
FINAL NOTICE

To: **Lloyds Bank plc**
Bank of Scotland plc

(together referred to as the "Firms")

Firm Reference Numbers: 119278 and 169628

Address: 25 Gresham Street, London, EC2V 7HN &
The Mound, Edinburgh, EH1 1YZ

Date: 28 July 2014

1. ACTION

- 1.1. For the reasons given in this notice, the Authority hereby imposes on the Firms a financial penalty of £105 million.
- 1.2. The Firms agreed to settle at an early stage of the Authority's investigation. The Firms therefore qualified for a 30% (stage 1) discount under the Authority's executive settlement procedures. Were it not for this discount, the Authority would have imposed a financial penalty of £150 million on the Firms.

2. SUMMARY OF REASONS

General

- 2.1. The Firms committed misconduct by breaching Principle 5 and Principle 3 of the Authority's Principles for Businesses through manipulating submissions to two benchmark reference rates, the Repo Rate and LIBOR, in order to seek to manipulate those rates.

Repo Rate and SLS

- 2.2. The Repo Rate benchmarked the rates offered by major banks in London for dealing GBP general collateral repo transactions, and was in operation between May 1999 and December 2012 when it was abolished.
- 2.3. The Repo Rate was used by the Bank of England to calculate the fees charged for using its SLS, which was a temporary taxpayer-backed measure to improve the liquidity position of the UK banking system during the financial crisis. The fees for drawing on the SLS were calculated by reference to the SLS Spread, which was the difference between three month GBP LIBOR and the three month Repo Rate, subject to a minimum 20 basis point spread.
- 2.4. Between them, the Firms breached Principle 5 of the Authority's Principles for Businesses from 25 April 2008 to 15 September 2009 by failing to observe proper standards of market conduct in relation to their Repo Rate submissions. The Firms routinely artificially inflated their three month Repo Rate submissions on days when the fees for drawing on the SLS were calculated in order to manipulate the SLS Spread to avoid paying the Bank of England the fees properly due to it.
- 2.5. The Firms' breaches of Principle 5 were extremely serious. The Firms relied on and benefited significantly from the SLS, a special taxpayer-backed facility introduced to assist UK financial institutions in response to the financial crisis.
- 2.6. Furthermore, because the fees that all financial institutions drawing on the SLS had to pay to the Bank of England were calculated by reference to the SLS Spread, manipulation of the Repo Rate would also have reduced any fees payable by all those other institutions on the dates concerned.
- 2.7. In addition to avoiding paying the Bank of England the SLS fees properly due to it, the Firms' misconduct also gave rise to a risk that the published Repo Rate benchmark would be manipulated and undermined the integrity of that benchmark.
- 2.8. The Firms also breached Principle 3 between 25 April 2008 and 7 June 2011 in respect of their Repo Rate submissions process and managing their participation in the SLS. Although the Firms had in place general policies and procedures concerning compliance standards which included management of conflicts of interest and required, amongst other things, staff to act with integrity, the Firms had no effective systems and controls to manage the dual roles performed by the GBP Money Market Desk (at Lloyds) and the Repo Desk (at Bank of Scotland) of making Repo Rate submissions and managing their participation in the SLS. In particular, they failed to:

- (1) Identify and manage the conflict of interest inherent in having Traders on the GBP Money Market Desk (at Lloyds) and Repo Desk (at Bank of Scotland) responsible for making Repo Rate submissions and for administering the Firms' participation in the SLS;
 - (2) Create or implement adequate policies or procedures to manage properly the way in which the Firms' Traders participated in both the Repo Rate submission process and the SLS;
 - (3) Provide adequate specific training to the Traders at both Firms who were responsible for determining Repo Rate submissions and participation in the SLS; or
 - (4) Create systems and reports to monitor Traders' activity in connection with their participation in the Repo Rate submission process and the SLS.
- 2.9. The duration and extent of the Firms' Repo Rate misconduct was exacerbated by these inadequate systems and controls.

LIBOR

- 2.10. LIBOR is a benchmark reference rate fundamental to the operation of both UK and international financial markets, including markets in interest rate derivatives contracts.
- 2.11. Between them, the Firms breached Principle 5 of the Authority's Principles for Businesses between May 2006 and June 2009 through misconduct relating to the calculation of LIBOR.
- 2.12. In order to improve the profitability of transactions on their respective Money Market desks, the Firms, through certain money market Traders (some of whom were Managers), sought to manipulate the LIBOR rate for certain currencies in the following ways:
- (1) Routine manipulation by both Firms of their GBP LIBOR submissions to benefit money market trading positions between September 2006 and June 2009;
 - (2) Manipulation from time to time by both Firms of their USD LIBOR submissions to benefit money market trading positions between January 2008 and May 2009;
 - (3) Routine manipulation by Lloyds Bank of its JPY LIBOR submissions to benefit money market trading positions from May 2006 to June 2009;
 - (4) Collusion from time to time by Lloyds Bank with Rabobank by making Requests to each other to manipulate their JPY LIBOR submissions to benefit their respective trading positions from May 2006 to October 2008; and
 - (5) Engaging in schemes of "forcing LIBOR" to influence the GBP LIBOR submissions of other LIBOR Panel Banks to benefit trading positions. Lloyds Bank engaged in at least three such schemes from September 2006

to December 2006, and Bank of Scotland engaged in at least one scheme in November 2006 and December 2006.

- 2.13. In addition, in order to avoid negative media comment and market perception about its financial strength, Bank of Scotland manipulated its GBP and USD LIBOR submissions as a result of at least two management directives in September and October 2008.
- 2.14. At both Firms there was a culture on the Money Market Desks of seeking to take a financial advantage wherever possible. For example on 19 July 2007 when a Lloyds Manager was informed by a Lloyds Trader about a Request made to another Lloyds Trader for a low JPY LIBOR, the Lloyds Trader commented that *"every little helps ... It's like Tesco's"*. The Lloyds Manager replied *"Absolutely, every little helps."*
- 2.15. The Firms' breaches of Principle 5 in respect of LIBOR were extremely serious. The Firms' misconduct gave rise to a risk that published GBP, USD and JPY LIBOR rates would be manipulated and undermined the integrity of those rates. The Firms' misconduct may have caused harm to institutional counterparties or other market participants. In addition, where Lloyds Bank colluded with Rabobank to manipulate JPY LIBOR, and where both Firms sought to manipulate other LIBOR Panel Banks' submissions by "forcing LIBOR", this misconduct significantly increased the likelihood of successfully manipulating LIBOR.
- 2.16. Despite the general policies and procedures described at paragraph 2.8, the Firms breached Principle 3 between May 2006 and September 2012 in relation to their GBP, USD and JPY LIBOR submissions process because they failed to:
- (1) Put in place any submissions-related systems and controls until March 2011;
 - (2) Identify the risk that the Traders responsible for LIBOR submissions would take into account the effect of LIBOR on the profitability of their own money market positions in determining the Firms' LIBOR submissions and failed to put in place adequate systems and controls to manage that risk; or
 - (3) Deal adequately with the BBA audit confirmation request and the FSA attestation; or
 - (4) Manage the business areas appropriately.
- 2.17. The LIBOR submissions-related systems and controls that the Firms introduced in March 2011 did reduce the risk of submissions being improperly influenced, although, as set out in paragraph 2.16(2), they nevertheless remained inadequate until September 2012.
- 2.18. As a result, the duration and extent of the Firms' LIBOR misconduct that lasted up to June 2009 was exacerbated by these inadequate systems and controls.

