

## INFORMATION FOR SHAREHOLDERS:

# UPDATE ON HISTORIC FAILURES AT HBOS READING

### BACKGROUND

Six people, two of them former employees of HBOS, were convicted and sentenced to up to 12 years in prison for criminal misconduct between 2003 and 2007 through the HBOS Impaired Assets Division, London and South East Region, based in Reading ('HBOS Reading'). The convictions in January 2017 for conspiracy to corrupt, fraudulent trading and associated money laundering offences followed a police inquiry that began in mid-2010.

HBOS was acquired by Lloyds Banking Group in 2009. The Board and management team of Lloyds Banking Group have fully accepted the seriousness of the events centred on HBOS Reading which occurred prior to the acquisition and have been extensively engaged in leading the Group's response. The Group has publicly apologised for the harm done to victims and it has worked with the police, regulators and other authorities to get to the bottom of what happened and to ensure that the victims are treated fairly and compensated appropriately.

Following the outcome of the trial and after extensive consultation with the FCA, the Group announced two key steps designed to address customer and public concerns and to restore confidence.

- 1. An independent customer compensation review:** In February 2017, the Group committed to reviewing the cases of all customers who might have been affected by criminal activities linked to HBOS Reading and to provide them swift and fair compensation. After consultation with the FCA, Professor Russel Griggs OBE was appointed as the independent reviewer to conduct the HBOS Reading customer case review. Further detail on progress is set out below. Now the review has completed its work and closed to new complaints we have announced an independent quality assurance review will be undertaken. We have agreed with the FCA that the review will be led by Sir Ross Cranston.
- 2. An independent review into how the Group handled the issue after acquiring HBOS in 2009:** While the criminal activity at HBOS Reading preceded the Lloyds Banking Group acquisition, the Group's Board has recognised legitimate questions over whether the issues relating to HBOS Reading were properly investigated and appropriately reported to the authorities following the acquisition. The Board therefore in April 2017 appointed Dame Linda Dobbs, a retired High Court judge, to undertake an independent review into these matters. The Group has committed to making the findings of Dame Linda's review available to regulators and to MPs in the House of Commons' Treasury Committee

The summary provided below is intended to help keep shareholders informed about these and other external investigations into the HBOS Reading events.

## **ONGOING INVESTIGATIONS INTO HBOS EVENTS PRIOR TO LLOYDS ACQUISITION**

The FCA and its predecessor, the FSA, have undertaken a number of investigations into the management of HBOS prior to its acquisition by the Group in 2009. The FSA issued a Final Notice and censure in March 2012 that concluded HBOS Corporate Banking Division had failed to take reasonable care to organise and control its affairs responsibly and effectively. In this notice the FSA highlighted the serious breakdown of controls in HBOS Reading.

The element of the FSA investigation into events surrounding the discovery of misconduct at HBOS Reading between June 2006 and May 2009 was suspended during the course of the police investigation, at the request of the police. Following the convictions in early 2017 the FCA recommenced this investigation. The process is ongoing and nearing a conclusion. The Group continues to provide its full cooperation to the FCA in producing their findings so that it can establish a clear picture of what happened during this period. We are committed to working with the FCA to respond to any findings that emerge.

The investigation by Thames Valley Police (TVP) into fraud associated with HBOS Reading led to the successful conviction of six individuals in January 2017. On 30<sup>th</sup> April 2018, the National Crime Agency (NCA) announced that it would lead a pre-investigative review of evidence related to further allegations of fraud at HBOS Reading that fell outside the scope of the original police investigation. The purpose of this work is to determine whether there are sufficient grounds to launch further criminal investigations. The decision for the NCA to lead this review was reached after discussions between the FCA, SFO and other police forces. TVP's investigation is also ongoing. The Group continues to assist the NCA and TVP with their reviews to ensure any further potential crimes associated with these events are fully investigated.

