate. This ensures that they can be relied on by investors in making investment decisions to hold, buy or sell an investment. By making statements about its capital position that were misleading in its annual report, Co-op Bank fell significantly below the standards expected of listed companies in the UK.
- 2.3. On 21 March 2013, Co-op Bank published its 2012 Financial Statements for the year ended 31 December 2012. The 2012 Financial Statements showed a loss of £673.7m. This was a significant change to that expected by Co-op Bank only a few months previously. A major contributory factor to this was impairment losses of £474.1m. These resulted in large part from work required after the year end to comply with the standards for provisioning set out in a letter to the industry from the Authority dated 20 December 2012. In addition, there was a further provision for Payment Protection Insurance claims of £149.7m and a partial write off of the value of a new bank IT system in the amount of £150m.
- 2.4. The 2012 Financial Statements contained the following statements in relation to Co-op Bank's capital position:

- (1) *"Adequate capitalisation can be maintained at all times even under the most severe stress scenarios, including the revised FSA "anchor" stress scenario; and*
 - (2) *"A capital buffer above Individual Capital Guidance (ICG) is being maintained, to provide the ability to absorb capital shocks and ensure sufficient surplus capital is available at all times to cover the Bank's regulatory minimum requirements."*
- 2.5. Statements made about capital are crucial to readers of banks' financial statements. They are a key guide to the health and future stability of a firm. These statements about capital in the 2012 Financial Statements were false and misleading.
- 2.6. In fact, since 15 January 2013, when the Authority issued Co-op Bank with revised capital requirements, Co-op Bank did not have sufficient capital to meet its revised Capital Planning Buffer ("CPB"). This was the capital buffer set down by the Authority *"to provide the ability to absorb capital shocks and ensure sufficient surplus capital is available at all times to cover the Bank's regulatory minimum requirements."* From this time there were frequent discussions between Co-op Bank and the Authority (and from 1 April 2013 the PRA) on steps necessary to improve its capital position. Whilst it did hold capital above its ICG, it should, have been apparent to Co-op Bank that this was a misleading statement.
- 2.7. In addition, there was no reasonable basis for stating that Co-op Bank had adequate capital in the most severe stress scenarios. This was particularly the case given the significant changes in what was known about Co-op Bank's financial position in the previous months. This same sentence had already been removed from another section of the financial statements after concerns were expressed about its accuracy.
- 2.8. Co-op Bank withdrew from the potential purchase of branches from Lloyds Banking Group (known as Project Verde) on 24 April 2013. On 9 May 2013 the credit agency, Moody's, downgraded Co-op Bank's debt ratings from A3/Prime 2 to Ba3/Not Prime (a downgrade of 6 levels). This resulted in a significant drop in the value of Co-op Bank's listed securities.
- 2.9. Co-op Bank announced it was holding insufficient capital on 17 June 2013 and required an additional £1.5bn of Common Equity Tier 1 ("CET1") capital. The PRA

confirmed in an announcement on 20 June 2013 that it was also of the view that the Co-op Bank had a £1.5bn capital shortfall.

- 2.10. During 2013, Co-op Bank carried out a Liability Management Exercise, with the aim of increasing the level of capital that it held by £1.5 billion. This exercise involved issuing new shares and new debt in exchange for cash and existing debt and preference shares. The value of holdings was significantly reduced when the Liability Management Exercise completed on 20 December 2013.
- 2.11. Co-op Bank's breach of Principle 11 by failing to notify the Authority of intended changes to two senior positions (and the reasons behind those changes) was also a serious failing. The regulator would expect to be notified of any intended changes to senior individuals without delay to enable it to properly consider and assess the management of the firm. This is particularly important when, as was the case with Co-op Bank in the Relevant Period, there were significant issues to be dealt with by the firm.

3. DEFINITIONS

- 3.1. The definitions below are used in this Final Notice.

"2012 Financial Statements" means the Co-op Bank financial statements for year-ended 31 December 2012.

"the Act" means the Financial Services and Markets Act 2000.

"the Authority" means the body corporate previously known as the Financial Services Authority and renamed on 1 April 2013 as the Financial Conduct Authority.

