international banks operating across all the banking disciplines are actually too complex to be governed by a traditional exec/non-exec format?

Mr Thurston: We have, as you well know, an executive chairman, and we do believe that it is very important for a group of our size and geographic reach—

Q1976 John Thurso: Which is to clarify he is in contravention to the model code.

Mr Thurston: There is clear separation of responsibilities between the Chairman and the CEO but he is an executive. With the scope and breadth of our activities, that is important. Our board of non-executive directors at a group level has a number of leading businessmen and women who have run businesses on a multi-national basis. In the UK bank we have a board of senior people, we have an audit committee, which is one of the key committees which oversees the risk management of the board: there are three members of that, they are all non-executive, each of them has 30 years' of experience in either the banking or financial services or accountancy business. So it does require significant experience in those roles.

Q1977 John Thurso: Mr Hester, can I come to you? I look at RBS, a once proud Scottish banking institution, British banking institution, brought to its knees. I look at those names on that non-executive board and say to myself, how come none of them said, "No, this is nuts"? You have come in, new broom, and I am sure are going to do a great job. What would you like to see done to make sure that kind of thing does not happen? What is the lesson in this for corporate governance?

Mr Hester: This is a really, really difficult question. Obviously, I was not there in the past, so I cannot comment on that other than to say that I think that the criticisms being thrown around are, in some cases, harsh but, obviously, the mistakes are there for all to see. I think that all companies struggle with the non-executive balance, and it gets down to humans rather than process, and it is really incumbent that you have an executive that wants strong challenge and that gives information to enable it, and it is equally important that non-executives understand that, because it is their job to help the companies succeed. Helping the company succeed does not always mean saying, yes, to the chief executive, it can mean a challenge, constructive challenge, but I have to tell you, I am not sure this is an issue of process. I think it is, unfortunately, an issue of humans and their behaviour.

Q1978 John Thurso: Mr Varley, one of the things that came out of yesterday's session was the fact that the investment merchant banking side came out of the partnership tradition, which is a wholly different culture, wholly different way of taking risk, wholly different remuneration. Banks came out of stock holding, people owning shares. Is it the case that we ought to really go back to something akin to Glass-Steagall where there is a separation, because the two cultures simply do not mix? Is it that corporate governance just cannot take care of the swash buckling side of the business?

Mr Varley: I saw the comment, and to me it was a very interesting comment. Going back to your question about governance and the composition of boards, I certainly find it very helpful around the Barclays Board table to have three of our non-executive directors who have significant investment banking experience. I am not suggesting for one moment that you want to have on a bank board a non-executive director cadre that is made up of former bankers, but I think it is extremely desirable to have at the board table people who understand the industry and, in particular, the most esoteric parts of it, and that would cover the investment banking world. It is no coincidence in our case that we, including our chairman, have an investment banking background. That is a very conscious decision. I certainly find it very helpful as a chief executive to know that I get that challenge from people who understand intimately the financial services industry and even the more abstruse parts of it.

John Thurso: We are going to write a report. We are going to make recommendations. Would you all like to reflect and give us a measured, written response?

Chairman: In answer to our question yesterday to Sir Tom McKillop, I put the puzzle that we had Sir Peter Sutherland, a former EU Commissioner, chairman of Goldman Sachs. We had Steve Robson, number two at the Treasury when the tripartite authority was established. We had Jim Currie who works at the EU. We could go on. Either people are stupid or there is something systematic. These people have an excellent track record so there must be some systematic issue and problem here. We have to push at that because I am coming to the view that maybe banks are different from other organisations and what we need in boards. If you can contribute to that for us, it would be very helpful.

Q1979 Mr Tyrie: I wanted to ask one follow up question to Mr Daniels about the HBOS deal. You said that it was a very prudent one. What due diligence did you do before you went ahead with that deal?

Mr Daniels: As a publicly traded company, there is a limited amount of diligence that can be done in an acquisition. That said, we put approximately 5,000 man days into the diligence effort. A great part of that was done by people that we had hired as experts, accounting firms, investment banks and so on, in an effort to value the portfolios properly.

Q1980 Mr Tyrie: If you had had more time, how many man hours would you expect to put in?