Penalty

- 2.19. The integrity of benchmark reference rates such as the Repo Rate and LIBOR is of fundamental importance to both UK and international financial markets. The Firms

sought to avoid paying the Bank of England the fees properly due to it and risked causing significant harm to other market participants. The Firms' misconduct also undermined the integrity of the Repo Rate and LIBOR, and threatened confidence in and the stability of the UK financial system. Repo Rate submissions and LIBOR submissions were manipulated on numerous occasions and this manipulation was condoned by a number of Managers. The Firms engaged in this serious misconduct in order to serve their own interests. The duration and extent of the Firms' misconduct was exacerbated by their inadequate systems and controls.

- 2.20. The Authority therefore considers it appropriate to impose very significant financial penalties on the Firms of £100 million for their Repo Rate misconduct and £50 million for their LIBOR misconduct.

3. DEFINITIONS

- 3.1. The following principal definitions are used in this Final Notice:

"Broker" means an interdealer broker who acted as an intermediary in, amongst other things, deals for funding in the cash markets and interest rate derivatives contracts. Brokers A and B (from two different firms) are referred to in this Notice;

"Manager" means a Lloyds Bank or Bank of Scotland individual (as indicated) with management responsibilities. A total of four Lloyds Managers are referred to in this Notice (two of whom are referred to as Lloyds Managers A and B). Two BoS Managers (BoS Managers A and B) are referred to in this Notice;

"LIBOR Panel Bank" means a bank with a place on the BBA panel for contributing LIBOR submissions in one or more currencies. Lloyds Bank, Bank of Scotland and Rabobank were LIBOR Panel Banks and are referred to in this Notice;

"Senior Manager" means a Lloyds Bank or Bank of Scotland individual (as indicated) who is more senior than a Manager, for example, one with responsibility to oversee a business area. Four BoS Senior Managers (BoS Senior Managers A to D) are referred to in this Notice; and

"Trader" means a Lloyds Bank or Bank of Scotland individual (as indicated) trading interest rate derivatives, money market instruments, repo agreements and other financial instruments. Six Lloyds Traders (Lloyds Traders A to F) are referred to in this Notice. Four BoS Traders (three of whom are referred to as BoS Traders A to C) are referred to in this Notice.

- 3.2. The following further definitions are used in this Notice:

"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;

"BBA" means the British Bankers' Association;

"BBA Guidance" means the additional guidelines circulated by the BBA's FX & MM Committee to LIBOR Panel Banks on 2 November 2009;

"Bank of Scotland" or "BoS" means the Bank of Scotland plc;

"DEPP" means the FCA's Decision Procedure & Penalties Manual;

"FCA" means the Financial Conduct Authority, which was, until 1 April 2013, known as the Financial Services Authority ("FSA");

"FCA Handbook" means the FCA Handbook of rules and guidance;

"FRA" means Forward Rate Agreement. A FRA is an over-the-counter contract between parties that determines the rate of interest, or the currency exchange rate, to be paid or received on an obligation beginning at a future start date. The borrower pays a fixed rate on the deal date agreed by the parties. Later, on a fixing date agreed by the parties, the lender will pay the floating rate, which in this case was the published LIBOR rate on that date;

"GBP" means pound sterling;

"JPY" means Japanese Yen;

"LIBOR" means London Interbank Offered Rate;

"Lloyds Bank" or "Lloyds" means Lloyds Bank TSB plc a regulated entity which changed its name to Lloyds Bank plc on 23 September 2013;

"Money Market Desk" means the trading desk with primary responsibility for trading cash and managing the funding needs of the bank;

"P&L" means profit and loss;

"Repo" means a sale and repurchase agreement. Repos are collateralised lending transactions in which one party agrees to sell securities to a counterparty in return for cash. At the time of the trade, the seller agrees to buy back from the purchaser the same or equivalent securities at a date in the future at an agreed price;

"Repo Desk" means the trading desk with primary responsibility for trading in Repos and for making Repo Rate submissions;

"Repo Rate" means the GBP BBA Repo Rate benchmark;

"Repo Rate Definition" means the rates offered by major banks in London for dealing general collateral repo transactions of normal market size with other banks at 11am London time;

"Repo Rate Panel Bank" means a bank with a place on the BBA panel for contributing GBP Repo Rates submissions. Lloyds Bank and Bank of Scotland were Repo Rate Panel Banks and are referred to in this Notice;

"Repo Trading" means trading in Repos;

"Rabobank" means Coöperatieve Centrale Raiffeisen-Boerenleenbank B.A.;

"Request" means, according to the context, a communication to adjust a LIBOR

submission to benefit a trading position or to increase a Repo Rate submission in order to reduce the fees properly due to the Bank of England under the SLS respectively;

“SLS” means the Special Liquidity Scheme;

“SLS Spread” means the difference in rates (or spread) between three month GBP LIBOR and the three month GBP Repo Rate;

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

“USD” means US Dollar.

4. FACTS AND MATTERS

BACKGROUND

The Firms

- 4.1. The Firms are wholly owned subsidiaries of Lloyds Banking Group plc, which was formed following the merger of Lloyds Bank plc (then known as Lloyds TSB Bank plc) with HBOS plc on 19 January 2009. HBOS plc is the holding company for Bank of Scotland plc. The Firms provide a wide range of banking and financial services and have both been authorised by the Authority since 1 December 2001.

Money Market and Repo Desks following merger

- 4.2. Following the merger in January 2009, each Firm’s Money Market Desk (including the Traders responsible for Repo Trading and Repo Rate submissions at Lloyds Bank and the Repo Desk at Bank of Scotland) continued to operate separately and remained in their respective offices until the end of June 2009, albeit working as part of the same banking group. From January 2009 until the end of June 2009, the newly formed Lloyds Banking Group plc reorganised and rationalised its various business areas.
- 4.3. From 1 July 2009, once the reorganisation was complete, the Money Market Desks (including Bank of Scotland’s Repo Desk which was separate from the Bank of Scotland’s Money Market Desk but shared the same reporting line) at the Firms were integrated, and the legacy Bank of Scotland employees relocated to Lloyds Bank’s Gresham Street offices.

REPO RATE and SLS BACKGROUND

Repo Rate

- 4.4. The Repo Rate was a benchmark interest rate based on Repos published by the BBA from May 1999 until December 2012 when it was abolished.
- 4.5. GBP Repo Rate submissions were made on each business day by twelve Repo Rate Panel Banks selected by the BBA. The Repo Rate Panel Banks made submissions according to the Repo Rate Definition across a range of maturities from overnight to one year. The BBA required Repo Rate Panel Banks to exercise their subjective judgement in evaluating the rates at which they were dealing general collateral repo transactions. The highest three and lowest three

submissions were disregarded and the remaining six were averaged by the BBA.

Repo Rate setting at the Firms

- 4.6. Both Firms were Repo Rate Panel Banks before the SLS was introduced. Following the merger of the Firms, Bank of Scotland plc continued to be a Repo Rate Panel Bank until 3 October 2011, as agreed with the BBA. The Firms submitted the same BBA Repo Rate from 23 January 2009 until 3 October 2011.
- 4.7. At Lloyds Bank, the responsibility for making Repo Rate submissions was assigned to certain Traders on the GBP Money Market Desk, who also had responsibility for the Firm's Repo Trading.
- 4.8. At Bank of Scotland, pre-merger and during the six months following the merger, the responsibility for making Repo Rate submissions was assigned to certain Traders on the Repo Desk (which was separate to the Money Market Desk but shared the same reporting line), who also had responsibility for the Firm's Repo Trading. These Traders were responsible for administering certain aspects of the SLS at their respective Firms and were aware of the basis upon which the SLS fee payments were calculated.