"CET1" means Common Equity Tier 1 capital. This consists of the sum of: common shares that meet the criteria for classification as common shares for regulatory purposes and which meet the criteria for inclusion in CET1 capital, stock surplus (share premium), retained earnings, accumulated other comprehensive income and other disclosed reserves and regulatory adjustments applied in the calculation of CET1. This is the definition used under the Basel III global regulatory framework for capital. This applied in the EU under the Capital Requirements Directive (CRD) IV which came into force on 1 January 2014.

Under the previous framework (the Basel II framework) the equivalent term was Core Tier 1.

“Co-op Bank” means Co-operative Bank plc.

“CPB” means Capital Planning Buffer. This is the amount and quality of capital resources that a firm should hold at a given time in accordance with the Authority’s general stress and scenario testing rule, so that the firm is able to continue to meet the overall financial adequacy rule throughout the relevant capital planning period in the face of adverse circumstances, after allowing for realistic management actions. It is in addition to the Individual Capital Guidance amount.

“DEPP” means the Authority’s Decisions Procedures and Penalties Guide

“EG” means the Authority’s Enforcement Guide

“ICG” means Individual Capital Guidance. This is the guidance given to a firm about the amount and quality of capital resources that the Authority/PRA thinks the firm should hold at all times under the overall financial adequacy rule as it applies on an individual company or consolidated level.

“LME” means the Liability Management Exercise conducted by Co-op Bank in 2013.

“PRA” means the Prudential Regulation Authority.

“the Tribunal” means the Upper Tribunal (Tax and Chancery Chamber).

“Relevant Period” is between 25 April 2012 and 21 June 2013.

“RIS” means a Regulatory Information Service.

“SREP” means Supervisory Review and Evaluation Process. As part of the SREP, the Authority / PRA reviews the firm’s Internal Capital Adequacy Assessment Process (“ICAAP”).

4. FACTS AND MATTERS

Company Background

- 4.1. Co-op Bank is a retail and commercial bank which offers a range of financial products, including current accounts, savings accounts, credit cards and loans. Co-op Bank has been authorised to perform regulated activities by the Authority since 1 December 2001.
- 4.2. On 1 August 2009 Britannia Building Society merged with Co-op Bank, with the combined business continuing to trade under both the Britannia and Co-op brands after the merger. Co-op Bank was a wholly owned subsidiary of the Co-operative Group (through the Co-operative Banking Group Limited) until 20 December 2013, when the Co-operative Group reduced its stake in Co-op Bank to 30 per cent, as part of its plan to raise more capital (named the Liability Management Exercise). The Co-operative Group's stake in Co-op Bank has since been reduced further to approximately 20 per cent.
- 4.3. During the Relevant Period, Co-op Bank had bonds and preference shares that were available for trade on a Regulatory Information Exchange. As such, Co-op Bank was subject to the UK Listing Rules.

Capital requirements and their importance

- 4.4. A firm's capital requirement is the amount of capital that a firm must hold and it is set by its financial regulator. These requirements are put into place to ensure that firms are managed prudently and do not take on excess leverage (i.e. debt compared to capital base). It is crucial that firms are able to withstand adverse trading or economic conditions. These requirements aim to protect firms, customers, the Financial Services Compensation Scheme (which compensates certain customers in the event of a bank failure) and the markets. The financial regulator establishes rules to make sure that institutions hold enough capital to ensure continuation of a safe and efficient market and are able to withstand any foreseeable problems.
- 4.5. The framework for capital requirements was established with the Basel Accords, published by the Basel Committee on Banking Supervision. The Basel II framework and the Capital Requirements Directive III were in force as at 21 March 2013. These set out guidance and rules on how banks and depository institutions must calculate their capital.

- 4.6. It is very important that firms publish accurate information concerning their capital position in their financial statements as it provides users of the financial statements with details of the prudential strength of the firm and its ability to withstand adverse scenarios.

