HOUSES OF THE OIREACHTAS

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AN COMHCHOISTE FIOSRÚCHÁIN I DTAOBH NA GÉARCHÉIME BAINCÉIREACHTA

JOINT COMMITTEE OF INQUIRY INTO THE BANKING CRISIS

Dé Céadaoin, 29 Aibreán 2015

Wednesday, 29 April 2015

The Committee met at 9.30 a.m.

MEMBERS PRESENT:

Deputy Pearse Doherty,	Senator Sean D. Barrett,
Deputy Joe Higgins,	Senator Michael D'Arcy,
Deputy Michael McGrath,	Senator Marc MacSharry,
Deputy Eoghan Murphy,	Senator Susan O'Keeffe.
Deputy Kieran O'Donnell,	
Deputy John Paul Phelan,	

DEPUTY CIARÁN LYNCH IN THE CHAIR.

Nexus Phase

AIB - Mr. Michael Buckley and Mr. Eugene Sheehy

Chairman: As we have a quorum, the Joint Committee of Inquiry into the Banking Crisis is now in public session. Is that agreed? Agreed.

Can I ask members and those in the public Gallery to ensure that their mobile devices are switched off at today's proceedings? We begin today's session 1, public hearing and discussion, with Mr. Michael Buckley, former group chief executive, and Mr. Eugene Sheehy, former group chief executive, Allied Irish Banks. In doing so, I'd like to welcome everyone to the 21st public hearing of the Joint Committee of Inquiry into the Banking Crisis.

This morning we will hear from Mr. Michael Buckley, former group chief executive, and Mr. Eugene Sheehy, also a former group chief executive of Allied Irish Banks. Mr. Michael Buckley retired as group chief executive and as director of AIB Group in June 2005. He has been director of AIB since 1995. Mr. Buckley is also a former managing director of the AIB Poland division and of the AIB capital markets division.

Mr. Eugene Sheehy joined AIB in 1971 and spent almost 20 years in retail banking, including branch manager appointments in a number of Dublin branches. He was appointed general manager retail operations in 1999, managing director AIB Republic of Ireland in 2001, and chief executive officer of AIB's USA division in 2002. He assumed responsibility as group chief executive with effect from 1 July 2005, a position he held until his retirement in 2009. Mr. Buckley, Mr. Sheehy, you are both welcome to today's proceedings.

Moving on to the formalities of today's business, I wish to advise the witnesses that by virtue of section 17(2)(*l*) of the Defamation Act 2009, witnesses are protected by absolute privilege in respect of their evidence to this committee. If you are directed by the Chairman to cease giving evidence in relation to a particular matter and you continue to so do, you are entitled thereafter only to a qualified privilege in respect of your evidence. You are directed that only evidence connected with the subject matter of these proceedings is to be given. I would remind members and those present that there are currently criminal proceedings going on and ongoing and further criminal proceedings are scheduled during the lifetime of the inquiry which overlap with the subject matter of the inquiry. The utmost caution should be taken not to prejudice those proceedings.

Members of the public are reminded that photography is prohibited in the committee room. To assist the smooth running of the inquiry, we will display certain documents on the screens here in the committee room. For those sitting in the Gallery, those documents will be displayed on the screen to your left. Members of the public and journalists are reminded that these documents are confidential and they should not publish any of the documents so displayed.

The witnesses have been directed to attend this meeting of the Joint Committee of Inquiry into the Banking Crisis. You have been furnished with booklets of core documents, these are before the committee and will be relied upon in questioning and form part of the evidence of the inquiry.

So if I could now, to begin proceedings, ask the clerk to administer the oath or affirmation to you.

The following witnesses were sworn in by the Clerk to the Committee:

Mr. Michael Buckley, former Group Chief Executive, AIB.

Mr. Eugene Sheehy, former Group Chief Executive, AIB.

Chairman: Okay, so I now invite Mr. Buckley, followed by Mr. Sheehy, to make their opening remarks to the committee. Mr. Buckley.

Mr. Michael Buckley: Thank you, Chairman. I very much hope I will be of assistance to the committee today in its important work.

I joined AIB as head of investment banking early in 1991. And subsequently, as I said, I served as managing director of AIB Capital Markets and then as managing director of the Poland division. In October 2000 I was appointed group chief executive designate and I formally took over as group CEO in June 2001. My successor was designated in March 2005 and I retired at the end of June 2005. From the date of my retirement onwards, I had no further involvement in the management and board of AIB group. As I was retiring ten years ago, I can honestly say that I had no premonition, let alone any evidence, that a liquidity and credit crisis was building internationally or that when that major crisis crystalised late in 2008, that AIB would be so vulnerable to it and ultimately would only survive through taxpayer support. I deeply regret what happened and the damage it inflicted on the lives of so many.

There are two interlocking parts, Chairman, to the account I want to give of my time as CEO of AIB. They are in my written witness statement. I'm just summarising them here. I'm going to start with the business strategy in general and as it applied to the Republic of Ireland in my time. And second of all, I want to talk about risk and credit management. First, the business strategy. In 2001 the business environment was fraught. It was in the wake of the dotcom crash, then 9/11 and we had the added challenge in Ireland of foot and mouth disease. As a result, the strong period of growth that started in the second half of the 1990s slowed for, I think, about two years, but from early to mid-2003 the economy returned to its catch-up growth spurt. There had been a 1 million person increase in the population between 1971 and 2001. The labour force had increased by 400,000, or 32%, in the ten years up to 2001. The number of people in employment had risen by about 400,000 also, or 49%, in the same ten-year period. Such a rate of demographic growth and change hadn't been seen in the history of the State and the numbers continued to grow through the whole period of my time as CEO. That meant the potential for many new customers and strong demand from that growing customer base across the whole range of financial products in a very low interest rate environment. I think that context is very important.

In 2001, investors saw AIB as a federation of banking franchises with varying growth prospects but without any distinctive common thread to its brands. They saw our main market, the Republic of Ireland, as dynamic but their view was that other banks operating here had more exciting growth prospects. The strategy we set out in response to those factors, was to position ourselves to build one distinctive model of doing retailing and commercial banking that could be applied to each country in which we operated. And that model was to focus on growing the total value of each good customer relationship based on having best products, best service and best people. In our largest business here in Ireland we believed that we hadn't been fully exploiting our greatest strengths, those were that we had between 30% and 40% market share of all personal current accounts and all business working accounts but a much lower market share of most individual product categories. So the strategy was to get better at responding to customer needs across the whole product spectrum.

I've mentioned the very strong demographics so building our relationships with good customers in the property and constructions sectors was a logical part of the strategy, but so too was building a stronger presence in the growing health insurance market and meeting the needs of our growing customer base in deposits, mortgages and investment products. When I presented that strategy to the board in 2001, I said that if we were successful in executing it we could have an aspiration of doubling our profits over the next five years. In some of the documents I've been given that aspirational outcome has been incorrectly represented as the strategy itself. In fact, the medium-term forecast and annual budgets presented to the board throughout my period are focused somewhat more modestly on achieving double digit earnings growth overall on a consistent basis. So doubling profits in a five-year period was never actually a budgeted target.

Property and construction lending grew strongly during my time, most of the material I have been sent about that looks at growth trends across the whole period of 2001 and 2009 in percentage terms. That in my view is misleading because the starting base was actually quite low. In money terms the entire group exposure to property and construction during my four years was about €6 billion in mid-2001 and it grew to about €19 billion, this is in euro, by mid-2005. And within those overall totals the figures for the Republic of Ireland were that it grew from €4 billion to €11 billion.

I have no evidence that at that level we had materially outrun the demand arising from deposit and demographics nor did I have a view coming to me from my credit professionals that standards were slipping at the time. On the contrary their view to me throughout and to the board was that credit quality was stable and strong.

In any business you're trying to keep a fairly wide range of shifting factors in good balance so towards the end of 2004, as a result of the fact that loan growth had been significantly outpacing deposit growth, I began to focus on the increasing loan-to-deposit ratio and on the proposal from myself and my management team, the board put in place at that stage targets, one for the simple loan-to-deposit ratio and the second for an adjusted loan-to-deposit ratio. That was done to begin to slow down the rate of credit growth to a level closer to the growth rate for deposits and also to help ensure that internal capital generation was positive.

I'm going to turn now to my second main aim in the period mid-2001 to mid-2005; which was improving our risk management capability. That was partly for strategic reasons, it was partly also because we had three massive regulatory projects to implement; Basel II, Sarbanes-Oxley and the new IFRS accounting standards, and, thirdly, because I had to deal with two major crisis management events during my time - the fraud in our Allfirst subsidiary in 2002 and the FX charging issues identified in Ireland in 2004. Collectively, all of those factors required the single risk and finance support organisation to be built across AIB Group which had always been heavily divisionalised. That was a huge five-year project as I saw it. In the wake of the Allfirst fraud we commissioned separate independent reviews and reports on treasury operational risk, credit risk, policy frameworks across all of those things to get assurance that they were fit for purpose and we constructed a series of projects to implement the recommendations arising. The general message in those reports was that within each division there were no major issues but that we needed to establish common standards across the whole group.

During 2002-03 we recruited an experienced chief risk officer, reporting directly to me, to build that single organisation. We put in place a single group-wide treasury organisation. We again recruited externally an experienced head of internal audit to build a group-wide capability and we enlarged the mandate and scope of the compliance function across the group. We devoted massive resources both to the regulatory projects and to remediation programmes arising from Allfirst and from the FX charging issues in 2004.

Implementation was still going on when I retired, including a wide range of actions designed to change those aspects of culture and practice in the bank that were obstacles to colleagues at any level feeling free to raise any issues that concerned them. And that was a strong personal mission of mine. I have a couple of final things to say, Chairman. First of all, turning to credit policies, delegated authorities and exception management, Deloitte had carried out a very detailed policy and process review, I think towards the end of 2002 if my recollection is right. What they found was that there were "well established processes, policy and delegated authorities based on skill and experience, that grading and monitoring systems accommodated early identification and management of deterioration of credit policy, that there was a system of credit review independent of business reporting lines and written policies pertinent to current business." That's the end of the quote. Their recommendations mainly had to do with ensuring consistency across all of our divisions. The delegated authorities to divisional credit committees were relatively modest during my time. They were increased somewhat towards the end of 2004, but not dramatically, and exceptions to large exposure policy were infrequent. The month before I retired, in May 2005, Standard & Poor's raised our long-term credit rating to A+. In their announcement, the agency said:

> The rating on AIB reflects its leadership position in its main market, the Republic of Ireland, strong credit risk management, good underlying financial performance and sound liquidity. They also reflect AIB's ongoing initiatives to improve its risk management procedures and control frameworks.