Special Liquidity Scheme ("SLS")

- 4.9. The Bank of England introduced the SLS in April 2008 to improve the liquidity position of the UK banking system. Under the terms of the SLS, banks and building societies could, for a fee, swap mortgage-backed and other securities that had temporarily become illiquid for UK Treasury Bills, for a period of up to three years. Because Treasury Bills are a highly liquid asset, they could in turn be used as collateral in Repo transactions in order to borrow cash. Institutions were able to swap assets under the SLS until January 2009. Through the SLS, the Bank of England lent Treasury Bills with a face value totalling £185 billion. The Firms' participation in the SLS ended on 7 June 2011, when they made their final SLS fee payments to the Bank of England.
- 4.10. The fee for participating in the SLS was based on the SLS Spread, which was the difference (or spread) between three month GBP LIBOR and the three month Repo Rate, subject to a minimum 20 basis points spread. This fee was calculated by multiplying the SLS Spread by the value of the Treasury Bills lent. The SLS Spread was initially fixed on the date of each swap (known as the drawdown) and was re-fixed every three months based on the prevailing SLS Spread on that date (referred to as the "SLS fixing dates" in this notice).
- 4.11. The total SLS fees paid to the Bank of England by all participating firms was £2.6 billion. The Firms were amongst the largest users of SLS. During the period of the Firms' participation in the SLS, between April 2008 and June 2011, Lloyds Bank paid £394 million and Bank of Scotland paid £884 million in SLS fees to the Bank of England. The Firms have paid an agreed amount of £7.76 million to the Bank of England in respect of losses it may have suffered in respect of SLS fees.

MANIPULATION OF REPO RATE SUBMISSIONS TO REDUCE FEES PAYABLE TO THE BANK OF ENGLAND UNDER THE SLS

- 4.12. Between 25 April 2008 and 15 September 2009, two Traders at Lloyds Bank routinely artificially inflated its three month Repo Rate submissions on SLS fixing

dates in order to manipulate the SLS Spread to avoid paying the Bank of England the fees properly due to it. In addition, from 23 January 2009 to 15 September 2009, the same Lloyds Traders routinely colluded with two Traders at Bank of Scotland on SLS fixing dates to manipulate the Repo Rate submissions of both Firms to avoid paying the fees properly due to the Bank of England.

- 4.13. The Lloyds Traders made Requests to Bank of Scotland Traders for higher Repo Rate submissions on the days when the applicable SLS Spread re-fixed because higher Repo Rate submissions from both Firms would have a greater impact on reducing the SLS Spread and therefore the SLS fees payable to the Bank of England.
- 4.14. During the period 23 January 2009 to 15 September 2009 Lloyds Trader A (who was a Manager at that time) and Lloyds Trader B between them made at least 11 documented Requests to BoS Manager A and BoS Trader A to artificially inflate Bank of Scotland's Repo Rate submissions. All of those Requests were taken into account by Bank of Scotland. Following the merger, Lloyds Bank made the same submissions as Bank of Scotland. Therefore, Lloyds Bank's submissions were also artificially inflated on those days.
- 4.15. Those Traders were aware that having two Repo Rate Panel Banks (out of the panel of 12) involved in the manipulation increased the likelihood of successfully manipulating the benchmark and therefore reducing the SLS Spread (see paragraph 4.19(2)).
- 4.16. In addition, the Traders were concerned at the level of fees that both Firms were paying to the Bank of England. On 20 April 2009, Lloyds Trader B and BoS Manager A discussed the new levels of additional SLS fees being imposed by the Bank of England for heavy users of the scheme:

Lloyds Trader B: *I think we worked out ours is going to cost us another 6.8 million quid*

BoS Manager A: *... just keeps on going up and up and up doesn't it?*

- 4.17. In the same telephone conversation, Lloyds Trader B made a Request to BoS Manager A explaining that *"...we need higher 3s because we've got a big fixing on the SLS today..."*. BoS Manager A took that Request into account when determining that day's Repo Rate submissions.
- 4.18. At no time did anyone concerned in the Requests at Lloyds Bank or Bank of Scotland refuse to take them into account, escalate any concern or provide any other challenge.
- 4.19. Examples of other Requests relating to the Repo Rate are set out below:
 - (1) In a telephone conversation on 23 January 2009, Lloyds Trader A made a Request to BoS Manager A (who was also a Trader) to increase the Bank of Scotland three month Repo Rate submission. BoS Manager A took this Request into account and made a Repo Rate submission of 1.02, instead of 1.00. Lloyds Bank's three month Repo Rate submission on that date was also 1.02:

Lloyds Trader A: *The only thing is, I like it, we try and push it, we put*

a higher rate when obviously we...

BoS Manager A: *Well do you want me to put 102 for the 3's?*

Lloyds Trader A: *Yeah do 102. It is just that we try and give a higher rate when we do the SLS obviously, so therefore we get a bit better yield on the book, are you with me?*

(2) In a telephone conversation on 1 April 2009, Lloyds Trader A made a Request to BoS Manager A explaining that *"...we have got a couple of SLS fixings today and tomorrow..."*. BoS Manager A said that he would change his submission from "69" and *"put 71 in, or whatever suits you ... you don't want to go too high because then it will set us out completely ... While we have got two votes we should use this to suit our advantage, you know what I mean?"*. BoS Manager A took account of the Request and submitted 0.71 that day. Lloyds Bank's three month Repo Rate submission was also 0.71 on that day.

4.20. From 16 September 2009, the SLS Spread moved below the 20 basis points minimum imposed by the Bank of England, so there was no benefit to the Firms in seeking to reduce the SLS Spread, and therefore the fees payable to the Bank of England for the SLS. On a number of occasions in April and May 2011 the SLS Spread moved above 20 basis points again, but then stayed below the 20 basis points minimum from 4 May 2011 until the Firms made their final payments under the SLS on 7 June 2011.

LIBOR BACKGROUND

4.21. LIBOR is the most frequently used benchmark for interest rates globally, referenced in transactions with a notional outstanding value of at least USD 500 trillion. GBP, USD and JPY LIBOR are widely used currencies in financial contracts.

4.22. During 2006 to 2012, LIBOR was published on behalf of the BBA for ten currencies with 15 maturities (including one, three and six months). LIBOR (in each relevant currency) was set by reference to the assessment of the interbank market made by a number of LIBOR Panel Banks selected by the BBA. Each LIBOR Panel Bank contributed rate submissions each business day.

4.23. These submissions were not averages of the relevant LIBOR Panel Banks' transacted rates on a given day. Rather, when making these submissions, the BBA required LIBOR Panel Banks to exercise their subjective judgement in evaluating the rates at which money may be available in the interbank market.

4.24. The definition of LIBOR during the period covered by this Notice set out the precise nature of the judgement required from LIBOR Panel Banks, namely: *"The rate at which an individual contributor panel bank could borrow funds, were it to do so by asking for and then accepting interbank offers in reasonable market size just prior to 11:00 London time."* The definition required submissions from the LIBOR Panel Banks related to funding. The definition did not allow LIBOR Panel Banks to consider factors unrelated to borrowing or lending in the interbank market.

4.25. Interest rate derivative contracts typically contain payment terms that refer to benchmark rates. LIBOR is by far the most prevalent benchmark rate used in the

over the counter (“OTC”) interest rate derivatives contracts and exchange-traded interest rate contracts.