Events leading to identification of the CPB deficit

- 4.7. On 14 November 2012 the Authority communicated to Co-op Bank the initial findings of the Authority's SREP and Capital Planning Stress Testing module that it had recently carried out on Co-op Bank. The Authority explained that it was evident that Co-op Bank's capital requirements and CPB would be increasing significantly. The Authority confirmed these findings, which included increases in Co-op Bank's ICG and CPB, in writing on 15 January 2013.
- 4.8. On 20 December 2012 the Authority sent a letter to banks and building societies on loan loss provisioning. This sought to ensure that firms took an appropriate approach to loan loss provisioning by setting out the circumstances in which a provision should be made. This caused Co-op Bank to change its practice significantly and led to a large increase in impairment provisions both for year-end 31 December 2012 and onward into 2013.

Identification of the CPB deficit

- 4.9. On 15 January 2013 the Authority wrote to Co-op Bank setting out its revised capital requirement including the ICG and CPB. This resulted from work done by Co-op Bank and the Authority in 2012.
- 4.10. Co-op Bank did not have enough capital to meet its revised CPB, and significant management action was required to improve its capital position. From this time there were frequent discussions between Co-op Bank and the Authority (and from 1 April 2013 the PRA) on steps necessary to do so.
- 4.11. On 21 March 2013 Co-op Bank published its financial statements for the year ending 31 December 2012. This was published through a Regulatory Information Service announcement at 7.00am. The accounts reported a loss before taxation of £673.7 million. This included impairment losses of £474.1 million and a £150 million provision relating to Co-op Bank's intended replacement IT system, Finacle.
- 4.12. The statements relating to Co-op Bank's capital position in its 2012 Financial Statements are set out in full in Appendix 1. In the section entitled 'Capital

management – capital resources (audited) at page 80 these contained the following:

- (1) *“Adequate capitalisation can be maintained at all times even under the most severe stress scenarios, including the revised FSA “anchor” stress scenario”*; and
- (2) *“A capital buffer above Individual Capital Guidance (ICG) is being maintained, to provide the ability to absorb capital shocks and ensure sufficient surplus capital is available at all times to cover the Bank’s regulatory minimum requirements.”*

The true position in respect of Co-op Bank’s capital position

- 4.13. From 15 January 2013 Co-op Bank knew that it did not have sufficient capital to meet its CPB. This was the capital buffer set down by the Authority *“to provide the ability to absorb capital shocks and ensure sufficient surplus capital is available at all times to cover the Bank’s regulatory minimum requirements.”* In addition, there was no reasonable basis for stating that Co-op Bank had adequate capital in the most severe stress scenarios. This was particularly the case given the significant changes in what was known about Co-op Bank’s financial position in the previous months. This same sentence had been already removed from another section of the accounts after concerns were expressed about its accuracy.
- 4.14. Co-op Bank withdrew from the potential purchase of branches from Lloyds Banking Group (known as Project Verde) on 24 April 2013. On 9 May 2013 the credit agency, Moody’s, downgraded Co-op Bank’s debt ratings from A3/Prime 2 to Ba3/Not Prime (a downgrade of 6 levels). This resulted in a significant drop in the value of Co-op Bank’s preference shares and listed debt.
- 4.15. Co-op Bank’s inadequate capital position was publicised on 17 June 2013, with the Co-op Bank announcing that it required an additional £1.5bn of CET1 capital. The PRA confirmed in an announcement on 20 June 2013 that it was also of the view that the Co-op Bank had a £1.5bn capital shortfall.
- 4.16. During 2013, Co-op Bank carried out a Liability Management Exercise, with the aim of increasing the level of capital that it held by £1.5 billion. This exercise involved issuing new shares and new debt in exchange for cash and existing debt and preference shares. The value of holdings was significantly reduced when the Liability Management Exercise completed on 20 December 2013.

Failure to notify the Authority of proposed changes to senior positions

- 4.17. In the period from April 2012 to May 2013 two separate discussions took place amongst certain senior individuals at Co-op Bank about the future position of two key individuals. As a result, it was intended that the holders of these positions would change. The Authority was not informed of either of these intended changes in a timely manner (and in one case not until after the position holder had left). Moreover, during one particular conversation with the firm, the Authority asked questions in relation to one of the position holders and was provided with an incorrect assurance.
- 4.18. The regulator would expect to be notified without delay of any intended changes to senior position holders (and the reason for the changes) to enable the Authority to properly consider and assess the management at Co-op Bank. This is particularly important when, as was the case with Co-op Bank in the Relevant Period, there were a number of significant issues being dealt with by the firm.