Mr Daniels: If we had unlimited access, which is not permitted by the law—

Q1981 Mr Tyrie: To a similar company but with more time.

Mr Daniels: We probably would have put in somewhere around three to five times as much time as we put in.

Q1982 Mr Tyrie: Since you have only just taken over on 19 January, how can you be so confident that it was a very prudent deal? You must be still doing the due diligence now.
Mr Daniels: We very clearly are learning and assembling a database in order to be able to run the company well.

Q1983 Mr Tyrie: How comfortable are you about the quality of the assets? Is it better, worse or about the same as you thought on the basis of the very incomplete due diligence you did?
Mr Daniels: The outcomes that we have seen thus far are within the ranges that we forecast.

Q1984 Mr Tyrie: You are very confident you are not suddenly going to have to come forward to us and to the public to tell us that there is a whole basket full of toxic assets which you had not foreseen being there?
Mr Daniels: Based on what we have seen thus far, we believe that we are well capitalised as a group.

Q1985 Mr Tyrie: Do you think this was a commercial transaction? Do you think it should be described as such?
Mr Daniels: I believe it should be.

Q1986 Mr Tyrie: You do not think there was a political element to this deal?
Mr Daniels: I believe that it was a good deal for Lloyds TSB.

Q1987 Mr Tyrie: Do you think there was a political element to this deal?
Mr Daniels: Very clearly, there was a clearance by government to help us with the Competition Commission so to that extent, yes, there was involvement by government.

Q1988 Mr Tyrie: I want to ask the others here whether they have any concerns about the fact that there was that political element and therefore competition was being reduced in the industry. Do not all feel obliged to comment but, if you do want to add something, perhaps we can go right to left. Are you concerned by the diminution of competition?
Mr Thurston: I think it is something we have to look out for in the future in terms of the way these businesses are managed to ensure there is no diminution in competition, as we should do in all such cases.

Q1989 Mr Tyrie: You do not think there will be?
Mr Thurston: I think it was the right decision to put aside the competition rules at a time of crisis, to take decisions. I think that is understandable, but we have to make sure that in doing so what results at the end of it is not anti-competitive. We have not had the ability to study the details of what the combined entity will be like and how it will operate.

Q1990 Mr Tyrie: Do you think we are going to be able to unwind it?
Mr Thurston: I am not sure.

Q1991 Mr Tyrie: Mr Varley?
Mr Varley: I think what was done had to be done at the time. I also take some comfort from the fact that the European Union takes an interest in the competitive landscape and will have an overview as to whether there is any distortion. If you are asking whether there will be any distortion, I believe not.
Mr Hester: I agree with my colleagues.

Q1992 Mr Tyrie: Do you want to add anything?
Mr Daniels: No.
Mr Tyrie: I am amazed by those replies. I would have thought you would be very concerned in the long term about competition in your industry. All I can suggest is that you come forward with some other deal which can give you a disproportionate slug of some other market.

Q1993 Chairman: On the issue of due diligence, a very experienced, senior, distinguished individual said to me, in terms of the complexity of some banks as organisations, that it could take a year to go through books and fully understand what is on the books, what are the risks and obligations. Is that way off the wall for you?
Mr Thurston: It would depend on the size of the organisation and the nature of its business.

Q1994 Chairman: You could envisage something like that with the complex organisations we have today?
Mr Thurston: That would be a very large, complex acquisition for that length of time.

Q1995 Mr Fallon: Stephen Hester, your majority shareholder, UKFI, has the objectives of protecting and creating taxpayer value, maintaining financial stability and promoting competition. How can all those objectives be reconciled?
Mr Hester: In my engagement with them so far, which has been significant, I think that they have been behaving like a very engaged institutional shareholder in relation to what I will call the strategic and shareholder value type issues. They do have other mandates that are not about shareholder value but are to do with the lending commitments, pay and those sorts of things, which are a little more political in terms of the engagement we have with them. Nevertheless, I certainly have no fears at the moment in terms of the way UKFI specifically are going about their job.

Q1996 Mr Fallon: Eric Daniels, how can they promote competition at the same time as protecting taxpayer value?