LIBOR setting at the Firms

- 4.26. Lloyds Bank (then known as Lloyds TSB Bank plc) was a LIBOR Panel Bank throughout the period covered by this Notice and remains a LIBOR Panel Bank. Bank of Scotland plc was a LIBOR Panel Bank from September 2007 (when it took over submissions from the HBOS plc subsidiary HBOS Treasury Services plc) until it ceased to be a LIBOR Panel Bank on 6 February 2009, following the merger of the Firms on 19 January 2009.
- 4.27. Lloyds Bank was a LIBOR Panel Bank for, amongst other currencies, GBP, USD and JPY. Bank of Scotland was a LIBOR Panel Bank for, amongst other currencies, GBP and USD, but not JPY.
- 4.28. At both Firms, responsibility for making LIBOR rate submissions was assigned to certain Traders working on each Firm’s Money Market Desks in London. At both Firms, the primary function of the Money Market Desks was managing the respective funding needs of the bank through intrabank and interbank borrowing and lending transactions.

LIBOR’s relevance to money market positions

- 4.29. LIBOR was relevant to the P&L of the Money Market Desks because large new cash transactions were referenced to it and where LIBOR fixed determined the profitability of those transactions. LIBOR was also relevant to Traders’ management of existing borrowing and lending facilities. In common with money market desks at other banks at the time, Traders who were responsible for making LIBOR submissions had access to information which allowed them to predict in advance the details of these forthcoming reset or rollover transactions.

ATTEMPTS TO MANIPULATE GBP, USD AND JPY LIBOR

Manipulation of LIBOR submissions to benefit money market positions

GBP and USD - summary

- 4.30. As explained further below, at both Firms between September 2006 and June 2009:
- (1) GBP and USD Traders took Requests from other Traders into account from time to time when making GBP and USD LIBOR submissions;
 - (2) GBP Traders routinely took into account their own money market positions when making GBP LIBOR submissions; and
 - (3) USD Traders from time to time took into account their own money market positions when making USD LIBOR submissions.

GBP and USD pre-merger – September 2006 to January 2009

- 4.31. The Authority has identified communications involving Lloyds Trader A and certain Brokers in 2007 in which they discuss the manipulation of Lloyds Bank’s GBP

LIBOR submissions. For example, on 17 August 2007, Lloyds Trader A called Broker A saying, "*I ain't got any 3s fixings mate. I've got no fixings today. So I can do my LIBORs wherever I f***** want to put them, mate.*"

GBP and USD post-merger – January 2009 to June 2009

- 4.32. Because Bank of Scotland ceased to be a LIBOR Panel Bank from 6 February 2009, after this time GBP and USD BoS Traders on the Money Market Desk were no longer able to influence LIBOR submissions internally by taking their money market positions into account when making LIBOR submissions. They therefore resorted to making Requests to Lloyds Bank Traders asking them to take BoS money market positions into account when making Lloyds Bank's LIBOR submissions.
- 4.33. Between 19 January 2009 and 30 June 2009, during the post-merger reorganisation, BoS Trader B made at least five documented Requests to Lloyds Trader A and Lloyds Trader C, who were responsible for making GBP LIBOR submissions. In addition, BoS Trader C made at least two documented Requests to Lloyds Manager A and Lloyds Trader D, who were responsible for making USD LIBOR submissions.
- 4.34. The language used by the Traders in the Requests indicated that the practice of making Requests was casual and routine.
- 4.35. The Lloyds Traders understood the nature of the Requests and took them into account when making LIBOR submissions. For example:
 - (1) On 31 March 2009, on receiving a Request for a high GBP three month LIBOR submission from BoS Trader B, Lloyds Trader A replied "*I have always got loads of loans going out at the end of the month so I always try and fix it higher.*"
 - (2) On 11 May 2009, on receiving a Request for a low USD one month LIBOR submission from BoS Trader C, Lloyds Trader D automatically assumed it was because of BoS Trader C's "*fixings*". BoS Trader C also said: "*i will tell you when we have big resets as to be honest we [should] be co ordinating the libor inputs to suit the books*" to which the Lloyds Trader D replied "*of course, that is very sensible ... let me know on that day mate.*"

JPY

- 4.36. In addition, Lloyds Trader E:
 - (1) Between May 2006 and June 2009 routinely took into account Lloyds' JPY money market positions when making JPY LIBOR submissions; and
 - (2) Between May 2006 and October 2008, colluded with at least one individual at Rabobank from time to time, making at least four documented Requests to and receiving at least 12 documented Requests from Rabobank and taking into account eight of these 12 Requests.
- 4.37. The Traders were motivated by profit for their Firms as well as for personal benefit because the performance of the Money Market Desk was a factor in the size of their bonuses.

Manipulation of LIBOR submissions to benefit derivatives and other trading positions

- 4.38. On two separate occasions a BoS Trader and a Lloyds Trader located outside the UK who were not on a Money Market Desk made Requests to the Traders (at Bank of Scotland and at Lloyds respectively) responsible for determining USD and JPY LIBOR submissions at their respective firms, both of which were taken into account by the Traders making the LIBOR submissions.

FORCING LIBOR TO INFLUENCE THE LIBOR SUBMISSIONS OF PANEL BANKS

Lloyds Bank's misconduct

- 4.39. Lloyds Traders on the Money Market Desks engaged in at least three schemes from September 2006 to December 2006 to "force LIBOR". The Lloyds Traders entered into FRAs and then bid aggressively in the cash market. Whilst this was at times when the bank needed to take in cash, the primary motivation was in order to influence upwards the one month GBP LIBOR submissions of other LIBOR Panel Banks and therefore increase one month GBP LIBOR rates, which would benefit those FRAs.
- 4.40. The purpose of this activity was to artificially inflate the one month GBP LIBOR rate higher than the fixed rate of the FRA and thereby increase the profitability of those FRAs. This manipulative behaviour was called "forcing LIBOR" by Lloyds Trader F. In describing the September 2006 scheme, Lloyds Trader F explained to Broker B, who assisted in the schemes, that he had instructed Lloyds Trader A to continue bidding on Monday 25 September 2006: *"I have just told them my plan ... I want to bid everything, so all LIBORs force up the one month."* The Traders were prepared to stand by their bids, but to avoid this they engaged in these schemes during periods of market illiquidity reasoning that *"you've got to do it when people can't lend"* and therefore the likelihood of their bids being fulfilled was lessened.
- 4.41. Lloyds Traders A and F engaged in at least three schemes between September 2006 and December 2006, with the assistance of Broker B, as described below. For example:
- (1) On 21 September 2006, Lloyds Trader F and Broker B discussed on a telephone call taking positions in FRAs with the plan *"...to force the LIBOR up over a tick and a half"* to make them profitable.
 - (2) On Thursday 21 and Friday 22 September 2006, Lloyds Trader F took positions in FRAs with a notional value of £10 billion with a fixed rate of 4.925 per cent that *"fixed"* on Monday 25 September 2006.
 - (3) Broker B arranged for a Trader at another bank to be the counterparty to the FRAs having explained in a telephone conversation on 31 August 2006 that: *"I'll have [bank] there as well...because that's what you want. You don't want the market to know what you're f***** doing"*.
 - (4) On Friday 22 September 2006, Lloyds Trader F started bidding for cash in GBP money market at 4.88. That day one month GBP LIBOR fixed at 4.91.