5. FAILINGS

- 5.1. The regulatory provisions relevant to this Final Notice are referred to in Annex A.

Breach of Listing Rule 1.3.3R

- 5.2. Listing Rule 1.3.3R states:

"An issuer must take reasonable care to ensure that any information it notifies to a RIS or makes available through the FCA is not misleading, false or deceptive and does not omit anything likely to affect the import of the information."

- 5.3. For the reasons set out in paragraphs 4.9 to 4.16, Co-op Bank breached Listing Rule 1.3.3R by publishing the 2012 Financial Statements.

Breach of Principle 11

- 5.4. Principle 11 states:

"A firm must deal with its regulators in an open and cooperative way, and must disclose to the appropriate regulator appropriately anything relating to the firm of which that regulator would reasonably expect notice."

- 5.5. For the reasons set out in paragraphs 4.17 to 4.18, Co-op Bank breached Principle 11 by failing to notify the Authority of intended changes in two senior positions and the reasons behind those changes.

6. SANCTION

Public censure

- 6.1. The principal purpose of issuing a public censure is to promote high standards of regulatory conduct by deterring persons who have committed breaches from committing further breaches and helping to deter other persons from committing similar breaches, as well as demonstrating generally the benefits of compliant behaviour.
- 6.2. DEPP 6.4.2G sets out the factors that may be of particular relevance in determining whether it is appropriate to issue a public censure rather than impose a financial penalty. The criteria are not exhaustive and DEPP 6.4.1G(1) provides that the Authority will consider all the relevant circumstances of the case when deciding whether to impose a penalty or issue a public censure. The Authority considered that the factors below were particularly relevant in this case.

Deterrence (DEPP 6.4.2G(1))

- 6.3. In determining whether to publish a statement of Co-op Bank's misconduct the Authority had regard to the need to ensure that firms take their obligations to publish accurate information to the market seriously. The Authority considered that a public censure should be imposed to demonstrate to Co-op Bank and others the seriousness with which the Authority regards its failings.

The seriousness of the breaches (DEPP 6.4.2G (3))

- 6.4. In deciding whether to impose a public censure or a financial penalty the Authority will have regard to the seriousness of the breaches. The Authority has, in particular, considered the following factors from DEPP 6.5AG:
- (1) the breaches were committed negligently rather than deliberately or recklessly;
 - (2) no profits were made or losses avoided by Co-op Bank as a result of the breaches, either directly or indirectly;

- (3) there was a significant risk of loss to individual investors or other market users in relation to the Listing Rules breach.

The previous disciplinary history of Co-op Bank (DEPP 6.4.2G (6))

- 6.5. The Authority has also considered the previous disciplinary history of Co-op Bank. Co-op Bank was fined £113,300 by the Authority for breaches of Principle 6 (Customers' interests) of the Authority's Principles for Businesses on 4 January 2013. In the Relevant Period (21 January 2011 to 9 May 2011) there were serious failings in Co-op Bank's handling of complaints arising from the sales of Payment Protection Insurance (PPI).

The impact of a financial penalty (DEPP 6.4.2G (8))

- 6.6. The Authority has had particular regard to the impact of a financial penalty on Co-op Bank. This includes, in particular, that Co-op Bank is currently engaged in a turnaround plan with the aim of ensuring that it meets its Individual Capital Guidance on a sustainable basis and has adequate capital to withstand a severe stress.

Conclusion

- 6.7. The serious failings in this case merit a substantial financial penalty. However, in the circumstances of this case, the Authority has decided not to impose a financial penalty. The Authority has given serious consideration to the impact of a substantial financial penalty (as set out in paragraph 6.6 above). The Authority considers that it is of great importance that Co-op Bank's turnaround plan is successful and that its capital resources are directed towards improving its resilience. In the exceptional circumstances of Co-op Bank, a public censure is considered appropriate and proportionate.

7. PROCEDURAL MATTERS

Decision maker

- 7.1. The decision which gave rise to the obligation to give this Notice was made by the Settlement Decision Makers.