That is the end of the quote. Thank you Chairman.

Chairman: Thank you very much, Mr. Buckley. Mr. Sheehy.

Mr. Eugene Sheehy: Chairman, members of the committee, thank you for affording me the opportunity to outline my views on the banking crisis. At the outset, I want to say I'm very sorry for what happened and my role in these events. I know a lot of people were let down and feel very angry, deservedly so. I draw no comfort from the extraneous factors that contributed to the crisis. I take personal responsibility for my actions and omissions. Public apologies on many occasions have not diminished the deep disappointment that I feel on a daily basis. Chairman, in my written statement I have addressed the themes that the inquiry requested me to focus upon including property risk concentrations, liquidity, business planning, remuneration, regulatory relationships, delegated authorities and the bank guarantee. Conscious of time and that these themes will be covered during my evidence, and in light of evidence given to the committee last week, I will confine my verbal remarks to a summary of the evidence contained in my written statement concerning the bank guarantee. I have been asked to make a statement on the appropriateness of the guarantee. Though we did not make the decision, I will describe my role on the night and this role is described in detail in my contemporaneous notes, of which you have a copy.

Together with our counterparts from Bank of Ireland, we asked for a meeting with Government. At that meeting, we requested a four bank guarantee, but not the blanket guarantee that was ultimately provided. We were in Government Buildings for over six hours, our presence at the meeting was not continuous, and we were dismissed from the decision makers' room on four occasions. At the first session we described what was happening in our business, and how our liquidity was being positioned. That day had been a tumultuous one on global financial markets. To stabilise the Irish banking market, we asked for a four bank guarantee. This was not a new idea. You will have copies of minutes of an AIB bank board meeting of the night before, in which I am quoted, "The authorities expect that two financial institutions will fail (unless white knights emerged) and would guarantee the obligations of the other institutions on a temporary basis", recorded in the AIB minutes the day before the guarantee. We were dismissed from the room while our request for a guarantee was considered.

At the second session we attended, we were told that Anglo was about to default. The Government wanted us to give Anglo a loan to get them through the week so that they could be decisively dealt with by the weekend. We refused initially and were dismissed and were asked to reconsider our position. Working over the phone with colleagues back in Bankcentre we mobilised resources and looked into every possibility to come up with a response that would meet the Government's needs. At the third session, we said we would give Anglo €5 billion until the weekend. On notice at this stage that Anglo was about to default, we refused to go on risk for Anglo. Our offer was conditional on a Government guarantee for this Anglo loan. This solution appeared to be acceptable to the Government and we said we would start moving assets to have the funds ready by Wednesday morning, and that in itself was quite a complex and intricate business.

The meeting reverted to the four bank guarantee and its form. We made suggestions regarding duration of the guarantee - we wanted a longer one than the one-year one proposed - and also on the merits of including bonds ... of which we were in favour of. We were dismissed while a drafting process was undertaken and during this interval our input was sought on ... in bilateral sessions regarding treatment of subsidiaries, for instance, our Polish business, and on what basis would be ... what basis would be used to determine the price of the guarantee. When we were called back for the fourth session, there was a short discussion about a solvency statement being issued with the guarantee. We didn't think it was necessary and after discussion, the Government decided not to include that reference. We returned to the room and at 3:30 a.m. we were told we were no longer needed. When we saw the guarantee document for the first time the following morning, we could not understand why Anglo and Irish Nationwide were included. All our discussions that night were based upon a premise that Anglo was to be taken down. We did not think they would be part of the guarantee, in fact, we were at that time, in response to a Government request, risking our own liquidity to keep Anglo afloat until the following weekend.

From our perspective, a four institution guarantee was appropriate and necessary for a number of reasons. Firstly, an Anglo default was absolutely certain to result in an immediate across-the-board agency downgrade for all Irish institutions and an immediate worldwide risk aversion for all Irish institutions. Secondly, in Great Britain where we had high street branches and €10 billion in retail deposits, we could expect an immediate run on our deposits. Thirdly, given the Irish public's reaction to Northern Rock, a very minor player in this market, during their crisis in 2007, you could deduce from that it was certain that there would be panic on the streets and that our branches would not be able to cope.

In the absence of a statutory mechanism to deal with a failing bank, the options were to nationalise, liquidate or guarantee. There was no contingency plan nationally to deal with Anglo or at EU level to deal with the crisis in general. In the absence of alternatives, the default option was a four bank guarantee for the remaining four institutions, not the blanket guarantee ultimately given. This, I believe, offered the best chance to cope with the fallout about to be triggered by the imminent liquidation or nationalisation of Anglo and Irish Nationwide. The lessons from two weeks previously were fresh in everybody's mind. Solutions that didn't convince the markets invited misfortune. This was amply demonstrated when the US authorities allowed Lehman's to fail. The decision did not restore market discipline and within days the US Government had to rescue many institutions - huge institutions - and introduce a €700 billion TARP, the troubled asset relief programme. These events contributed hugely to initiating the meltdown in global liquidity.

I wrote up my notes of the minutes ... my minutes of the meeting a couple of days afterwards and absent hindsight observations that ... I have made some in this statement ... they are a contemporaneous record of events on the night as I saw them. Since I submitted my statement a month ago, I have been furnished with another record of events on the night from a Department of Finance source, which has been quoted at the committee. Comments are attributed to me that I cannot remember making. There was absolutely no evidence of any discussion of AIB's solvency on the night, in either my note or that of Dermot Gleeson's. We were asked for an update on what was happening in our banks which we gave. We were asked to provide funds to cover Anglo until the weekend which we agreed to provide. We were asked about the form of guarantee. We gave advice on duration and the instruments that could be included. We gave advice on duration and the instruments that could be included. We were asked for our views on Anglo and Irish Nationwide, we said they should be nationalised. This fact is recorded in both my note and that of Dermot Gleeson. This fact is further collaborated by the note from the Department and I quote "Minister asks FR, did they agree with AIB, Bank of Ireland, that two need to be nationalised first. FR did not agree."

If I said the words attributed to me in the Department of Finance note, they could only have been in the context of what would have happened to the system if no remedial action was taken. There was absolutely no issue about AIB solvency at that time.

Chairman, in conclusion I spent 38 years in AIB, operated at many levels and I knew the organisation very well. I was proud of what the bank had achieved over the decades. I always viewed my job when I became CEO as one of stewardship, responsibility to staff, customers, shareholders and the public in general. It was my wish that in due course I would hand on the job to somebody else with the bank in good shape. That I failed in that responsibility, for me is a matter of eternal regret and sorrow.

Thank you, Chairman.

Chairman: Thank you very much, Mr. Sheehy, and thank you again, Mr. Buckley. I am sure other members will over the course of the morning return to some of the matters you raised about the guarantee, but as we are aware the guarantee was a response to a crisis, it wasn't the instigating factor of the crisis and that's what I would like to delve into now, if you don't mind.

Mr. Buckley, in your opening statement, can you confirm to the committee, that is what you're telling the committee, that you left AIB in a fundamentally sound position when you departed?

Mr. Michael Buckley: That is my belief, Chairman. Yes.

Chairman: Okay. Thank you very much. In that regard so, Mr. Sheehy, could you maybe explain to us as to what actually happened under your watch that led to AIB having to go in to a bailout programme and be guaranteed?

Mr. Eugene Sheehy: Yes, Chairman. I fully agree with my colleague that in the middle of '05 the outlook and the condition of the bank was very positive and that continued, in my view, for a number ... a couple ... of years after that. It was only when the market began to unravel, both internationally ... one way I look at it is, there was an international context, there was a national context, and there was an institution specific context. And, all three of those dimensions changed for the worst in ... from the middle of late 2007 onwards. There were reasons for it and I'll only address the institution specific ones. Obviously, everybody is familiar with the context as you had in the Context Phase.

When the market turned negative we were ... we found ourselves overexposed in property in the Republic of Ireland and specifically certain types of property in the Republic of Ireland. Our expectations as to how those assets would behave in a downturn didn't pan out. The stress tests we relied upon, while there were one in 25 year stress tests weren't equipped for a one in a hundred year stress, and as a consequence post-2009 as the market continued to display very severe write-downs, the bank's capital position became compromised and it required support from the State. Earlier of course, it had got support in relation to the guarantee, so that would be my explanation of how it came to be.

Chairman: Alright and we'll deal with that as the morning now goes on. Our first lead questioner is Deputy Kieran O'Donnell. Deputy, you have 25 minutes.

Deputy Kieran O'Donnell: Thanks very much, Chairman. Welcome to Mr. Buckley and Mr. Sheehy.

Mr. Buckley, can I just ask a question of your time? During your tenure, like a number of major control issues arose and you mentioned Rusnak, Faldor and the foreign exchange, the incorrect interest charges for offshore accounts. How would you reconcile that with the governance standards that you would have outlined each year in the annual reports?

Mr. Michael Buckley: I think, Deputy, we were ... first of all we were very clear about any control failures that happened during that time. I mean ... so that's the first point I'll make. When the Allfirst treasury fraud occurred over in Baltimore we immediately ... within I would say 36 hours of first hearing that there was an issue, I was on the radio first thing in the morning sizing it, and very quickly then we said we would bring in independent investigators, which we did, of the highest quality, to investigate it thoroughly, and we promised at the very beginning that we would publish all of the findings of those investigations. So, first of all, I think that's a very important governance statement because we were making a promise to shareholders and to customers and to our own people that nothing would be brushed under the carpet, and that is a path that we followed two years afterwards when the FX charges issue came up.

Deputy Kieran O'Donnell: How would you explain that these three scandals arose at the time they were reported as such, arose in a ... over a two year period?

Mr. Michael Buckley: I think that to some extent that was a coincidence but it would be foolish of me to say that that was totally a coincidence. I think there were some very important common threads between them. The thing I would say is that a common thread between them is that, to take the FX charges and related things first of all, those issues, by and large, referred back to the 1980s up to the early 90s, and the subsequent investigations found that in most cases the particular issues that had been brought to the regulator's attention and, via the regulator, to our attention, had been dealt with, by and large, during the course of the 1990s so there was a large element of history about them. To me, they were probably ... the FX charges was probably the most upsetting part personally to me of my time as CEO because it said that there was stuff going on there that, in terms of the values and principles that I would have had, that were contrary to those principles. Now ... but we did tear up the floorboards. I mean, I remember when the FX charges thing came up first, I was on television, and I said those very words. I said, 'This information about that issue has gone to the regulator and what we are going to do is not only to investigate that as far as it goes but we will tear up the floorboards on every issue of charges that we know about and we'll try to find anything that we don't know about", and we made a promise to customers that we would remediate every case of customer detriment, which we did. So that's ... I think that's the governance part of-----

Deputy Kieran O'Donnell: On that point, like, the Rusnak came to prominence in '02, Faldor case in '03, the foreign exchange rate setting came in '04.