(5) Lloyds Trader F explained to Broker B that he had instructed Lloyds Trader A to continue bidding on Monday 25 September 2006: *"I have just told them my plan ... I want to bid everything, so all LIBORs force up the one month"*. At 11:11am on 25 September, after LIBOR had fixed, Lloyds Trader A stopped bidding and one month GBP LIBOR fixed at 4.9575. As a result, Lloyds Bank made a gross profit of £266,063 on the £10 billion of FRAs.

4.42. Lloyds Trader A, Lloyds Trader F and Broker B engaged in two further schemes of "forcing LIBOR" in October and December 2006, which resulted in further gross profits on the associated FRAs of £937,336.

Bank of Scotland GBP LIBOR misconduct to benefit "rolls"

4.43. Bank of Scotland had a portfolio of assets (typically loans made to third parties) that were referenced to GBP LIBOR and re-fixed on a rolling basis for the term of the asset, which process was described as a "roll". Bank of Scotland engaged in a scheme whereby it sought to take advantage of the fact that GBP LIBOR submitters at other LIBOR Panel Banks took into account perceived conditions in the three month GBP cash market. This scheme involved increasing Bank of Scotland's bids for three month GBP cash in order to influence the perception of other GBP LIBOR Panel Banks, with the aim of causing them to increase their three month GBP LIBOR submissions. BoS Trader B engaged in at least one such scheme in November and December 2006.

4.44. BoS Trader B described this activity to BoS Manager B in the course of an email report on 4 December 2006. BoS Trader B said that, *"towards the end of the month our key focus became the reset of the large 3 month roll on the 1st of Dec where we had £6b open so about a week before this I started [sic] to gradually drive the 3's up, with a view that any funding achieved on the way would be useful"*.

4.45. BoS Trader B's primary focus was not to fulfil Bank of Scotland's cash requirements, but to improve the profitability of Bank of Scotland's GBP money market book positions which benefited from a higher LIBOR. BoS Trader B reported that LIBOR had increased: *"the net result was very successful on the libor front with... an increase of approx 3-4 bp on the week earlier."*

MANAGERIAL AWARENESS OF MANIPULATION OF REPO RATE AND LIBOR SUBMISSIONS

4.46. Certain Managers at both Firms were directly involved in or knew about and permitted the practice of manipulating submissions for the Repo Rate and GBP, USD and JPY LIBOR. As a consequence, these Managers condoned the Requests and promoted a culture on the Money Market Desks where such misconduct was accepted.

(1) Four individuals at the Firms, two of whom were Managers at the time, were directly involved in the GBP Repo Rate manipulation;

(2) 12 individuals at the Firms, four of whom were Managers were directly involved in, or aware of Requests relating to GBP, USD and JPY LIBOR;

- (3) Three individuals at Lloyds Bank (one of whom was a Manager) and two at Bank of Scotland (one of whom was a Manager) were involved in, or aware of, the forcing LIBOR schemes; and
 - (4) A total of five individuals at Bank of Scotland were involved in at least two management directives about LIBOR submissions to avoid negative media comment and market perception about its financial strength, and related misconduct, including one Manager and one Senior Manager.
- 4.47. Some Managers showed casual disregard for proper standards, creating and/or perpetuating a culture on the Money Market Desks of seeking to take a financial advantage wherever possible. For example, on 19 July 2007 when Lloyds Manager B was informed by Lloyds Trader F about a Request made to Lloyds Trader D for a low JPY LIBOR, Lloyds Trader F commented that *"every little helps ... It's like Tesco's"*. Lloyds Manager B replied *"Absolutely, every little helps."*

MANAGEMENT DIRECTIVES AT BANK OF SCOTLAND ABOUT LIBOR SUBMISSIONS TO AVOID NEGATIVE MEDIA COMMENT AND MARKET PERCEPTION

LIBOR during the financial crisis

- 4.48. Liquidity in the interbank market in London reduced significantly following the onset of the financial crisis. In the latter half of 2007 and throughout 2008, interbank lending came to a virtual standstill and there was extreme dislocation in global money markets. This reduced the information available to LIBOR submitters when determining submissions, especially in the longer tenors. These conditions persisted throughout 2008.
- 4.49. A further consequence of the solvency concerns was that the borrowing rates of the different LIBOR Panel Banks began to diverge as lending institutions became more sensitive to credit risk. Scrutiny of LIBOR submissions increased as market participants and the media sought indicators as to which banks were faring less well in the developing crisis.
- 4.50. During 2008, there was concern at Bank of Scotland about making LIBOR submissions away from the pack because Bank of Scotland management wanted to avoid negative media comments and market perception about the bank's creditworthiness. On 6 May 2008, BoS Senior Manager A emailed BoS Senior Managers B and C about USD LIBOR submissions: *"It will be readily apparent that in the current environment no bank can be seen to be an outlier. The submissions of all banks are published and we could not afford to be significantly away from the pack."*

Direct instructions at Bank of Scotland to take relative pack position into account: September and October 2008

- 4.51. On at least two occasions, in September and October 2008, a BoS Manager gave direct instructions to BoS Traders to take relative pack position into account when making GBP and USD LIBOR submissions.
- 4.52. The financial crisis and associated market turmoil reached a new level of intensity following the collapse of Lehman Brothers on 15 September 2008. On 18 September 2008, following market speculation about its solvency it was publicly

announced that HBOS plc would be acquired by Lloyds TSB Bank plc, subject to shareholder approval. As described above, the merger ultimately completed on 19 January 2009, with Bank of Scotland ceasing to be a LIBOR Panel Bank on 6 February 2009.

- 4.53. On 24 and 25 September 2008, BoS Trader C made USD LIBOR submissions that represented large increases over previous days. On 24 September 2008, Bank of Scotland's three month USD LIBOR submission was 40 basis points higher than the next highest submission. This continued on 25 September 2008, when Bank of Scotland's three month USD LIBOR submission was 55 basis points higher than the next highest submission.
- 4.54. On 26 September 2008, BoS Manager B instructed BoS Trader C to lower Bank of Scotland's USD LIBOR submissions into line with other LIBOR Panel Banks. In a Bloomberg message to a trader at another bank, BoS Trader C said *"ive been pressured by senior management to bring my rates down into line with everyone else."* Accordingly, on 26 September 2008 Bank of Scotland's three month USD LIBOR submission fell to the same level as the highest other submission, albeit it remained 44 basis points above the published LIBOR rate.
- 4.55. Over the course of October 2008 Bank of Scotland's three month USD LIBOR submissions fell into line with the level of the LIBOR fix and remained within the pack of submissions until the merger with Lloyds Bank on 19 January 2009.
- 4.56. In October 2008, in order to improve market liquidity, the Bank of England announced a scheme under which the Treasury would guarantee GBP interbank borrowing. On 21 October 2008, BoS Manager B emailed BoS Traders with responsibility for making GBP LIBOR submissions, including BoS Trader B, and wrote: *"With guaranteed issuance now setting at a spread to BBA fixings, and people evaluating our unguaranteed spread against both the fixing and our guaranteed issuance I do not want to be an outlier in BBA submissions – this could potentially create an issue with buyers of our paper. Submit 3-6 months Libors at the expected BBA level for the time being."*
- 4.57. By this email, BoS Manager B instructed BoS Trader B to depart from the LIBOR definition when making LIBOR submissions, because that would have resulted in the bank being an *"outlier"*, and to try to match the rate at which LIBOR would actually fix. BoS Senior Manager D was copied on the email and subsequently indicated to BoS Manager B that he endorsed its contents, by replying *"Agree with this"*.
- 4.58. On 21 October 2008, Bank of Scotland moved from being an outlier in its GBP submissions to being within the pack for the following two weeks.
- 4.59. Until the merger with Lloyds Bank on 19 January 2009, Bank of Scotland very rarely moved out of the pack.