7.2. This Final Notice is given under, and in accordance with, section 390 of the Act.

Publicity

7.3. Sections 391(4), 391(6) and 391(7) of the Act apply to the publication of information about the matter to which this notice relates. Under those provisions, the Authority must publish such information about the matter to which this notice relates as the Authority considers appropriate. The information may be published in such manner as the Authority considers appropriate. However, the Authority may not publish information if such publication would, in the opinion of the Authority, be unfair to you or prejudicial to the interests of consumers or detrimental to the stability of the UK financial system.

7.4. The Authority intends to publish such information about the matter to which this Final Notice relates as it considers appropriate.

Authority contacts

7.5. For more information concerning this matter generally, contact Andrew Wigston (direct line: 020 7066 6286/email andrew.wigston@fca.org.uk) of the Enforcement and Market Oversight Division of the Authority.

Guy Wilkes
Acting Head of Department
Financial Conduct Authority, Enforcement and Market Oversight Division

Appendix 1

The 2012 Financial Statements included the following statements relevant to Co-op Bank's capital position (emphasis added in bold):

- (1) Overview' section, page 3: "... *our balance sheet remains robust with good capital ratios, which we will take measures to continue to strengthen, and high levels of liquidity.*"
- (2) The banking environment' section, page 4: "*Our core business remains profitable, while our balance sheet is robust. However, we are not complacent about our financial strength and our strategic focus for the medium term is directed at implementing measures to enhance the strength of our capital ratios. In addition to a risk mitigation transaction executed since the year end, these include strengthening the management team and engaging a major investment bank to support on a range of balance sheet deleverage options. Further to the signing of the sale and purchase agreement for the sale of the Co-operative Banking Group's life insurance business which, subject to regulatory approval, is expected to generate a significant release of capital, the strategic review will encompass a review of the scale and composition of the financial services group.*"
- (3) Performance' section, page 4: "*These results are disappointing, but are framed by the outcome of a recent strategic review designed to build on the strength of the Bank's core retail and business operations and at the same time increase our focus on de-risking the non-core assets in order to further strengthen the balance sheet. This review, supported by a strengthened management team and premier league advisory partners, will deliver capital benefits from a range of initiatives including a review of the composition of our wider Banking Group and the deleveraging of our balance sheet. The completion in 2013 of the sale of the Life and Savings business owned by the Co-operative Banking Group should, subject to regulatory approval, further strengthen the capital position.*"
- (4) 'Business and financial review - Overview' section, page 6: "*As a result of the financial performance noted above, the Core Tier 1 ratio has reduced to 8.8% (2011: 9.6%). Since the year end, the Bank has completed a securitisation transaction to reduce risk on the balance sheet, which has improved the Core Tier 1 ratio by 0.4%, and which would increase the*

year end ratio to 9.2% on a pro forma basis. This transaction is one of a range of actions targeted, as part of a strategic review, at improving our capital strength."

- (5) *'Business and financial review – Balance sheet' section, page 7: "The capital position has been impacted by the statutory loss for the year, with a Core Tier 1 ratio of 8.8% (2011: 9.6%). The total capital ratio was 14.4% (2011: 14.7%), with a Tier 1 ratio of 9.4% (2011: 10.1%). Further detail on the capital position of the Bank can be found in the capital management section on page 80. As noted above, since the year end, the Bank has completed a securitisation transaction to reduce risk on the balance sheet, which would improve the year end Core Tier 1 ratio to 9.2% on a pro forma basis."*
- (6) *'Business and financial review - Outlook' section, page 9: "We are working to strengthen our profitable core business, enhance our retail offer and simplify our high street presence under one Co-operative brand. In the short term, while market conditions remain difficult, we will re-double our focus on cost management, improving our capital strength, deleveraging the balance sheet and controlling impairment risk by actively managing our non-core business for value."*
- (7) *'Corporate Governance – Audit Committee focus during 2012' section, page 18: "The committee met 11 times during the financial year. During 2012 the committee focused on ... the appropriateness of the accounting judgements in the 2012 annual report and the 2012 interim report. The key judgements for the bank were... going concern. The Audit Committee took particular care to review the going concern status of the organisation in depth. Profit, capital and liquidity forecasting were debated along with the proposed actions to improve the position..."*
- (8) *'Statutory disclosures information - Going concern' section, page 29: "... The new governor of the Bank of England has indicated that rates are likely to be low for longer with inflation being allowed to rise to improve growth. In response, a broad-ranging strategic review of the business is underway with the objective of improving the capitalisation and profitability of the Group."*
- (9) *'Statutory disclosures information - Capital' section, page 30: "The Group's policy is to conserve a robust capital base so as to maintain investor,*