Mr. Michael Buckley: Yes.

Deputy Kieran O'Donnell: So I mean, I suppose to borrow an Oscar Wilde phrase, for one to happen would be unfortunate, two is careless. So clearly people were not taking account of the investigations that were going on in the other areas. So how do you finally account for that? And you might also explain to me as well in terms of property lending, that during your tenure, post '04, so '04 and '05, you had an increase in property lending of 6% in '03. You had 48% of an increase in '04, and you had 52% of an increase in '05, just before Mr. Sheehy took over.

Mr. Michael Buckley: Yes.

Deputy Kieran O'Donnell: And that's significantly higher than your two main competitors at the time, Bank of Ireland, which was 24% and 23%, half of that amount virtually, and Anglo were at a figure of 35% and 38%. So you might explain how we have these sequence of events whereby you had these various defrauding of customers happening and, at the same time, '04 and '05, you had this rapid explosion in property lending under your watch, Mr. Buckley.

Mr. Michael Buckley: There ... thank you Deputy. I think there are several questions there, if you don't mind I'll answer them separately, is that okay, Chairman? So first of all, if I take the Allfirst one, that wasn't a case of defrauding customers; it was a case of defrauding the bank. There was no customer detriment involved there. Second of all, in the FX charges, and I include other things in that as well in that particular area, in the principal issue there that gave rise to that whole scandal, there was no customer detriment. What had happened was, we as a bank, were required to get written approval in the mid-90s, I think it was 1996 or something like that, for our foreign exchange charges. We had failed to do that. The investigation then found that actually our charges in the marketplace were no worse than any other bank, so therefore we were not disadvantaging customers. Despite that, we went and remediated and refunded every customer that we could find. The third element, Faldor, was a situation where there was no customer detriment. This was a question as to whether, how will I say, a particular legal entity - an investment vehicle - had been given preferential treatment by our investment management arm. It wasn't anything about customer detriment.

Deputy Kieran O'Donnell: Could you move on to the loans then?

Mr. Michael Buckley: Yes, absolutely. Yes, there were very big increases in that year and a half period or so before I finally retired and I would say there were two reasons for that. One, as I said in my opening statement, the economy was beginning to recover from a pretty tough few years after the dotcom, and we got ... there was a sort of catch-up spurt I think.

Deputy Kieran O'Donnell: You were significantly ahead of your competitors.

Mr. Michael Buckley: Yes, but we had always been a bank that lent to property and construction. I mean, if you go back to 1998-----

Deputy Kieran O'Donnell: Was it endemic in the culture of AIB?

Mr. Michael Buckley: But, if I may say so, there is nothing wrong with lending for property and construction development. I mean, in 1998 our loan book for property and construction, depending on whether you count in or out our US subsidiary, was somewhere between 12% and 15% of our total book. So we had a long history in lending and we were quite comfortable that we were an experienced lender to property and construction.

Deputy Kieran O'Donnell: Can I just move on to Mr. Sheehy? Just on the whole issue, I am taking the property side. You would have very much breached the prudential lending limits in July '06. How do you reconcile that, because you were effectively, by the end of 2006 you were breaching these limits significantly and by 2008 you were way ahead. You were ... effectively, you could have about 250% of own funds in two related sections. You were at 390%. How do you reconcile that Mr. Sheehy?

Mr. Eugene Sheehy: Deputy, in 1995 the regulator changed the guidelines for concentration limits to 200% for one asset class and 250% for related assets.

Chairman: I will just make a short intervention. When you are responding to this, there is some documentation that actually relates to that. I will reference it as you are making the response so it can just go up on the screen. Okay.

Mr. Eugene Sheehy: Yes, okay. Fine.

Deputy Kieran O'Donnell: It is B2, Vol. 1, page 6.

Mr. Eugene Sheehy: Yes, I'm-----

Deputy Kieran O'Donnell: You are familiar with it.

Mr. Eugene Sheehy: Yes. So yes, there were guidelines and they were breached and advised to the board, and discussed at the board and discussed at management generally. What was happening ... if that happened in total isolation of what was happening overall in terms of regulation, I would say the bank was ignoring a guideline, but that wasn't the case. We weren't ignoring the guideline. We were talking to the regulator about the guideline and the regulator was talking to us about the emerging solution to risk concentrations which-----

Deputy Kieran O'Donnell: Taking that context, Mr. Sheehy, at the end of 2008, you were far in excess. You were breaching the guidelines on one sector, we'll say, which should have been 200%, you were at 275%. The two sectors should have been at 250% and you were at 390%. Was the regulator in agreement with this, satisfied with this?

Mr. Eugene Sheehy: Well, you are picking two different points in time now. The '06 reference was ... okay, we were up against and going over, and the way these things were being measured was going to be changed under Basel II. The '08 data point is at the end of a period where the market has stopped functioning correctly, so you weren't getting-----

Deputy Kieran O'Donnell: You were getting to the top of the hill?

Mr. Eugene Sheehy: Well, you have no cash flow coming in at that stage so your ratios were going to go up.

Deputy Kieran O'Donnell: No, I'm asking how did the regulator view that?

Mr. Eugene Sheehy: Well, we were in discussion with the regulator about it - there's evidence of that in the bank documents - and we were working jointly at the time on the Basel II model and how that would look at sector concentrations, so that was a big issue because it was a totally different way to look at risk concentrations where in-----

Deputy Kieran O'Donnell: There are two questions, Mr. Sheehy.

Mr. Eugene Sheehy: Yes.

Deputy Kieran O'Donnell: No. 1-----

Chairman: Give the witness time to respond when he-----

Deputy Kieran O'Donnell: -----why you breached it-----

Mr. Eugene Sheehy: Yes.

Deputy Kieran O'Donnell: -----and, No. 2, what view did the regulator take?

Chairman: Allow Mr. Sheehy to respond.

Mr. Eugene Sheehy: Okay. We breached it and it was ... as soon as it was identified, you know, it was reported and discussed with the regulator, so, if you like, it was a breach in open sight, it wasn't something that was hidden. The regulator acknowledged the breach, didn't remove the limit, you know, but at the same time acknowledged that we were working on the Basel II process, which was going to look at it in a different way.

If I could just briefly explain, Basel II, the approach to credit concentration in Basel II is totally different. It is not by looking at a definition of an asset class, it looks at all individual credits and applies different stresses and measures to them and attaches a risk weighting to them which leads to a calculation, so it was really as different as chalk and cheese, the way this system was moving towards it. In the meantime, we were in breach and we were talking to the regulator.

Deputy Kieran O'Donnell: Should you have breached the limits?

Mr. Eugene Sheehy: In hindsight, no, we shouldn't have breached the limits.

Deputy Kieran O'Donnell: And can you explain, Mr. Sheehy, why, under your tenure, between '05 on, your development loans, property and construction loans, you had a 52% rise in '05; '06, 41%; '07, 32%; way in excess of your competitors in Bank of Ireland, which were 23%, 23% and 22%, virtually ... significantly less. And, looking at it, that even with Anglo in 2005, you had 52% of an increase and you had ... Anglo had 38%. So, can you explain how you ... Mr. Buckley says you had ... you were a bank that lent to property, but how did you foster this culture where you had this rapid escalation in property and construction lending?

Chairman: Mr. Sheehy.

Mr. Eugene Sheehy: I note the comparators you're making and I'm only going to talk about a comparison between ourselves and Bank of Ireland because that's the only equivalence. They were a retail commercial bank; so are we. There was a slight difference in our customer base. We were much heavier than they were in the SME sector and property and construction was widespread. We had, you know, in the ... we had very large customers and then we had 650 customers who had property and construction loans of over €1 million, so it wasn't ... it was very broadly spread and reflected our franchise and the nature of our franchise.

Deputy Kieran O'Donnell: Well, except, Mr. Sheehy, it made you-----

Chairman: Sorry, I need to let Mr. Sheehy time to respond.

Mr. Eugene Sheehy: I'm just following up on something my colleague, Donal Forde, said the other day. We kept pace with our customers. We didn't grow market share in that case. Point-to-point, you will get different percentages moving around. Some of the examples you gave are different end financial years.

Deputy Kieran O'Donnell: Correct, I accept that, but generally.

Mr. Eugene Sheehy: But generally, we had a customer base that was business-focused and heavier in business than, say, Bank of Ireland. Our customers wanted to be in the property and construction business. We had a good track record with these customers and we followed them.

Deputy Kieran O'Donnell: And how do you view that in the context that you were so exposed to property that it has meant that €20 billion of taxpayers' money has ended up going into AIB? And you're on record as saying that you'd rather die than take equity.

Mr. Eugene Sheehy: Yes, I can address that particular statement if you want. That was in October 2008, in a public meeting, and an individual asked me, you know, "Are you about to have a rights issue?" Now, it's very simple rules in corporate governance about what you do if you're a public company. There's also lots of documents you will have seen that we were adequately capitalised at the time. If a board had decided to raise funds in a share placement with customers, you would have to immediately announce that. At the time we were looking at capital, and we had a whole range of mitigants that we thought we could apply. We were a long, long way from ever having to, at that stage, ask shareholders to pay up. At the time there was an active shorting in the market, and a huge amount of speculation on bank shares in Ireland that were being played out of London and New York. I had to be very definite and honest in my response. Sorry, I lost the first part?

Deputy Kieran O'Donnell: Twenty billion euro of taxpayers' money gone into AIB.

Mr. Eugene Sheehy: Yes.

Deputy Kieran O'Donnell: As a result of this jumping, we'll say, into property and at such a rapid rate.

Mr. Eugene Sheehy: That's-----

Chairman: The question is: there was a rate of growth in AIB; was that worrying? And did that result in a €20 billion requirement of the Irish State to actually assist AIB as a consequence of that rapid growth and the management related to it?

Mr. Eugene Sheehy: There is absolutely no doubt the two things are absolutely binary connected. They were connected. There is no doubt.

Deputy Kieran O'Donnell: Can I just move on to the guarantee? And you made reference to your quote that the ... it's on AIB C3b, Vol. 2, page 29, which is the minutes of the Department of Finance. And you said: "People we've been dealing with for decades pulling back. One month we would be funding bank overnight. Bad if it can't even get that disaster bankruptcy." Are you disowning that statement?

Mr. Eugene Sheehy: I said I can't remember it.

Deputy Kieran O'Donnell: Had ye a liquidity problem? Did AIB-----

Mr. Eugene Sheehy: Oh absolutely, everybody had a-----

Chairman: I just asked Mr Sheehy to deal with the statement first and then we'll move on to the next question.