THE FIRMS' SYSTEMS AND CONTROLS

Repo Rate

- 4.60. Although the Firms had in place general policies and procedures concerning compliance standards which included management of conflicts of interest and required, amongst other things, staff to act with integrity, between April 2008 and

May 2011 the Firms had no specific systems and controls to manage the dual roles performed by the GBP Money Market Desk (at Lloyds) and the Repo Desk (at Bank of Scotland) of making Repo Rate submissions and managing the participation in the SLS. In particular, the Firms did not:

- (1) Identify and manage the conflict of interest involved in having Traders on the GBP Money Market Desk (at Lloyds) and Repo Desk (at Bank of Scotland) responsible for making Repo Rate submissions and for administering the Firms' participation in the SLS, where these Repo Rate submissions affected the published Repo Rate which was used to calculate the SLS Spread and therefore the SLS fees payable to the Bank of England;
- (2) Create or implement adequate policies or procedures to manage properly the way in which the Firms' Traders participated in both the Repo Rate submission process and the administration of the Firms' participation in the SLS;
- (3) Provide adequate specific training to the Traders at both Firms who were responsible for determining Repo Rate submissions and the administration of the Firms' participation in the SLS; or
- (4) Create systems and reports to monitor Traders' activity in connection with their participation in the Repo Rate submission process and the administration of the Firms' participation in the SLS.

LIBOR

Absence of any submissions-related systems and controls until March 2011

- 4.61. Despite the general policies and procedures described at paragraph 4.60, until March 2011 neither of the Firms had any systems, controls, training or policies specifically governing the procedure for making LIBOR submissions despite: (i) commentary by the Wall Street Journal in 2008 noting the risk of derivatives trader influence; (ii) a series of communications and papers from the BBA about the integrity of the benchmark, culminating in the amended BBA Guidance in 2009 which specifically noted that derivatives traders should not be involved in the submission process; and (iii) concerns raised by a regulator in 2010 relating to USD LIBOR submissions.
- 4.62. Specifically, before March 2011, the Firms did not:
 - (1) Conduct a review of the integrity of its LIBOR submission processes;
 - (2) Have any systems, controls or policies governing the procedure for making LIBOR submissions;
 - (3) Provide training to its Traders who were responsible for making LIBOR submissions about the submissions process in relation to the appropriateness of requests for favourable submissions. As it was, new submitters were simply shown how to set LIBOR by the current or outgoing submitter; or
 - (4) Carry out any monitoring of submissions made.

Conflicts of interest and inadequate new procedures

- 4.63. Neither Firm identified the risk that the Traders who were responsible for LIBOR submissions would take into account the effect of LIBOR on the profitability of their own money market trading positions as a factor in determining the Firms' LIBOR submissions. The risk existed because Traders' bonuses were, in part, linked to the P&L of the Money Market Desks. While the risk was less obvious than the risk of derivatives trader influence identified by the BBA (referred to in paragraph 4.61 above), and at the time the BBA may have considered that money market traders were well placed to set LIBOR, this did not absolve the Firms of the obligation to identify and manage the risks associated with such an arrangement.
- 4.64. The Firms prepared written guidelines for LIBOR submissions which were finalised in March 2011 (entitled the "*LIBOR Submission Procedure Document*"). The LIBOR Submission Procedure Document stated that "*it is important that LBG's LIBOR contribution reflects the money market trader's **independent** assessment based on the definition contained within the BBA's LIBOR website. Any attempt to influence the trader's assessment by another LBG employee or by a third party must be **reported to the trader's line manager or the Director Money Markets immediately ...***" (sic; emphasis as in original). However, the guidelines did not explicitly state that Traders making LIBOR submissions should not submit so as to benefit trading positions on the Money Market Desk. The inherent conflict of interest in Traders being responsible for determining LIBOR submissions was not explicitly managed, and nor did the associated additional controls put in place in and around that time manage this conflict.
- 4.65. The LIBOR submissions-related systems and controls that the Firms introduced in March 2011 did reduce the risk of submissions being improperly influenced. Nevertheless, the risk that Traders responsible for LIBOR submissions would consider the impact of LIBOR on the profitability of trading positions on the Money Market Desk as a factor in determining Lloyds Bank's LIBOR submissions was not managed until training was delivered to Traders responsible for making LIBOR submissions in September 2012.

BBA Audit and FSA attestation

- 4.66. On 16 December 2010, the BBA requested that the Firms send "proof" that its LIBOR setting processes had undergone a BBA-mandated internal audit. At this point in time, no such audit had taken place. Although an audit of the Firms' LIBOR-submitting processes was carried out in March and April 2011, the Firms did not provide confirmation to the BBA that the required audit had taken place until 21 October 2011.
- 4.67. Lloyds Banking Group plc received a request from the Authority for an attestation to the adequacy of the systems and controls in place for its LIBOR submissions on 2 February 2011 (at which time Bank of Scotland was not a LIBOR Panel Bank, only Lloyds Bank was). Lloyds Banking Group subsequently expanded the scope of an ongoing audit of the Money Market Desk to include the LIBOR submission process. However it gave this attestation to the Authority on 16 March 2011 before this audit was complete in circumstances where the procedures introduced in March 2011 were, in any event, inadequate (as set out in paragraphs 4.63-4.65 above).

Failure to manage the business areas appropriately

- 4.68. Between May 2006 and March 2011, both Firms failed to manage their respective Money Market Desks appropriately.
- 4.69. A total of seven Managers at both Firms were aware of, and in some cases actively involved in, the LIBOR misconduct (as detailed at paragraph 4.46). All of those Managers at both Firms failed to take adequate steps to address the misconduct. As a result, those Managers were responsible for creating and/or perpetuating a culture on the Money Market Desks in both Firms where impropriety in connection with LIBOR was accepted. This is evidenced by the various manifestations of LIBOR misconduct that are described in this Notice. Taken together, these facts evidence a failure of management oversight.
- 4.70. Further, the manipulation of submissions was not detected by the Firms until after they had been asked to investigate potential issues in 2010.

5. FAILINGS

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

Principle 5

- 5.2. Principle 5 of the Authority's Principles for Businesses requires that a firm must observe proper standards of market conduct.
- 5.3. The Firms sought to manipulate the Repo Rate between April 2008 and September 2009. Accordingly, the Firms failed to observe proper standards of market conduct.
- 5.4. The Firms sought to artificially inflate their three month Repo Rate submissions in order to manipulate the SLS Spread to avoid paying the Bank of England the fees properly due to it.
- 5.5. A total of four individuals (one Manager and one Trader at each of the Firms) were involved in the Repo Rate manipulation.
- 5.6. In respect of LIBOR:
- (1) Both Firms sought to manipulate GBP and USD LIBOR submissions to benefit GBP and USD trading positions between September 2006 and June 2009;
 - (2) Lloyds Bank sought to manipulate JPY submissions to benefit JPY LIBOR trading positions between May 2006 and June 2009 and colluded with Rabobank to benefit JPY trading positions between May 2006 and October 2008;
 - (3) Lloyds Bank engaged in at least three schemes, from September 2006 to December 2006, to force GBP LIBOR and Bank of Scotland engaged in at least one such scheme, in November and December 2006; and

- (4) Bank of Scotland directed its Traders to manipulate its GBP and USD LIBOR submissions to avoid negative media comment and market perception on at least two occasions in September and October 2008.
- 5.7. Accordingly, the Firms failed to observe proper standards of market conduct in relation to GBP, USD and JPY LIBOR submissions.
- 5.8. A total of 16 individuals, of which seven were managers, were directly involved in or aware of the LIBOR misconduct.