creditor and market confidence and to sustain future development of the business. However, the Group still recognises the need to maintain a balance between the potential higher returns that might be achieved with greater gearing, and the advantages and security afforded by a sound capital position.

Total capital resources are £2,578.2m (31 December 2011: £2,975.9m), with Core Tier 1 capital after regulatory deductions of £1,576.8m (31 December 2011: £1,947.4m).

The Group's capital position remains acceptable with a period end Core Tier 1 position of 8.8% (31 December 2011: 9.6%). Throughout 2012, the Bank and its individually regulated operations have complied with all externally imposed capital requirements. However, the Board recognises the need to build the capitalisation of the Group to provide increased resilience and capacity for future growth. Actions taken early in 2013 have already improved this position to 9.2%.

Current forecasts show that the Group's capital will remain above minimum regulatory requirements over the period of the Plan. However, in response to the impact of new Basel III regulations and the expectation of a prolonged economic downturn, we are reviewing our business with the intent of improving our profitability and capital position. Without management action, explained in the Opportunities section below, compliance with regulatory capital requirements would come under pressure."

- (10) 'Statutory disclosures information - Risks' section, page 30: "The idiosyncratic risks that could affect the future performance of the Group are: ... Failure to complete management actions to strengthen the Group's capital position."
- (11) 'Statutory disclosures information - Opportunities' section, page 30: "The Board sponsored strategic review seeks to build on this platform. This wide-ranging strategic review of our Banking Group businesses, considers the management actions at the Board's disposal which will be undertaken in order to improve profitability and capitalisation of the Group in line with market expectations and Basel III capital requirements ... The signing of the Sale and Purchase Agreement and subsequent completion of the sale of our Life and Savings business, followed by the planned downstreaming

of capital into the Group will also have positive implications for our capital position, subject to regulatory approval."

- (12) 'Statutory disclosures information - Conclusion' section, page 30: *"The directors are satisfied that the Group is a going concern, has sufficient profit, capital and liquidity in place and forecast, and has plans in place to strengthen that position going forward."*
- (13) 'Capital management – capital resources (audited)' section, page 80: *"The Bank's policy is to maintain a strong capital base so as to maintain investor, creditor and market confidence and to sustain future development of the business. However, the Bank still recognises the need to maintain a balance between the potential higher returns that might be achieved with greater gearing, and the advantages and security afforded by a sound capital position."*

Our submissions to the FSA in the period have shown that the Bank and its individually regulated operations have complied with all externally imposed capital requirements.

The Bank's Core Tier 1 capital position at the year end was 8.8% (2011: 9.6%). However, the Board recognises the need to build the capitalisation of the Bank to provide increased resilience and capacity for future growth. To this end, a strategic review is underway targeting growth in the Core Tier 1 ratio. Part of this was concluded in January 2013 when a risk mitigation transaction completed which would increase the year end ratio to 9.2% on a proforma basis.

Adequate capitalisation can be maintained at all times even under the most severe stress scenarios, including the revised FSA 'anchor' stress scenario.

A capital buffer above Individual Capital Guidance (ICG) is being maintained, to provide the ability to absorb capital shocks and ensure sufficient surplus capital is available at all times to cover the Bank's regulatory minimum requirements..."

- (14) 'Capital management – Capital allocation' section, page 82: *"... Since the year end, the Bank has completed a securitisation transaction to reduce risk in the balance sheet which has improved the Core Tier 1 ratio by*

0.4%. The signing of the Sale and Purchase Agreement relating to the Life and Savings business owned by The Co-operative Banking Group in 2013 is expected to further strengthen the capital position."