Mr. Eugene Sheehy: So I said it in my opening statement, I can't remember saying that, and I said that, you know, that kind of language could have been used in relation to the systemic issue of, if the system, the entire banking system, as a result of the imminent Anglo default, was allowed to continue, liquidity would have kept on shortening and shortening and shortening. And if that happened, banks that are solvent, bank that have more assets than, you know, surplus assets, can go out of business because they just can't get cash.

Deputy Kieran O'Donnell: And are you saying AIB did not have a solvency problem on the night of the guarantee?

Mr. Eugene Sheehy: Yes, absolutely, did not have.

Deputy Kieran O'Donnell: And on the night of the guarantee did AIB go in with a guarantee, I suppose, an outline, a draft of a guarantee?

Mr. Eugene Sheehy: I've racked my brain on this, Deputy, and I can't actually remember whether there was a piece of paper or not. If there was, it must have been a very small piece of paper or it must be in the Department's records. I can't remember it.

Deputy Kieran O'Donnell: What was the outline of that? What was the outline of your guarantee you were looking for?

Mr. Eugene Sheehy: The outline of the guarantee, and I don't recall whether it was a written one or not, would be: stabilise the situation immediately. The 20 ... that day globally was unbelievable and it was clear that worse things were to come internationally. So stabilise the situation. However-----

Deputy Kieran O'Donnell: The specific form of a guarantee you were looking for?

Mr. Eugene Sheehy: Well remember we have a guarantee eight days before already, a €100,000 guarantee, €200,000 for a kind of a household limit. So it wasn't ... this was to some degree an iteration of a series of steps that the State was trying to take to stabilise the situation. What we didn't know on the day when we went in was that there was an institution-specific problem which would have exacerbated and multiplied to a huge degree all the other problems we thought we had when we went into the meeting.

Deputy Kieran O'Donnell: And if you were looking for both Anglo and Irish Nationwide to be nationalised?

Mr. Eugene Sheehy: We were asked for our advice on that, and that's what we said.

Deputy Kieran O'Donnell: Did ye have further discussions, communications with Government or officials in the Financial Regulator after the guarantee was put in place on the night of the guarantee?

Mr. Eugene Sheehy: There were discussions in the days that followed, but frankly it ... the entire focus in the days after the guarantee were coping with what was happening globally in London and seeing how the guarantee bedded in. Our big issue actually in the days that followed the guarantee was that pricing for deposits priced up to the sovereign and there was no distinction between strong or weak institutions.

Deputy Kieran O'Donnell: Can I ask you ... yes, can I ask you in the context of AIB C3b, Vol. 2, page 45, Project Omega, what was Project Omega?

Mr. Eugene Sheehy: Project Omega, I think it was in November, we were asked by the Minister for Finance-----

Deputy Kieran O'Donnell: Finance.

Mr. Eugene Sheehy: -----to seriously consider taking over Anglo.

Deputy Kieran O'Donnell: Okay.

Mr. Eugene Sheehy: If the Minister asks you, you do look at something so we engaged in the normal corporate finance mark-up process for 60 or 70 pages of it. A fair bit of it was boilerplate stuff actually. It's not ... it wouldn't be a very heavy document. It was discussed at my forum the group executive and dismissed and resolved that it would not be pursue. And our conclusion was then reported to the board. It was not discussed by the board.

Deputy Kieran O'Donnell: Not discussed by the board. Why not?

Mr. Eugene Sheehy: Well, we told them that we weren't going to do it.

Deputy Kieran O'Donnell: Okay. And did the board accept that?

Mr. Eugene Sheehy: Yes.

Deputy Kieran O'Donnell: So it was it was made known to the board.

Mr. Eugene Sheehy: Yes.

Deputy Kieran O'Donnell: Specifically. And in that ... this is a presentation to the board ... did you make this presentation, Mr. Sheehy?

Mr. Eugene Sheehy: The presentation was not made to the board. That was given ... it might have been in the board papers.

Deputy Kieran O'Donnell: But it wasn't...

Mr. Eugene Sheehy: We said to the board: ‘’Got the request, looked at it, not a runner. Pass on’’.

Deputy Kieran O’Donnell: And can I ask you, put in there, it said: ‘’In addition any transaction should only be undertaken following full due ... and would require significant Government support. Were the Government ... the Minister for Finance was he ... had he made put forward to you that they would be willing to provide support if AIB took over Anglo?

Mr. Eugene Sheehy: There was no detailed discussions about it. We were just asked to have a look at it. There wasn’t any negotiations or terms or ...

Deputy Kieran O’Donnell: And did you go back to the Minister to say that would not happen, that ye were not...?

Mr. Eugene Sheehy: I can’t recall how we went back but we ... I may have communicated to the Department that, you know, it wasn’t going ahead.

Deputy Kieran O’Donnell: The final thing I want to check is on remuneration. And, Mr. Sheehy, your salary peaked in 2006 at €2.4 million per annum.

Mr. Eugene Sheehy: Total compensation.

Deputy Kieran O’Donnell: Total compensation, but €1.3 million of that was a bonus, right. The question I want to ask is: how could you justify such a salary? And it would appear that the remuneration scheme for higher executives was brought in under your watch, Mr. Buckley, so that you had a situation up to ‘04 where the bonuses weren’t crazy relative to salary up to ‘04, but from ‘04, ‘05 on-----

Chairman: Maybe ... don’t apply a judgment-----

Deputy Kieran O’Donnell: Can I ask-----

Chairman: Sorry Deputy, don’t apply a value judgment to the figure. Mr. Sheehy’s job is to explain the judgment of the figure.

Deputy Kieran O’Donnell: Mr. Sheehy, can you explain how you ended up on a salary of €2.4 million per annum and how can you justify that? And was your remuneration policy ... did it build in any element of risk in terms of a judgment of property transactions?

Mr. Eugene Sheehy: The numbers are very high, not justifiable in my view in today’s terms and----

Deputy Kieran O’Donnell: If I-----

Chairman: Deputy, if you ask a question, you have to allow the witness time to respond.

Deputy Kieran O’Donnell: Well you’ll appreciate time is limited.

Chairman: I do and that’s why I’d ask you to keep your questions short.

Mr. Eugene Sheehy: I would say they were not justifiable, period, okay, no matter what time you’re looking at it. How were they constructed? There’s a number of components, as you know. There’s a salary, a bonus and there’s a long-term incentive and there’s ... I believe we had a robust policy around it. Large elements of the policy never worked, you know, the long-term incentives never worked because the goal ... the targets were too high. I had a personal policy of reinvesting all my bonuses in AIB stock. But, look, there's no way you could tell anybody in the street that these were acceptable levels of pay. That's a fact.

Deputy Kieran O'Donnell: And the can you justify a salary of €1 million a year, a basic salary at that level in '06-'07?

Mr. Eugene Sheehy: I didn't have it. You'll see that ...

Deputy Kieran O'Donnell: You had a basic salary-----

Mr. Eugene Sheehy: I had a basic salary. I think it peaked at I think €900 and something-----

Deputy Kieran O'Donnell: Correct, you were just short of €1 million.

Mr. Eugene Sheehy: Yes, but it wasn't €1 million and-----

Deputy Kieran O'Donnell: Well I think it's splitting hairs, Mr. Sheehy.

Chairman: Deputy please, please ... Sorry, Mr. Sheehy and Deputy, please questions to the Chair and responses to the Chair.

Please allow the witness to answer without a value judgment being applied. Indeed the committee in its final report will apply its own value judgments. Mr. Sheehy.

Mr. Eugene Sheehy: Thank you. Just in general on remuneration. You know, there was a number of components to it and they were scientifically constructed. We had three external consultants who looked at it. And their methodology was to bring you into a peer group and a reference group and that was probably the biggest driver of the pay policy. I never asked and I don't know of any colleagues who ever asked the remuneration committee for a pay increase. It was kind of mechanically devolved out of a system of peer references. And if you look at the Nyberg report you will see that AIB was much, much lower ... rather than ... of the peer group, in terms of size. So, there was a science to it. There wasn't executives going up, banging the door saying "I want more pay". It never happened. But the actual amounts that we were paid were too high ... I mean, when I came from the States I was paid a lot less over there, but they had a totally different philosophy about long-term compensation, so you could make a lot of money in the States as a bank executive if you stayed in an institution for a long time, because there was a huge upside in stock. Here there was ... actually it turned out, no upside in long-term compensation because the bar had to be ... was ... CPI plus 10% compound which is virtually impossible ... actually impossible to make, so they never vested it. I think once in ten years there might have been a small vesting. So there was flaws in the design, too much influence by peer reference, but there was no clamour among bank executives, the people who reported to me directly, for more pay.

Chairman: Thank you. I just want to clarify with you a couple of matters ... just finishing off that point. Very simply, Mr. Sheehy, looking back at what was the financial standing of the bank during that period, was the level of your remuneration, bonus and reward merited?

Mr. Eugene Sheehy: In hindsight, no. At the time you could have made a case for it and you know ... third parties, professional third parties would have made a case for it.

Chairman: I just want to clarify one thing with you, just to assist the committee and it is going back to that note of 30 September that Deputy O'Donnell related to - it is coming up on the screen in front of you. To your view, is that an accurate account of the evening's records? You are familiar with that document?

Mr. Eugene Sheehy: I am, and it is not ... in some respects ... you know, I think Mr. Gleeson referred to a mix up of points he made with ... under Mr. Burrows's heading. But I have no doubt it's a best effort and I wouldn't criticise it ... you know it might be a bit mixed up but-----

Chairman: I can only account, in fairness to yourself, Mr. Sheehy, the parts of those notes and those records, that it should be to yourself. I know there are records there in regards to Mr. Burrows, Mr. Hurley and others, but there are a number of points that refer to you. Do you consider that to be an accurate account?

Mr. Eugene Sheehy: As I have said, I don't recall using the word "bankruptcy". And if there is an inference being taken from that statement, that there was something to do with AIB solvency, I would absolutely reject that that ever arose.

Senator Sean D. Barrett: Go raibh maith agat, a Chathaoirligh, and welcome to our visitors from AIB. What was proposed on the night of the guarantee was a four-bank guarantee. Was that for deposits only and how much would that guarantee have cost?

Mr. Eugene Sheehy: Our proposal was for a four-bank guarantee. Clearly when you are discussing nationalisation, liquidation or default of an institution, that's not part ... that institution isn't part of the future, that's part of the past that has to be dealt with. We argued, I certainly argued, that the bonds should be included and the reason for that was if you looked at the mistakes that were made in the US around Lehman's and the inconsistency from day to day of the regulatory response, not only in the US but in Europe and in the UK - where we knew ... we found out subsequently there was secret loans being given to banks - you had to be clear about the message you were giving to the market. Clarity is very important. If some of those instruments weren't covered, our investor relations desk would have 100 calls within one minute about "Define exactly what you mean here". So the definition and the clarity were important.