Principle 3

- 5.9. Principle 3 of the Authority's Principles for Business states that a firm must take reasonable care to organise and control its affairs responsibly and effectively, with adequate risk management systems.
- 5.10. Both Firms breached Principle 3 during the periods set out below in relation to (i) Repo Rate submissions and management of the SLS; and (ii) LIBOR. They did not take reasonable care to organise and control their affairs responsibly and effectively. Nor did they have adequate risk management systems. The duration and extent of the Firms' misconduct within the periods set out below was exacerbated by these inadequate systems and controls.
- 5.11. The Firms' management failed to manage the relevant business areas appropriately. In fact, as noted above, certain Managers knew about (and in some cases were actively involved in) attempts to manipulate Repo Rate and LIBOR submissions.
- 5.12. During the period from April 2008 to June 2011, although the Firms had in place general policies and procedures concerning compliance standards and which required, amongst other things, staff to act with integrity, it did not have in place any specific systems, controls or policies governing its procedure for making Repo Rate submissions and to manage the SLS scheme. In particular the Firms did not take any steps to address the conflict of interest inherent in having the Traders responsible for Repo Rate submissions also managing the Firms' participation in the SLS.
- 5.13. During the period from May 2006 to March 2011, although the Firms had in place general policies and procedures concerning compliance standards and which required, amongst other things, staff to act with integrity, it did not have in place any specific systems, controls or policies governing its procedure for making LIBOR submissions. In particular the firms did not take any steps to address the conflict of interest inherent in having Traders whose trading positions depending on LIBOR being responsible for making the Firms' LIBOR submissions.
- 5.14. In early 2011, the Firms prepared written guidelines for LIBOR submissions but these were inadequate as they did not directly manage the inherent conflict of interest which was not managed until training was delivered to Traders in September 2012. As mentioned in paragraph 4.63, this was a less obvious but nevertheless significant risk.
- 5.15. In March 2011, Lloyds Banking Group attested to the Authority that its systems and controls in place for its LIBOR submissions were adequate. However this

attestation was not accurate (although the Authority does not find that this failure was deliberate).

6. SANCTION

- 6.1. The Authority imposes a financial penalty on the Firms of £100 million in respect of misconduct in connection with Repo Rate submissions and the SLS and of £50 million in respect of misconduct in connection with LIBOR submissions.
- 6.2. The Authority's policy on the imposition of financial penalties and public censures is set out in the Authority's Decision Procedure & Penalties Manual ("DEPP"). The detailed provisions of DEPP are set out in Annex A.
- 6.3. In determining the financial penalty, the Authority has had regard to this guidance. The Authority's current penalty regime applies to breaches which take place on or after 6 March 2010. However, most of the period covered by this Notice falls under the previous penalty regime, so DEPP in its pre-6 March 2010 form has been applied. The Authority has also had regard to the provisions of the Authority's Enforcement Manual ("ENF") relevant to the pre-28 August 2007 part of the Relevant Period.
- 6.4. The Authority considers the following DEPP factors to be particularly important in assessing the sanction.

Deterrence – DEPP 6.5.2G(1)

- 6.5. The principal purpose of a financial penalty is to promote high standards of regulatory and/or market 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 business. The Authority considers that the need for deterrence means that a very significant fine on the Firms is appropriate.

Nature, seriousness and impact of the breach – DEPP 6.5.2G(2)

- 6.6. The Firms' breaches were extremely serious. They took place over a number of years, across a number of LIBOR currencies and the Repo Rate. The misconduct involved a significant number of employees whose communications show that manipulation was considered accepted business practice.
- 6.7. In the case of the Repo Rate misconduct, the individuals involved in it knew that the effect of their manipulation of their Repo Rate submissions was to avoid paying the Bank of England fees properly due to it for the participation of the Firms in the SLS.
- 6.8. The SLS was a taxpayer-backed scheme introduced by the Bank of England in 2008 to assist UK banks and building societies during the financial crisis. The Firms' misconduct in manipulating their Repo Rate submissions in order to reduce the SLS Spread, and therefore avoid paying the Bank of England fees properly due to it, shows a complete disregard for proper standards.
- 6.9. The communications indicate that manipulation of GBP LIBOR submissions by the Firms and JPY LIBOR by Lloyds Bank was routine, and in addition, from time to time USD LIBOR submissions were manipulated by the Firms.

- 6.10. In respect of LIBOR, the Firms' misconduct extended beyond manipulating its own internal GBP, USD and JPY LIBOR submissions to suit trading positions to attempts to manipulate LIBOR or influence the submissions of LIBOR Panel Banks by (i) both Firms engaging in "forcing LIBOR" schemes to benefit derivative and money market trading positions (Lloyds Bank engaged in at least three such schemes and Bank of Scotland engaged in at least one such scheme); and (ii) by Lloyds Bank colluding with Rabobank to manipulate JPY LIBOR submissions from time to time. In addition, on at least two occasions Bank of Scotland manipulated GBP and USD LIBOR submissions to avoid negative media comment and market perception.
- 6.11. The Authority acknowledges that the frequency of documented LIBOR Requests is lower than at other firms who have been the subject of disciplinary action by the Authority for LIBOR manipulation.
- 6.12. LIBOR is the prevalent benchmark reference rate in a number of relevant markets including markets in OTC derivatives contracts and futures contracts traded on exchanges such as LIFFE in London. LIBOR also has a wider impact on other markets. The integrity of benchmark reference rates such as LIBOR is of fundamental importance to both UK and international financial markets. The Firms could have caused harm to institutional counterparties or other market participants if the final LIBOR fixes were affected by the actions of the Firms' managers and employees on any given day.
- 6.13. The Firms had no systems and controls in place in respect of Repo Rate submissions and their participation in the SLS. There were also serious systemic weaknesses in the Firms' systems and controls in relation to LIBOR, and the systems and controls introduced in March 2011, although reducing the risk of LIBOR submissions being improperly influenced, were inadequate. The duration and extent of the Firms' Repo Rate and LIBOR misconduct was exacerbated as a consequence.
- 6.14. The Firms' misconduct threatened the integrity of these benchmarks, the orderliness of the markets and confidence in and the stability of the UK financial system.

The extent to which the breach was deliberate or reckless – DEPP 6.5.2G(3)

- 6.15. The Authority does not conclude that either Lloyds Bank or Bank of Scotland as firms engaged in deliberate misconduct. Nevertheless, the improper actions of many Lloyds Bank and Bank of Scotland employees involved in the misconduct were at least reckless and frequently deliberate. The Firms, because of a poor culture on their Money Market Desks and weak systems and controls, failed to prevent the deliberate, reckless and frequently blatant actions of a number of their employees.

The size, financial resources and other circumstances of the firm – DEPP 6.5.2G(5)

- 6.16. Both Firms are large, sophisticated and well-resourced financial services institutions. Serious breaches committed by such a firm merit the highest penalties.

The amount of benefit gained or loss avoided – DEPP 6.5.2G(6)

- 6.17. Traders at the Firms sought to manipulate the Repo Rate in order to reduce the amount of fees payable to the Bank of England for use of the SLS. The Authority has not determined the amount of benefit gained. In addition, Traders at the Firms sought to manipulate LIBOR submissions in order to improve the profitability of trading positions.

