

Philip Hampton
Chairman

22nd August 2014

Andrew Tyrie MP
Treasury Committee
House of Commons, Committee Office
7 Millbank
London
SW1P 3JA

Gogarburn
Edinburgh
EH12 1HQ
Telephone: 0131 556 8555
Direct: 0131 523 2672
Facsimile: 0131 523 5812
www.rbs.com

Dear Andrew,

Thank you for your letter of 23rd July 2014. I welcome the opportunity to respond before the Treasury Select Committee considers this matter again. I have also had the chance to read Sir Andrew Large's very clear letter of 8th July to the Committee which I had not previously seen.

The matter you raised - whether or not RBS executives misled the Committee - is of course a very serious one. The evidence the bank's representatives provided was not correct in answering the question as to whether GRG was a profit centre in the terms Sir Andrew described in his November 2013 report. This lack of clarity on an important point is very disappointing to the Committee as it is to me and I apologise for it.

In order to help you assess whether or not the Committee was misled Ross McEwan and I, supported by a number of our senior colleagues, have undertaken a review of the specific issues in question. I have discussed the evidence given to the Committee directly with Chris Sullivan and Derek Sach. We have also reviewed the evidence and relevant documents and correspondence. I have set out below the areas where answers to the Committee in my view were not correct or require further clarification.

In addition to Mr Sullivan failing to recall he had reviewed a draft of the Clifford Chance report (as explained in his letter of 15th July), there are two key areas where evidence to the Committee was not correct, or could at least be seen as conflicting with Sir Andrew's evidence to the Committee. I have addressed these below. I have also asked Mr Sullivan and Mr Sach to review their evidence thoroughly and to bring to your attention any additional areas that they believe need further clarification or correction (and also to provide to you any details that they committed to respond to you on during their testimony). Mr Sach has written to you separately to do this. Mr Sullivan does not have anything further to say beyond his comments to you in his letter of 15th July.

Was Sir Andrew Large's description of GRG as a Profit Centre correct?

In his Independent Lending Review, Sir Andrew said that GRG was run as an "internal profit centre". He defined this as "internal organisational boundaries defined to measure the financial contribution of a particular area of a larger organisation". Senior GRG representatives including Mr Sach reviewed relevant extracts from Sir Andrew's draft report. Other senior RBS representatives reviewed the whole report. None of them took issue with his use of the "profit centre" definition.



The answer to whether Sir Andrew was right is “yes”; his definition was reasonable and correct as it applies to GRG. Having read his 8th July letter it is plain that that is the answer the Committee should have received and I am sorry that they did not.

In his 8th July letter Sir Andrew notes that “the possibility remains that the bank feels that the term “profit centre” in some way adds to any public perception that the presence of such a mechanism leads to a systematic abuse of the bank’s position... ”Mr Sach and Mr Sullivan have confirmed that when providing evidence to the Committee their responses were informed by their reaction to this adverse characterisation of “profit centre”.

This was a mistake. Your questions and those of your colleagues were clear. Based on the review we have undertaken my colleagues on the Board and I believe it was an honest mistake and that neither of the bank’s representatives intended to mislead the Committee. When the clear definition of “profit centre”, used by Sir Andrew, was subsequently brought to their attention, both Mr Sullivan and Mr Sach agreed with it and agreed that the Committee deserved a clearer answer and that is why Mr Sullivan wrote to you.

Did GRG have ultimate authority to transfer customers?

This topic was discussed with the Committee and it is clear from Sir Andrew’s 8th July letter that the answers caused him some concern. Historically, the authority of GRG to ‘call in’ a case was created to ensure a timely transfer of the appropriate business into GRG. Mr Sach stated during his evidence that it was designed for larger corporates and whilst in theory it could apply to SMEs, this power was never used for SMEs during the period in question. Sir Andrew has expressed surprise as this latter point was not made to him when he was conducting his review into SME lending. RBS accepts that this was an oversight and I have discussed the issue with Sir Andrew directly.

Mr Sach has re-confirmed that to the best of his and his senior colleagues’ knowledge the authority was not used in respect of SMEs. Nevertheless, I share Sir Andrew’s view that the existence of the authority, regardless of whether it is used or not, could create a perceived potential conflict of interest.

How we treat our SME customers

We are already acting on Sir Andrew’s recommendations and we will keep your Committee and Sir Andrew updated on our progress.

A key objective of GRG was essentially to minimise the losses and costs associated with distressed loans and, wherever possible, to return customers to financial health. As you know, the FCA is currently reviewing the bank’s treatment of SME customers in financial distress and we are of course fully cooperating with that review. The FCA report will provide clarity on the bank’s historical treatment of SME customers in financial distress and allow all of us to form a clear view about how the bank treated SME customers and whether that GRG objective was met. In addition to the changes we are already making, if there are further specific lessons to be learned or issues identified by the FCA review we will act on them promptly.

I know you rightly expect the highest standards from those that provide evidence to the Committee. I regret that we have not met these standards on this occasion. Nevertheless, based on the review we have undertaken, it is my view, and the view of my colleagues on



the Board, that the bank's representatives did not intend to mislead the Committee but we accept that the bank's representatives evidence was not correct in the areas I have highlighted.

Once again I appreciate being afforded the opportunity to be able to respond to the Committee on this important issue.

Yours sincerely,

Philip Hanston