It is worth pointing out that on the night, AIB had no bonds or subordinated debt instruments that would in any way have been enhanced by the guarantee. None. We had perpetual debt, which is irrelevant for a timed guarantee and we had dated debt, the earliest of which fell due in 2013. So there was no agenda from our point of view of getting something extra.

The pricing of the guarantee on the evening wasn't discussed. Now, we did have a reference, if you looked at the €100,000 guarantee for individuals which was introduced on 20 September, and that had a 20 basis point price on it. In the bilateral discussions that we had around pricing of the guarantee I was pushing for an FDIC model which is the US model about ... you price the guarantee relative to the risk you are taking, and the risk you are taking is based on a formula, called a CAMEL formula, which takes in capital, liquidity, management risk. It would take a bit of working to do but there was a model for pricing of guarantees that's the biggest model in the world, used by the FDIC in the US.

Senator Sean D. Barrett: So you had two organisations left out. Were there any other differences between what the Government actually did and what you were proposing, apart from leaving out two banks?

Mr. Eugene Sheehy: We didn't propose anything. We gave advice on ... in response to questions we were asked. We said we needed a guarantee, the system needed a guarantee of some type, because of what had happened that day and what was absolutely certain would happen over the coming days. And after that then for instance, when it came to the duration, there was a one-year duration proposed. The way the markets operate one year is actually a product, you know, 90 days is a product, there are buckets of time-based funding instruments and one year is one year for one day. It just becomes technically very difficult to do anything with a one-year guarantee, so we recommended a two-year guarantee and subsequently the European Commission came out and said that that was the only type of instrument that would have had a chance of working, less duration would not have worked.

Senator Sean D. Barrett: But we don't know the difference between the cost of what you were proposing and what the costs turned out to be for the Government's proposals, is that right?

Mr. Eugene Sheehy: The cost of the guarantee ... I don't know what ... I don't think it costs the State anything. The issue for the cost for the State arose when the assets of the banks fell short. I mean, the guarantee ... there was several billion in fees paid for the guarantee and it was eventually retired.

Senator Sean D. Barrett: The regulator proposals of the McDowell report earlier in that decade ... did the banks support those or oppose them?

Mr. Eugene Sheehy: The McDowell report ... you'll have to refresh me on the McDowell report, it wasn't in my documents.

Senator Sean D. Barrett: It was a proposal for a separate regulator and it was opposed by the Department of Finance and the Central Bank. There was quite a controversy at the time, probably under Mr. Buckley's term I suppose.

Chairman: Are you familiar with the document that Mr. McDowell, the former Attorney General, was bringing forward at the time? If you are not, I will just move on to another question.

Mr. Eugene Sheehy: I wouldn't know the detail of it but if the question is about, you know, was the regulatory structure appropriate which ... I mean we had dealings, and I had dealings, with the FR from the time. I had some dealings with them before I left to go to the US, I had a lot of dealings with them when I came back. At the time, certainly from mid-2005 on, the focus was on consumer-related issues, as a knock-on I think from the issues that Deputy O'Donnell raised - you know, the governance issues. So there was a big focus on that, and then it was immediately kind of replaced by the three big programmes: SOX, Basel and IFRS, which totally consumed the regulator's energy and our energy, certainly through 2006 and most of 2007. So it was a ... I think the regulator at that time was taxed with a huge amount of oversight in what was happening in the market.

Chairman: He was described as "hopeless" in a document which was sent to you. Was that a widely held view in AIB?

Mr. Eugene Sheehy: It wasn't my view.

Chairman: Dermot Gleeson ... I just need you to attribute that, Senator ... Dermot ... Mr. Gleeson's commentary of last week.

Senator Sean D. Barrett: Yes.

Mr. Eugene Sheehy: It wasn't my view. As I say, I had a lot ... I had a lot of contact with the regulator and his team. I found them to be tough enough people to deal with. When all the regulatory stuff came down on the SOX, Basel, and IFRS, I know that, where I could call on battalions and experts to come in and help me out, I thought they were dreadfully under-resourced ... is my view, during ... in trying to cope with that weight of change ... technical change. I recall Mr. Gleeson's statement and I've spoken to him about it and he regrets saying it. He says it was in a fit of pique in those hours and days after the guarantee. But I found the regulator and his team to be diligent, hardworking public servants who always acted with integrity.

Senator Sean D. Barrett: The question of property was raised by Jim O'Leary, an economist from NUI Maynooth, at the board meeting on 13 January 2004 ... at your board. What resulted from that query by Mr. O'Leary?

Chairman: Who's this question to, Senator?

Senator Sean D. Barrett: 2004.

Chairman: No, who are you making the question to? Mr. Buckley or Mr. Sheehy?

Senator Sean D. Barrett: Mr. Buckley, I think, was in charge at that time.

Mr. Michael Buckley: I think that's me.

Chairman: And the reference on that question there, if you have it?

Senator Sean D. Barrett: B1, page 74.

Chairman: Thank you.

Mr. Michael Buckley: I believe I remember, Senator, what you're talking about. Yes, I think what happened, Senator, was that Jim O'Leary, at a board meeting in, as I recall it, sort of May-June sort of time in 2004, asked for a presentation about property and construction lending from a strategy, credit quality, etc., point of view, and a detailed presentation was made to the board in October of that year, which covered all of the ... which covered all of those issues, the business strategy, where we had got to, volume growth, and credit quality. And I recall that the presentation was made by, I think, three people. One was the executive responsible for that sector, for lending to that sector from a business development point of view, another was the head of credit in the Republic of Ireland division and the third person was a senior executive from the group credit committee. And, after a wide-ranging review of our activity, our strategy, etc., the credit officers there were asked were they happy with credit quality, did they believe that the risk mitigants that were present in the portfolio were appropriate, relative to the size of the portfolio, and they answered "Yes" to all of those questions. So, in other words, they said that at that point in time, which was, as I recall, October 2004, that the quality ... the credit quality of that book was sound as far as they were concerned. And, I think ... sorry, my recollection is that after the usual questions and challenges that the board expressed itself as being happy with what they had been told.

Senator Sean D. Barrett: Because in the group internal audit report in March 2006, which is B4, page 6, Chairman-----

Chairman: Of?

Senator Sean D. Barrett: Of Vol. 1. What that states ... the audit ... 2.5 years, virtually, later than when Jim O'Leary made his comment in January 2004, the audit in 2006:

The audit did not include an assessment of property related credit quality. In addition we did not raise an issue around the management of concentration risk at a Group level as this was raised in a previous audit of the Credit Framework in 2005.

Given that we now know this is what brought the bank down, wasn't it a remarkably complacent response to the concerns of Jim O'Leary?

Mr. Eugene Sheehy: Chairman, will I take that? It's a 2006 reference.

Chairman: Yes, please. Yes.

Mr. Eugene Sheehy: Senator, if you ... it's important that I just describe how internal audit works. We agree ... I agree with them, and the chairman of the audit committee agrees, every year on a work programme, you know, what are we going to ... what do we need to look at this year? So the work programme ... so we would have asked them to follow this work programme to check out and validate that processes within each function were being carried out. And after that they rate the problems and typically they do find issues and problems there and you can see there's a rating chart - material, significant, important, and minor. If you look at this report, there wasn't any material problems identified and these factors are worked out as a money function - how much could it cost if it went wrong? But the observations, you know, I think are fair. We are ... we always needed to be given a view from fresh eyes in a process - what was going on there and what do we need to concentrate on? So we would always take these results from the audit as a call to action.

Senator Sean D. Barrett: Thank you. Because on B2, Vol. 1, page 19, in May 2007, Dr. Alan Ahearne was making the same concerns to the board ... that property prices were 30% overvalued.

Mr. Eugene Sheehy: Yes, we had a seminar where Dr. Ahearne and John FitzGerald attended and there was a general discussion about that. And, that would have informed our own internal stress-testing model which applied a 30% reduction to residential property as part of our one-in-25 year stress test. So we didn't ignore or dismiss his observations and we took the high end. I mean, Dr. FitzGerald had a lower estimate, but we took the 30% fall, which, of course, would have been unprecedented in experience terms but that was applied in our stress test for residential property. So it was ... his observation was taken on board and applied in the stress test.

Senator Sean D. Barrett: But the eventual discount from the properties transferred by you to NAMA was 56%.

Mr. Eugene Sheehy: Yes. Of course the ... not all the property was transferred to NAMA so ... but even still I count ... dismissing that mathematical effect on the percentage, we all know that the decline in property prices was far higher than anybody expected, worse than the one-in-25 year expectation.

Senator Sean D. Barrett: Mr. Forde told us that the threshold submission to the group credit committee for loan approval was raised from €40 million in 2005 to €75 million in 2006. That's an 88% increase. Did that indicate that this ... we were getting out of touch with ... a property bubble ... to raise the threshold by 88%?

Mr. Eugene Sheehy: The thresholds and the levels of sanction are driven by a number of factors. There's the absolute amount, which you have quoted. There's the sensitivity of the amount to the grade of the sanction, and you will see in the matrix that the poorer grades weren't increased. So you don't increase the lending sanction for the poorer grades; you do for the better grades. And there's also the link between the sanction amounts and own funds. You know, how much can you put on risk of your own funds? There was no increase in the amount of risk you could put on own funds because own ... I'm talking about equity, because that had increased in the same period, so that was capped at 2.1% of own funds. The worst performing grades were not increased. So it wasn't a ... the numbers look significant but it was a fairly logical thing to do at the time.

Senator Sean D. Barrett: Could I draw attention, Chairman, to B1, Vol. 1, page 62? There's increase in exposure to a company from €789 million to €991 million where the large ... the group large exposure policy limit was €150 million. So the increase alone at one board meeting was greater than the limit and the eventual ... the new limit was six times what the original one was. Again, did that not illustrate a lending policy which was becoming reckless?

Mr. Eugene Sheehy: I absolutely reject reference to the word "reckless". If you look at that reference there to, on page 62 ... that discussion was supported by a 64 page submission on that credit. It was quite detailed. It's a very large number, but there were very large deals going on at the time. It was participation in a syndicated loan actually. The methodology used there was that when loans went over certain limits, they went to the next level of authority. And they carried with them the approvals and arguments that the various levels prior to that had made. In this case, when we looked at it and it went to board, there was a lot of support. The individual had enormously, much higher net worth, there was professional evaluations, there was in overall, I think, a loan-to-value of around 50% in the entire exposure. So there was ... logically it made sense at the time.

Senator Sean D. Barrett: Yes. The name is redacted. Do we know if this one went to NAMA?