Conduct following the breach – DEPP 6.5.2G(8)

- 6.18. In determining the appropriate level of penalty, the Authority acknowledges the cooperation provided by the Firms during the course of the Authority's investigation. The Authority acknowledges that, in line with their obligations, the Firms identified the BBA Repo Rate issue and promptly reported it to the Authority. The Authority further acknowledges that the Firms have paid an agreed amount of £7.76 million to the Bank of England in respect of losses it may have suffered in respect of SLS fees.

Disciplinary record and compliance history – DEPP 6.5.2G(9)

- 6.19. Before and during the period covered by this Notice, the Authority issued one Final Notice against Lloyds Bank and two Final Notices against Bank of Scotland:
- (1) In September 2003, the Authority imposed a penalty of £1.9 million on Lloyds TSB Bank plc (now known as Lloyds Bank plc) for systems and controls breaches in relation to its conduct in selling high income bonds between October 2000 and July 2001;
 - (2) In May 2011, the Authority imposed a penalty of £5 million (£3.5 million after the 30% discount for settling at stage 1) on Bank of Scotland for breaches of Principle 3 and Principle 6 between July 2007 and October 2009 relating to its handling of complaints relating to retail investments; and
 - (3) In March 2012, the Authority imposed a public censure on Bank of Scotland for breaches of Principle 3 between January 2006 and December 2008 relating to the management and control of its corporate lending.
- 6.20. Since the end of the period covered by this Notice, the Authority has also issued one Final Notice against Bank of Scotland and two joint Final Notices against the Firms:
- (1) In October 2012, the Authority imposed a penalty of £6 million (£4.2 million after the 30% discount for settling at stage 1) on Bank of Scotland plc for breaches of Principle 3 in relation to incorrect mortgage terms and conditions that it gave to standard variable rate customers;
 - (2) In February 2013, the Authority imposed a penalty of £6,164,327 (£4,315,000 after the 30% discount for settling at stage 1) on Lloyds TSB Bank plc, Lloyds TSB Scotland plc and Bank of Scotland plc for breaches of Principle 3 (and DISP 1.4.1R(5)) between May 2011 and March 2012 relating to their failures to pay redress promptly to PPI complainants; and

- (3) In December 2013, the Authority imposed a penalty of £35,048,500 (£28,038,800 after the 20% discount for settling at stage 2) on Lloyds TSB Bank plc and Bank of Scotland plc for their breaches of Principle 3 between 1 January 2010 and 31 March 2012 relating to serious failings in the systems and controls governing the financial incentives that they gave to sales staff.

- 6.21. The failure of the Firms to establish and maintain adequate systems and controls in the above cases is not wholly similar to this case and, with the exception of the March 2012 Final Notice, the cases do not relate to the wholesale banking businesses of the Firms. However, all six previous matters highlight the inadequacies of the Firms (both members of Lloyds Banking Group plc) in implementing adequate systems and controls for their different business areas.

Other action taken by the Authority – DEPP 6.5.2G(10)

- 6.22. On 27 June 2012, 19 December 2012, 6 February 2013 and 29 October 2013, the Authority issued Final Notices against Barclays Bank plc, UBS AG, The Royal Bank of Scotland plc and Rabobank in respect of misconduct similar to the Firms' misconduct as described in this notice. The Authority has considered the Firms' misconduct relative to other firms in determining the penalty.

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.

Manner of and time for Payment

- 7.3. The financial penalty must be paid in full by the Firms to the Authority by no later than 11 August 2014, 14 days from the date of the Final Notice.

If the financial penalty is not paid

- 7.4. If all or any of the financial penalty is outstanding on 12 August 2014, the Authority may recover the outstanding amount as a debt owed by the Firms and due to the Authority.

Publicity

- 7.5. 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.

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

Authority contacts

- 7.7. For more information concerning this matter generally, contact Nick Bayley (direct line: 020 7066 5342) or Kate Lloyd (direct line: 020 7066 1258) of the Enforcement and Financial Crime Division of the Authority.

Therese Chambers

Project Sponsor
Financial Conduct Authority, Enforcement and Financial Crime Division

ANNEX A

RELEVANT STATUTORY PROVISIONS, REGULATORY REQUIREMENTS AND FCA GUIDANCE

1. STATUTORY PROVISIONS

1.1. The FCA's statutory objectives, set out in section 2(2) of the Act, are market confidence, financial stability, consumer protection and the reduction of financial crime.

1.2. Section 206 of the Act provides:

"If the Authority considers that an authorised person has contravened a requirement imposed on him by or under this Act, it may impose on him a penalty, in respect of the contravention, of such amount as it considers appropriate."

1.3. Lloyds Bank and Bank of Scotland are authorised persons for the purposes of section 206 of the Act. The requirements imposed on authorised persons include those set out in the FCA's rules made under section 138 of the Act.

2. REGULATORY PROVISIONS

2.1. In exercising its power to issue a financial penalty, the FCA must have regard to the relevant provisions in the FCA Handbook of rules and guidance (the FCA Handbook).

2.2. In deciding on the action, the FCA has also had regard to guidance published in the FCA Handbook and set out in the Regulatory Guides, in particular the Decision Procedure and Penalties Manual (DEPP).

Principles for Businesses ("PRIN")

2.3. The Principles are a general statement of the fundamental obligations of firms under the regulatory system and are set out in the FCA's Handbook. They derive their authority from the FCA's rule-making powers as set out in the Act and reflect the FCA's regulatory objectives. The relevant Principles are as follows:

2.4. Principle 3 provides:

"A firm must take reasonable care to organise and control its affairs responsibly and effectively, with adequate risk management systems."

2.5. Principle 5 provides:

"A firm must observe proper standards of market conduct."

Decision Procedure and Penalties Manual (DEPP)

2.6. Guidance on the imposition and amount of penalties is set out in Chapter 6 of DEPP. Changes to DEPP were introduced on 6 March 2010. Given that the majority of the misconduct occurred prior to that date, the FCA has had regard to the provisions of DEPP in force prior to that date.

- 2.7. DEPP 6.1.2 provides that the principal purpose of imposing a financial penalty is to *"promote high standards of regulatory and/or market conduct by deterring persons who have committed breaches from committing further breaches, helping to deter other persons from committing similar breaches, and demonstrating generally the benefits of compliant behaviour."*
- 2.8. DEPP 6.5.2 sets out some of the factors that may be taken into account when the FCA determines the level of a financial penalty that is appropriate and proportionate to the misconduct as follows:
- (1) deterrence;
 - (2) the nature, seriousness and impact of the breach in question;
 - (3) the extent to which the breach was deliberate or reckless;
 - (4) whether the person on who the penalty is to be imposed is an individual;
 - (5) the size, financial resources and other circumstances of the person on whom the penalty is to be imposed;
 - (6) the amount of benefit gained or loss avoided;
 - (7) difficulty of detecting the breach;
 - (8) conduct following the breach;
 - (9) disciplinary record and compliance history;
 - (10) other action taken by the FCA;
 - (11) action taken by other domestic or international regulatory authorities;
 - (12) FCA guidance or other published materials; and
 - (13) the timing of any agreement as to the amount of the penalty.
- 2.9. The FCA has also had regard to the provisions of the Enforcement manual (ENF) in force prior to 28 August 2007, in relation to misconduct which occurred prior to that date.