ANNEX A

1. JOINT INVESTIGATION

- 1.1. On 1 April 2013, a new “twin peaks” regulatory structure came into being under which the Financial Services Authority was replaced by the Authority and the Prudential Regulatory Authority (“PRA”). The effective date of that change, 1 April 2013, is known as Legal Cutover (“LCO”). Following LCO both the Authority and the PRA have an enforcement remit and are able to exercise a range of enforcement powers and impose sanctions under the Act.
- 1.2. Although the conduct to which this matter relates occurred prior to LCO, Part 5 of the Financial Services and Markets Act 2012 (Transitional Provisions) (Enforcement) Order 2013 (“Order”) permits the PRA and/or the Authority to take action to address contraventions occurring pre LCO but for which the PRA and/or the Authority would have been an appropriate regulator had the contravention occurred on or after LCO. Both the PRA and the Authority therefore have the ability to take action in this matter.
- 1.3. In January 2014, the Authority and PRA agreed to undertake a joint investigation into the potential Principle 11 breaches. The Authority and the PRA are both permitted to take action pursuant to the Order.
- 1.4. The Authority and PRA considered a joint investigation necessary because the failings encompassed both conduct and prudential issues and therefore had implications for the statutory objectives of both regulators. In particular, the matter is relevant to:
 - (1) The Authority’s overarching strategic objective of ensuring that the relevant markets function well and the advancement of the Authority’s operational objectives of (i) securing an appropriate degree of protection for consumers and (ii) protecting and enhancing the integrity of the UK financial system; and
 - (2) The PRA’s general objective of promoting the safety and soundness of PRA authorised persons by “seeking to ensure that the business of PRA-authorised persons is carried on in a way which avoids any adverse effect on the stability of the UK financial system” under section 2B(3)(a) of the Act; specifically where adverse effects may result from the lack of adequate senior management.

2. RELEVANT STATUTORY PROVISIONS

- 2.1. In discharging its general functions, the Authority must, so far as reasonably possible, act in a way which is compatible with its strategic objective and advances one or more of its operational objectives (section 1B(1) of the Act). The Authority's strategic objective is ensuring that the relevant markets function well (section 1B(2) of the Act). The Authority has three operational objectives (section 1B(3) of the Act).
- 2.2. The Authority's operational objectives are the consumer protection objective (section 1C of the Act), the integrity objective (section 1D of the Act) and the competition objective (section 1E of the Act).
- 2.3. Section 91 of the Act states:

"(1) If the [Authority] considers that:

(a) an issuer of listed securities, or

(b) an applicant for listing,

has contravened any provision of listing rules, it may impose on him a penalty of such amount as it considers appropriate.....

(3) If the Authority is entitled to impose a penalty on a person under this section in respect of a particular matter it may, instead of imposing a penalty on him in respect of that matter, publish a statement censuring him".

- 2.4. Section 205 of the Act states:

"If the [Authority] considers that an authorised person has contravened a relevant requirement imposed on the person, it may publish a statement to that effect".

3. RELEVANT REGULATORY PROVISIONS

- 3.1. In exercising its power to issue a penalty, the Authority must have regard to the relevant provisions in the Handbook of rules and guidance ("Handbook"). The Handbook provisions relevant in this matter are the Principles, the DEPP, and EG.
- 3.2. The Principles are a general statement of the fundamental obligations of firms under the regulatory system. They derive their authority from the Act's rule-

making powers and reflect the Authority's regulatory objectives. The relevant Principle in this matter is Principle 11:

Principle 11 states:

"A firm must deal with its regulators in an open and cooperative way, and must disclose to the appropriate regulator appropriately anything relating to the firm of which that regulator would reasonably expect notice"

- 3.3. The Authority's policy for imposing penalties is set out in Chapter 6 of DEPP.
- 3.4. EG sets out the Authority's approach to taking disciplinary action (Chapter 2) and issuing financial penalties (Chapter 7).
- 3.5. Listing Rule: 1.3.3R states:

"An issuer must take reasonable care to ensure that any information it notifies to a RIS or makes available through the FCA is not misleading, false or deceptive and does not omit anything likely to affect the import of the information".