Mr. Eugene Sheehy: Yes. And I'll just ... could I make one reference from the comptroller and auditor's report on NAMA in 2014? And he says:

> There is an apparent inverse relationship between the level of debt and the relative impairment charges for individual debtors at the end of 2012. The rate of impairment for those debtors who owed over €1 billion or more where their loans were acquired was just over 4%. While those whose debts were less than €75 million at acquisition, the impairment was around 21%.

I couldn't have anticipated that at the time and neither did NAMA at the time, but sometimes the bigger relationships because of the diversification that they had, you know ... typically they would all have had significant UK exposure-----

Chairman: Five minutes now, Senator.

Mr. Eugene Sheehy: They ... size didn't mean worse, I suppose is ... that's my point.

Senator Sean D. Barrett: The decision to pay the dividend of €270 million on 26 September 2008 ... that seems incredible in retrospect.

Mr. Eugene Sheehy: It would ... it-----

Chairman: Sorry, that's a leading question, just ask for some ... we all know how much was paid. And I'm sure Mr. Sheehy has a view on it now.

Mr. Eugene Sheehy: First of all, the decision to pay the increased internal dividend was not taken on 26 September 2008. The dividend was paid on 26 September 2008. The decision to pay the dividend was taken in July 2008, for the half year ended June 2008. This is two months prior to Lehman's and the general collapse of the markets. In addition, the question implies that the dividend was ... extra dividend was €270 million. The dividend ... the interim dividend is always smaller than the final dividend. Generally it is a kind of two thirds, one third split. Our interim dividend for the previous half year, June 2006 was 27.2 cent per share. We have 878 million shares, that was increased by 2.8 cent per share, a total cost of €24.58 million. So the €270 million that was paid on 29 September, approved in July, was made up of €270 million, of which €24 million was the increase.

Why did we make that decision? First of all, if the decision was being made in September, no dividend would have been paid. In the post-Lehman's world, no dividend would have been paid. All bets were off at that stage. So when we declared a dividend, communicated it to market ... that notice is filed on the Stock Exchange. It is now a mandatory, contractual obligation to pay the dividend, so you have no leeway to change your mind after you declare it. It is contracted. Shares are bought on the market, either ex or cum dividend from the date you make the declaration.

We wouldn't have paid the dividend in September, if that was when we were making the decision so that's my answer there.

Senator Sean D. Barrett: Could I just return, finally, Chairman, to B5 on page 5? It's a question on which Deputy O'Donnell has raised but these references are a year later and a year closer to the crisis. The payment to the four executive directors was €6.4 million, of which yours was €2.1 million. Was there still no evidence that this was a banking model which was going to cost the taxpayers a lot of money very quickly?

Mr. Eugene Sheehy: This is '05? We are talking about '05?

Senator Sean D. Barrett: This is '07. The document is B5 and the page number is five. And the payments ... the total are Mr. Doherty, €1.663 million; Mr. Forde, €1.394 million; Mr. O'Donnell, €1.273 million; and Mr. Sheehy, €2.105 million. And the total, €6.435 million.

Mr. Eugene Sheehy: Well, at that stage there wasn't any evidence of what was going to come.

Senator Sean D. Barrett: Thank you very much. Thank you, Chairman.

Chairman: Okay, was there much discussion on this matter, Mr. Sheehy? Did it ... was it decided over one board meeting or a series of meetings?

Mr. Eugene Sheehy: The pay issue-----

Chairman: Yes.

Mr. Eugene Sheehy: -----is decided by a separate committee of the board who are advised generally in the absence of the CEO. The CEO would come in when, obviously not when you're there ... not when your own pay is being decided. And the way it worked was, there would be a review of the financials, a review of general governance and behaviour you know did you meet all those criteria . And then a presentation by ... at the time we used a firm called

Kepler.

Chairman: A presentation to the senior board or at that board?

Mr. Eugene Sheehy: No, to the remuneration committee-----

Chairman: The remuneration committee, okay.

Mr. Eugene Sheehy: -----who then minuted those events and those minutes were passed to the main board. And the chairman of the remuneration committee would also verbally report to the board. So the board would have been fully engaged in the outcomes.

Chairman: And this would be decided over one board meeting or over many when it would come up?

Mr. Eugene Sheehy: There was, I think, in all about 40 different schemes that the remuneration committee had to opine on, you know, in seven different countries. So they looked at all of those schemes.

Chairman: I would understand that the remuneration committee would be looking at this quite extensively because that's their job but the board would be the board that would sign off on it. How long would the board give to considering this issue then, because ultimately they have to sanction it?

Mr. Eugene Sheehy: Well, I would be out of the room.

Chairman: Okay.

Mr. Eugene Sheehy: Okay.

Chairman: Okay.

Mr. Eugene Sheehy: But the ... they certainly took time on it. The ... they would be other ... the remuneration committee is made up of non-executive directors.

Chairman: I am aware of how the structure is. And at the senior board level, was there any dissenting voice there? Somebody says look, maybe this is too much this year, maybe there's ... you know, we need to kind of make a measured approach. There's a lot of concern out there. Maybe we should defer it. Any of this-----

Mr. Eugene Sheehy: The full board was aware of my views because I briefed them on it many times, that AIB's policy, my policy and the chairman's policy was to be below the median in the market. And that's borne out, very clearly, in the Nyberg graph.

Chairman: I just want to deal with a couple of issues there just before we tidy up before the break. This relates to the quality of the business model, setting process, just to tidy up there from some of the questions that may be outstanding before we go for a break.

We will be referring to core documents AIB B2, Vol. 1 and that is AIB reference 01278, page 19, paragraph two. What I want to explore with you, Mr. Sheehy, here is the development of the bank's business strategy. I would imagine that this is one of the main responsibilities of the board and try to maybe establish with you how much board time was being taken up with regard to the strategy. And the sort of time that was devoted to discussing the development of the sustainable business strategy. So maybe just to begin with that question, how regularly and how often was the business model that was being operated under your tenure being discussed at board level?

Mr. Eugene Sheehy: Chairman, you'll see from the board minutes that there was in almost all board meetings a business presentation. What we tried to do, given the diversity of the business, was to bring a business to the board every month and say here's this business this is how it's going. So all the businesses were run through, you wouldn't get through them all in one year, what their strategy was, what the market conditions were and that included a property business as you know there was ... they did two or three of those presentations. So the board wanted and demanded to meet businesses and to get a strategic view of where those businesses were going. So that was an ongoing process and part of the planning process. In relation to the overall strategy of the board ... the board obviously got the annual budget and it got a rolling five-year plan as well and to some degree they were linked to remuneration.

Chairman: It's not really on the remuneration issue I'm talking to you, Mr. Sheehy, it would be in regard to the concentrations in property sector lending this is a sustainable business model was there commentary on the board, like we've heard testimony from other witnesses here about what's called the "grow-fast model". Was people saying that we're now begin to mirroring the grow-fast model, that our concentration levels in particular sectors, particularly property, are maybe growing beyond what would be the traditional approach that we've taken? Was there any ... because our examination records are not indicating that, so maybe there's something that we're not seeing that you could tell us this morning that would demonstrate that these concerns were being expressed at AIB level ... at senior board level.

Mr. Eugene Sheehy: The property lending strategy was discussed very frequently and formally, during the credit reviews and you will see a lot of detail in the credit reviews. So ... you know ... it was always there.

Chairman: I'm sure it was discussed and maybe it was discussed in the context that "We're going to have another bumper year this year, that our growth is going to be X and all the rest of it and that our lending targets are being reached", if there were targets in place and so forth, but was anybody at board level saying there is a concern here with how the business model is developing?

Mr. Eugene Sheehy: Well ... those questions were all asked in the context of the credit report, you know the, the half-yearly credit report. Just in ... to put a bit of context on it, Chairman ... the Republic of Ireland business accounted for 43% of the group profits and the property division in the Republic of Ireland accounted for 25% of ROI's profits. So you're talking about between 13% and 15% of the group profits related to this part of the bank that caused, you know, our demise, effectively. So the board had a lot of things to look at but they did look at the property concentration and general what's the view on the market, what are we hearing from our customers, what's the macro indicators. That was a constant, as you can imagine, a constant part of the dialogue of the board.

Chairman: Okay, maybe jump forward a couple of years so, and I want to refer to the ... because I'm still looking at the adequacy of board oversight in regard to internal controls and to ensuring that risk was properly identified, managed and monitored which is what we're talking about now. And I'll go to core document AIB B17 ... B1 ... page 79 and 80. And this relates to EC, under EC treaty rules the bank was obliged to submit a restructuring plan to the EU Commission and this was finalised in April 2010. It was further updated in 2011 and further revised again in 2012. Now the question I'm putting to you here, Mr. Sheehy, in it's revised 2012 EU restructuring plan, paragraph 3.9, AIB acknowledges that its decision to expand into property was misguided and that its risk management and internal governance systems were not as effective as they should have been in controlling this risk. Now could you please comment upon this and maybe come to them in regard to your earlier comments to me as well.

Mr. Eugene Sheehy: Certainly, Chairman, I mean its a 2012 document. Obviously, I didn't write it and it, it's a hindsight view of what happened and ... you know ... we got the property decision wrong. So-----

Chairman: So would you believe that, going back to our earlier discussion on the earlier question, that at board level, was there enough attention being paid or was there enough cognisance of the concerns that may have been operating in the banking model operated by AIB at that time?

Mr. Eugene Sheehy: The board and the senior management took the thing very seriously, we talked about it all the time, it was not neglected as an issue. So I do think there was a proper focus of attention on it.

Chairman: And would you see the comment you just made to me as then being congruent with the position that AIB acknowledges its decision to expand into property was misguided and that its risk management and internal governance systems were not as effective as they should have been in controlling this risk?

Mr. Eugene Sheehy: Not as effective but not for-----

Chairman: Which an examination of that period as opposed-----

Mr. Eugene Sheehy: Not as effective as it should have been but not for lack of effort.

Chairman: Okay but you would see that ... both your position and this position as being congruent?

Mr. Eugene Sheehy: Yes.

Chairman: Okay, thank you very much. I now propose that we take a break and that we return at 11.25. Is that agreed? Agreed.

Sitting suspended at 11.06 a.m. and resumed at 11.28 a.m.

Chairman: Okay. Everyone back in the room and seated and, this is to remind myself as well, with their phones readjusted to flight mode. We will resume business, okay? All right. So, I am now bringing the meeting back into public session. Is that agreed? Agreed. And just one other matter there, Mr. Buckley, before I bring in Senator O'Keeffe, is if I could just come to yourself, maybe just to explore and get some understanding of the access ... the relationships had ... the access and relationship particularly how ... the relationship that AIB had with the Financial Regulator, the Central Bank and the Department of Finance, okay. And a ... the nature and the appropriateness of that relationship between the Central Bank, the Department of Finance and the banking institutions, in this specific case, AIB. What did you see, Mr. Buckley, as the main purpose and indeed the main outcome of the round-table discussions held with the Central Bank post-publication of the financial stability reports from 2004 onwards?

