THE MOST SERIOUS FINANCIAL SCANDAL OF MODERN TIMES

13. LLOYDS ASSET THEFT FRAUDS – ENGINEERING THE DEFAULT

- Under the Basel agreements, international standards were agreed for how much capital banks should be required to hold in order to guard against financial and operational risks. The 2008 global financial crisis occurred before Basel II became fully effective. Under Basel III, more stringent standards were quickly adopted in key countries including those in Europe and the US. Under Basel III, a bank's tier 1 and tier 2 assets had to equate to at least 10.5% of its risk-weighted assets, up from 8% under Basel II.

- In the aftermath of the crisis, banks took steps to improve their capital ratios. However, some of the methods used by banks such as Lloyds and RBS were not legitimate.

  Given that the UK is facing another round of major insolvencies, it is important that business customers are made fully aware of the extensive wrongdoing, which took place in the aftermath of the previous banking crisis.

  Engineering the default

- **Core and non-core:** Banks such as Lloyds knew that once capital had been re-allocated from non-core assets to core, it could be lent at a greater multiple to a higher quality borrower. Thus, if the bank incurred a loss by defaulting a lower grade, non-core customer, the loss could be offset against tax and the bank would derive greater profits from the higher quality borrower.

- For the lower grade, non-core customer, who had been placed in Lloyds Business Support Unit (BSU), which after 2007 became a profit centre, their loan was then instantly callable and they were subjected to higher interest and other financial penalties. Escape became difficult, if not impossible.

- The distinction between core and non-core was emphasised by the global private investment company, Legatum, which made a “significant investment” in Lloyds Banking Group in 2011. The company stated that Lloyds’ “stock price more than doubled in the 24 months that followed”. However, Legatum’s shareholding was only short-term.

- **Larger business customers had their defaults engineered.** This could be done in several ways:

  (1) Re-assessment of loan-to-value (LTV) – a revaluation which significantly undervalued the business’ assets and put them in to breach of their covenants.

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(2) Technical breach of covenants – such as a temporary dip in EBITDA or caused by a late submission of information. These are often breaches that have no bearing on the performance or viability of the business.

(3) Removal of, or change to banking facilities and the move to asset-based finance.

- **Leading accounting firms, such as KPMG and PWC**, acting as agents for the bank, were often involved, with their "Trojan Horse" mechanism working like this from their viewpoint:

  - Gain an introduction to the company: always on an amicable basis. Become a non-executive director.

  - Befriend them: Persuade the company's owners that you are there to help and are working in their best interests, even if this is not the case. Obtain full access to the accounts. Avoid formal instructions.

  - Recommend an Independent Business Review (IBR), which is never independent but is invariably very expensive. Avoid giving a complete version of the report to the company's owners. This will be reserved for the bank. Valuations will be downgraded, enabling loan-to-value (LTV) covenants to be broken in due course.

  - Introduce a turnaround professional, who will work with you and the bank and against the company's owners. This is despite the turnaround professional being officially the client of the customer, being paid by the customer and therefore according to contract law and the Turnaround Professionals' code of conduct, bound to act in the interests of the customer.

  - Restructure the finances and security to gain control: Demand extra security including personal guarantees. Introduce an adviser / manager to convey falsely the impression of independence.

  - Once that has been done, the company's owners have lost control, without even noticing the subtle changes in position.

- **Smaller businesses also had their defaults engineered.** This often involved the escalation of punitive interest rates including the unilateral imposition of fixed rate borrowing terms, as well as the manipulation of property valuations to achieve engineered loan-to-value covenant breaches. They have borne the use of false bankruptcies as a principal means of weakening targeted customers; conspiracy to defraud through false representation, failing to disclose information and abuse of position. Lloyds' officers have also compelled customers to accept and pay for supposedly Independent Business Reviews (IBRs) by accounting firms or sole practitioners to achieve the desired outcome for the bank. Such moves, however, were only the forerunners of much greater misconduct to come.

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