## **LLOYDS ENGAGEMENT FOLLOWING ITS ACQUISITION OF HBOS**

HBOS Reading has received senior level attention from Lloyds Banking Group since HBOS was acquired in 2009. After initial exchanges with the regulator in the first half of 2009, a formal review into the events at HBOS Reading was instructed in conjunction with the FSA in September 2009. This review reported in March 2010 and the information that came to light during this review helped the police to commence their criminal investigation later in 2010 which ultimately led to the January 2017 convictions.

### **Supporting the Police & Regulator Investigations**

Whilst the police investigation was on-going, the Group's focus was to support their activity and avoid other actions that could prejudice any subsequent trial. This was consistent with the police request that the FSA suspend their investigations. A team with legal support was set up in the Group to provide the information required by the police, under the governance of a senior executive committee. During this period the Group was necessarily constrained in what it could do and say in relation to the on-going criminal investigation and a number of ongoing customer disputes were placed on hold while the police investigation was underway.

The Group supported the police investigation with the provision of a substantial volume of documents and witness statements. Separately, the police were able to use their extensive investigatory powers to pursue their inquiries in ways which were not open to the Group, including the ability to interview witnesses under caution and to gather information held outside of the Group.

Following the trial the Board established the independent review under Dame Linda Dobbs to assess whether the issues relating to HBOS Reading were properly investigated and appropriately reported to the relevant authorities after its acquisition of HBOS in 2009 until the end of the criminal trial in January 2017. This includes consideration of the Group's support for TVP and its handling of a document known as the 'Project Lord Turnbull Report'. This document was prepared by a former employee and notes in its introduction that it comprises detail from an interview that the employee had with TVP in July 2013. When received by the Group it was passed through our governance arrangements to the Regulator and the Police for their use in their ongoing enquiries into events at HBOS prior to Lloyds' acquisition. A joint statement with the author issued in November 2018 noted that the author acted in good faith and integrity

in assisting the police investigation and in raising her concerns with the Group and confirmed that these concerns were documented following a request from the Group that she set out her concerns in writing. Both the Group and our former employee have agreed that Dame Linda Dobbs' review is the appropriate forum for considering matters in relation to the report.

### Compensating customers impacted by the HBOS Fraud

Once the trial concluded and the risk of prejudice had passed, the Group sought to move quickly to set up a voluntary review to provide offers of compensation to customers whose businesses had been impacted by the fraudulent activities at HBOS Reading. Our aim was to avoid the delay and cost involved from customers having to pursue claims through the courts. The independent review under Professor Griggs OBE was established to provide compensation for any financial or consequential loss suffered and for the distress and inconvenience they had been caused by the events themselves. All these elements were taken into account in Professor Griggs' determination of the compensation level, with the Board setting the objective of providing fair compensation which would exceed that available to victims through a lengthy and costly legal process.

We are pleased to report that all of the 71 business customers and their directors that have participated in the customer compensation review have now received offers and that all but a handful of those offers have been accepted. We continue to engage with a small number of customers who have rejected their offers and who are now pursuing their claims separately. We are also pleased that the two business customers who chose not to participate in the Review have reached separate consensual settlements with the Group. We continue to have confidence that this compensation process, in which Professor Griggs has had full discretion to exercise his independent judgement, has resulted in fair outcomes for customers. We do however recognise the need for public confidence in this review and we have therefore announced our commitment to instruct an additional review to provide assurance that customer outcomes have been both fair and reasonable and to identify any lessons to be learned. We have agreed with the FCA that this Assurance Review will be undertaken by Sir Ross Cranston.

### **NEXT STEPS**

The Board and Executive of Lloyds Banking Group recognise that the criminal activities that took place in HBOS Reading over a decade ago have not only had a damaging impact on the lives of those customers affected but have also cast a long shadow in undermining confidence and trust more widely. We are determined to rebuild that trust by ensuring the various investigations get to the bottom of what went on. As the FCA, NCA, TVP and Dame Linda Dobbs reviews are all on-going it would not be appropriate for the Group to comment on their work or prejudge their findings, but we have no doubt there will be lessons to be learned. We continue to assist all of these investigations.