Mr. Michael Buckley: Chairman, I don't have a very clear recollection of those round-table events or of their connection with the financial stability report. I do remember one, and there may only have been one in my time of those meetings, I do remember one meeting to which all of the chief executives and local managing directors of the banks were invited by the chairman of the Central Bank. I think I have alluded to something I said at it in my ... in my ... in my written statement and my recollection at that meeting, if I am right, if that is the meeting you are alluding to, or one of those meetings, is that it was a meeting at which the chairman of the Central Bank would've gone through that report and would've asked those in the room to ... whether they had any comments or whether they had any issues, would've talked about the banking market in very general terms. So, I would have recalled it as a pretty unstructured meeting in itself. If that's answering your question-----

Chairman: And during that time, because I know you retired in 2005, but how would you maybe characterise the bank's relationship with the Financial Regulator in the period from 2003 until 2005? Mr. Gleeson gave a kind of analogy last week about referees and the relationship, that teams on the pitch have a referee. How would you describe your relationship?

Mr. Michael Buckley: Well, if I could start on-----

Chairman: Mr. Gleeson, my apologies. Mr. Gleeson, yes.

Mr. Michael Buckley: If I could start in 2002, Chairman. My first big interaction with the Central Bank in its prudential role was in 2002 when we had the Allfirst fraud. As you can see, it has marked my recall of my whole time as CEO, but there I found .... what happened at the stage was that we had to deal with a whole lot of regulatory intervention from the Federal Reserve in New York because, remember the fraud had happened in a US-regulated bank with a subsidiary of ours and the local regulator, and what I found was that there was a very professional, very thorough approach adopted by both of the regulators. They worked together, very closely, we had to sign up a memorandum of understanding, we had to undertake a very detailed programme of remedial action. That programme was given oversight by a man called John Hyman, who had been the previous controller ... one of the previous controllers of the currency in the USA. So, and we worked our way very thoroughly. I put one of my most senior executives full time on making sure we met all the requirements. So, in that case I found the regulator acting, if you like, in its prudential mode, behaved very professionally.

The second thing, I'd say, and I am sorry if I'm taking too long but I just want to give you a balanced account. In the FX charges and related issues that came up during 2003-04 which Deputy O'Donnell has already referred to, I found that the regulator which at this stage was on the conduct side, the customer side of it, was very proactive, was very demanding, rightly, as I would say. And again, I found that we got into that way of independent investigation, independent oversight, we had a former Comptroller and Auditor General involved, we had a former Governor of the Central Bank involved. And I found that that relationship was properly demanding from the regulator.

Now, other than those two big crisis events, I would have interacted with the regulator ... and other than the meeting that you mentioned in the beginning ... I would have interacted with the regulator a couple of times a year when our interim results were coming out and when our annual results were coming out, the process was that myself and my finance director would go in the day before, before we made the market announcement, into the Central Bank and have a meeting with the prudential side of the Central Bank. We would present our results to them, they were ... if you like ... we were open to any questions they would ask us and I suppose my recall of those meetings is that ... and I think I mentioned this in my written statement, that they weren't very demanding, they weren't very probing. So, they are my three bits-----

Chairman: Sure.

Mr. Michael Buckley: -----if you like, of my answer.

Chairman: So, during the visits by the Financial Regulator, did the bank ever contact the ... subsequently then financially ... or contact the Financial Regulator or the Central Bank Governor directly in respect to any issue arising from a supervisory visit from the Financial Regulator to your bank?

Mr. Michael Buckley: Well, we would have had, I suppose, my recall of all of that time, is that we would have had a huge amount of interaction, largely like to a fairly considerable extent through our head of compliance at the time but that there was continuous interaction on any issue which raised, if you like, conduct problems or where we were investigating issues that had been raised directly or by us with the Central Bank. We would have a lot of interaction----

Chairman: Mr. Gleeson, in his testimony last week, as I said, familiarised or kind of similarised the role of the regulator as being something like a referee. Now, if to develop upon Mr. Gleeson's analogy of ... a sporting analogy, referees in different codes of sport have different responses to them. In rugby, if the captain acts, operates in a very, maybe, described as a gentlemanly sort of role with the referee, and in soccer terms, maybe the players go nose to nose with the referee. What sort of approach did the AIB take, if they had concerns, as to how the refereeing was taking place, and Mr. Gleeson was saying that it was a very competitive market and the referee should have stepped in to calm things down. But players themselves have a responsibility to come to the referee to say ... at any stage, did you go to the regulator's office and say, "The model as it is developing at the moment, is of concern to us and we would like you to make an intervention"?

Mr. Michael Buckley: No, I didn't, Chairman, and the reason I didn't is that I didn't believe myself that the model was seriously out of kilter during my time.

Chairman: Thank you. Senator O'Keeffe, ten minutes.

Senator Susan O'Keeffe: Thank you, Chair. Mr. Buckley, can I ask you specifically on page 8 of your statement, you say there were periodic requests from the Central Bank Financial Regulator, usually addressed to the chair of the AIB, raising concerns about and asking for reports on the mortgage market and AIB's lending strategy in relation to it. Can you tell us what sort of concerns were being raised at that point? And specifically, the concerns that they were raising.

Mr. Michael Buckley: Okay, okay. I can remember during my time a couple of pieces of work that the regulator had asked us to do on mortgages and essentially the concerns that the regulator was raising was, you know, were we happy that the level of risk we were taking on in the mortgage market was appropriate. Now, could I give you a little bit of background ... only ... I know you don't have much time.

Senator Susan O'Keeffe: I don't and I just specifically want to know what the concerns were, Mr. Buckley.

Mr. Michael Buckley: The concerns were generalised concerns about the mortgage market where LTVs in particular were going, loan-to-value ratios and our response - we would have been a bank who was dragged up the curve by the market in terms of LTVs, because the pace was set by Bank of Scotland, by Ulster Bank, other banks like that and I remember very clearly that our reports back to the regulator would say, “Yes we do give some 90% mortgages”, of whatever number we would have been using, but we are very careful that our policies in relation to giving those sort of mortgages confined them to either to applicants, who are in a special place by virtue of their jobs and their career prospects, let’s say, people in certain professions and second of all, people who were getting significant support from family sources to, in a sense, supplement deposits and things like that, or supplement their repayment capacity.

Senator Susan O’Keeffe: Was the Financial Regulator concerned about anything that AIB was doing?

Mr. Michael Buckley: No, not specifically.

Senator Susan O’Keeffe: Not specifically-----

Mr. Michael Buckley: No, these would have been all sort of industry-wide requests that would have been put out and we would have been responding in terms of our business model.

Senator Susan O’Keeffe: Thank you. Mr. Sheehy, when Mr. Forde was with us here last week, he said that there were meetings going on all over August and September, that there was rising concern in the bank, there were management meetings at the weekend and so on. So, he said ... I asked “Was there a very clear understanding that things were getting very serious?” “Yes”. “For everybody including yourselves?” “Yes”. “And that it could be fatal?” “Yes, that’s fair enough to say”. What would you say to that remark that Mr. Forde made, as a colleague of yours?

Mr. Eugene Sheehy: Well, it’s absolutely accurate. If the system is moving towards a condition where there is no liquidity, it is absolutely fatal, for everybody.

Senator Susan O’Keeffe: In that situation, the bank went ahead as discussed earlier and paid the dividend, because it had been agreed ... I think you told us in June, July?

Mr. Eugene Sheehy: Contractually obligated----

Senator Susan O’Keeffe: Contractually obligated.

Mr. Eugene Sheehy: -----from July onwards.

Senator Susan O’Keeffe: So, you yourselves were in a declining situation at that time, you were having meetings, you were concerned about the fate of the bank, there was ... but you still had to go ahead and pay the dividend. Have I understood that correctly?

Mr. Eugene Sheehy: You’re mixing two things. You’re talking about solvency and I’m talking about liquidity. The liquidity issue was what was of concern-----

Senator Susan O’Keeffe: So-----

Mr. Eugene Sheehy: -----but if you had had no liquidity, absolutely no liquidity, you would become insolvent.

Senator Susan O’Keeffe: Yes, and so that brings us back, I suppose, perhaps to the remark that is attributed to you that night ... that ... about the bankruptcy remark that you’ve discussed earlier. Is it possible that in that context, you may have been arguing that, well, if we are illiquid, we will be insolvent?

Mr. Eugene Sheehy: No, that's not what I said. We were solvent. The system in general and globally was entering into a condition it had never been in before. We had to do something about it. That's what we said to the Government.

Senator Susan O'Keeffe: Why-----

Mr. Eugene Sheehy: But it wasn't ... we had no concerns, no concerns-----

Senator Susan O'Keeffe: You had no concerns.

Mr. Eugene Sheehy: -----about solvency.

Senator Susan O'Keeffe: Okay. Why did Bank of Ireland and AIB ask to meet Government rather than Government ask to meet you or, again, have we understood that correctly from the contemporaneous note, that you guys made the request?

Mr. Eugene Sheehy: We made the request, yes.

Senator Susan O'Keeffe: Why did you make the request?

Mr. Eugene Sheehy: Because 29 September was the most tumultuous day in the history of international financial services and we were a part of it.

Senator Susan O'Keeffe: Had the Government made any indication that day or the previous day that they wanted to talk to you?

Mr. Eugene Sheehy: I think I was talking to officials every day, probably continuously, for 30 days before that. I mean, there was a daily dialogue, there was a daily update on liquidity to the Central Bank. It would be wrong to say there was an event and then a break, it was a continuous contact and dialogue.

Senator Susan O'Keeffe: So, forgive me, I want to go back and clarify the matter about what you actually brought to that meeting because both the contemporaneous notes, yourselves and Mr. Gleeson, you say "We had drawn up an alternative form", and he refers to ... he said, you know, that the Government ... "We had an extensive formula which was eventually adopted later in the night pretty well word for word". They were your contemporaneous notes in 2008, both of you. In 2015 both of you now are arguing that it was, a piece of paper in Mr. Gleeson's case, torn out of a notebook, in your case, I think you said this morning, a slip of paper. So I'm just ... I am confused. I believe other people may also be confused, so if you could clarify your contemporaneous note versus your recollection now.

Mr. Eugene Sheehy: I don't think I say in my contemporaneous note that I brought a form.

Senator Susan O'Keeffe: You say "We had drawn up an alternative form" on page 3 of your contemporaneous note.

Mr. Eugene Sheehy: And that may have happened in the anteroom that we were in. The honest answer ... I cannot remember the piece of paper. We were certainly in dialogue with the Government about technical issues of what should be in, what shouldn't be in, we could have written it out. I have no piece of paper as a record of the night other than my note. If we wrote something down we might have handed it over but it certainly would have been a very informal piece ... if it happened, and I'm not going to try to read into the record something that I'm not sure of. I just don't remember it.

Senator Susan O'Keeffe: What was it you wanted to see Government about then? Why did you want to go ... if it wasn't with something in your hand, and you say it wasn't, then what did you go to do?

Mr. Eugene Sheehy: Well, we felt that on the day, the 29th, with everything that happened globally, that we needed to see the Government, because we were looking at what was going to ... what could happen if you did nothing. That's the problem. What would happen if you did nothing? The Government had already brought out a guarantee on the 20th, which was quite a substantial increase on the previous one. We had adequate liquidity and when we say that we have enough liquidity 'til the end of October or five or six weeks, that assumes that you never get another cent. That's a kind of a ... you know if you keep on funding that keeps on moving out. But you have to take a point in time. The point in time situation was that if the markets froze totally, and there was no reason for an observer, looking at 29 September, to say "I know what's going to happen tomorrow" because nobody knew what was going to happen tomorrow.

Senator Susan O'Keeffe: Okay.

Mr. Eugene Sheehy: So we felt we had to go to the Government and say "Look, this is what we see out there. We ... you know, something needs to be done to stabilise the situation".

Senator Susan O'Keeffe: You've all remarked, pretty much everyone that's come here before us, that you were all very surprised at the fact that all the banks were included. When you heard all the banks were included on the following morning, did you call anybody, did you ring the Department of Finance, did you have any ... "My God, what's happened, why did you do that? We left thinking it was four and now it's six". Or did you just sit down and go "Well there we are"?

Mr. Eugene Sheehy: The Government had made a decision. We weren't going to start coming out and criticising it in ... with the focus that was on the country at the time ...

Senator Susan O'Keeffe: No, I'm sorry, with due respect, Mr. Sheehy, I didn't ask you to ... if you'd came out. I asked you if you were on the phone to anybody asking "Why?", "What had happened?", "What had changed?".

Mr. Eugene Sheehy: The only calls I remember making the next day were about pricing issues in London, which were quite problematic, in relation to deposits. You know, we had a big retail deposit base in London. They were the only calls I made.

Senator Susan O'Keeffe: So you'd argued to have the other two banks excluded but when they were included, you just got on with it?

Mr. Eugene Sheehy: We had no choice.

Senator Susan O'Keeffe: Can I ask you whether you personally ever invested in property?

Mr. Eugene Sheehy: Never.

Senator Susan O'Keeffe: Okay. Were you ever in the Galway tent?

Mr. Eugene Sheehy: I was in the Galway Races I think in 1969 but I was a young fellow at the time.

Senator Susan O'Keeffe: You were. Did you ever have hospitality with property developers?

Mr. Eugene Sheehy: No. I met, I think, two developers in the space of my tenure. One was just a courtesy call to a meeting, somebody who I dealt with when I was a branch manager 20 years before, and the other one was a serious meeting of a developer who owed us a lot of money and I wanted to make the point with the team that things were serious and he would have to-----

Senator Susan O'Keeffe: Finally, Mr. Sheehy, this morning ... you apologised and Mr. Buckley expressed regret, and yet listening to some of the remarks today, I'm still not clear what you're apologising for.

Mr. Eugene Sheehy: Well, I'm very clear. We took too much risk in a sector that turned out to be toxic. I was CEO, I could have stopped it. That's what I'm apologising for.

Senator Susan O'Keeffe: You could have stopped it?

Mr. Eugene Sheehy: In theory, yes.

Senator Susan O'Keeffe: But you didn't.

Mr. Eugene Sheehy: Correct.

Senator Susan O'Keeffe: Thank you.

Chairman: Deputy John Paul Phelan. Deputy, ten minutes.

Deputy John Paul Phelan: Thank you, Chair. Gentlemen, I just want to follow on from that question from Senator O'Keeffe in relation to decisions that could have been made, that Mr. Sheehy has just referenced. Was there any point in your own tenure that you expressed concerns about the concentration of lending in the property and development sectors that you can recall?

Mr. Eugene Sheehy: I was comfortable enough with it until early '08.

Deputy John Paul Phelan: To go back to previous questioning about the guidelines that existed from the Financial Regulator, and, you know, on concentration limits, 200% for a sector and 250% for two related sectors. The constant answer that we've had from other witnesses, including yourselves, is that, you know, a changeover was taking place to Basel II. Did you not, or did you, have any personal qualms about the fact that not only was AIB breaching those sectoral requirements while you were chief executive, but that the breach actually grew once it had been pointed out?

Mr. Eugene Sheehy: Well, first of all I was glad I was aware of it and that it was formally reported and dealt with, you know, in above-board fashion. I took comfort from the fact that it was in transition and it's not possible to totally ignore the context of what you're doing at the time, which was an absolute change from that model, of a kind of a stock percentage model, to a risk-based model. That was what we signed up for. We were in the process of a formal application to change. We were in constant dialogue about what that involved, how the models would work and the regulator was in touch with us. So, point in time, you know, you can say this was happening but there was also a continuous activity going on, changing from that model to another one, with both sides who were involved in it totally participating.

Deputy John Paul Phelan: Outside of the continuous ... I can't remember the exact quote but to paraphrase you, you said that "The issue of sector lending was discussed at board level a number of times". Were there any concrete actions, ever, in your time, from the board of AIB ... decisions on addressing the issue of over concentration in the construction and the property sectors?

Mr. Eugene Sheehy: Well you can see from some of the board minutes the ... when the credit people reported in the half-yearly reports, they would be asked to come back with more information about residential development, and then there subsequently was a ... there was a presentation on that. So there was a dialogue, requests, requests to come back and that happened.

Deputy John Paul Phelan: But was there ... were there any concrete actions taken following that dialogue which took place over a long period of time or was it just continuous dialogue with no actions?

Mr. Eugene Sheehy: Well, there are always actions and, you know, in the risk and credit functions and the sector teams there was constant change in terms of trying to develop better MIS, getting more market intelligence about what was happening. So it wasn't a static thing, it's an organic thing, you're constantly changing ... the market is constantly changing, you're constantly trying to grapple with the conditions when the loan was made, the conditions now, you're reviewing the loan, you're looking at the customer's cash flows, so it's ... it's quite an organic and dynamic process.

Deputy John Paul Phelan: But taking that into account, how then did the concentration continue to grow in that sector right up until virtually the edge of the collapse?

Mr. Eugene Sheehy: Well, towards the back-end of the collapse it was simply the market freezing and that ... there was interest roll-up because there was cash flow problems generally in the second half of '08. Prior to that, we ... our application went in in January '08 for Basel, which was accepted. The regulator didn't change the sector limits at the same time as they got the application and accepted it, that would actually change those limits, and you can see from subsequent correspondence that they intended to engage in a series of meetings to change those limits all the way up to 2010, but those discussions have never happened.

Deputy John Paul Phelan: Can I just change for a second briefly to ask you, Mr. Sheehy, in relation again to your time as chief executive, the targets that were set by the board in relation to earnings per share, did you feel at the time and in the context of where the market was, that they were sustainable?

Mr. Eugene Sheehy: You will see from my written statement that in September '05, I changed when I wrote to the divisions for the planning cycle. There was a five-year rolling view of EPS growth, which was 12% compound, and I moderated it at that time. I stated why I wanted to moderate it. There are all sorts ... there is a mathematical reason, obviously it gets harder to grow on growth. That is one thing. The UK was beginning to soften. We had the three big regulatory projects coming down which were going to cost ... they did cost in excess of €200 million. There was salary cost pressures all the way through the bank because of competitive forces and funding was getting more expensive, so I took it down from 12% to 10%, which is the same as putting an average growth back from 15% to 12%. So I did moderate it because it wasn't sustainable and just as a by the way, changing that measure of five-year plan eliminated the possibility, if those plans were met, of all the LTIPs, the long-term incentive plans, vesting. They couldn't vest because the plan now was less than the minimum hurdle required for them to vest, which was CPI plus 10% compound.

Deputy John Paul Phelan: Can I ask you in relation to the night of the guarantee and the quote that was put by the Chairman and Deputy O'Donnell in relation to the memo? You have more or less ... well you have said that you can't recollect using the phrase. Would it be in your view, or not, a fair statement to say that an official of the Department of Finance who obviously took that memo could have interpreted your comments on the night to mean that there were bankruptcy issues facing AIB in the immediate term on that particular night?

Chairman: The document that was displayed earlier, Deputy Phelan. Yes, okay. Fine.

Mr. Eugene Sheehy: Well, you know, as far as I'm concerned, AIB's solvency was never discussed at the meeting, and as I said, if words like that were used it was in the context of a systemic failure arising from no liquidity for the system.

Deputy John Paul Phelan: Can I ask, did you see Mr. Gleeson's testimony to the committee?

Mr. Eugene Sheehy: I did, yes.

Deputy John Paul Phelan: Is there anything in it that you disagree with?

Mr. Eugene Sheehy: I can't recall ... I mean, I mentioned my view of the regulator. That was one issue between us. He doesn't feel like that. No, I don't recall anything in particular.

Deputy John Paul Phelan: Was there ever a time when you were working with him, when he was your chairman, that he overruled a position that you held on lending concentrations within the bank or on the general direction of the bank?

Mr. Eugene Sheehy: No, there wasn't.

Deputy John Paul Phelan: And was there any point in your time that you yourself held the view that sectoral concentrations in construction and development were too high and you wanted to take the bank in a different direction?

Mr. Eugene Sheehy: No.

Deputy John Paul Phelan: I briefly wish to turn to Mr. Buckley. You stated, and this reference was made earlier - B1, Vol. 1, page 16. It is the Jim O'Leary quote again, which was from a minute from 13 January 2004. You said that there was a presentation to the board following on from that in October 2004. Was it customary that it would take nine months to act on a reservation expressed by a pretty senior economist who was a member of the board, who raised significant concerns in ... at the start of 2004?

Mr. Michael Buckley: I don't recall why the presentation came in October, and I don't know. Could I look at the minutes?

Deputy John Paul Phelan: You can. Yes.

Chairman: Yes.

Mr. Michael Buckley: I am sorry, Deputy, this is a-----

Deputy John Paul Phelan: It is a redacted page.

Mr. Michael Buckley: Yes.

Deputy John Paul Phelan: It is B1, Vol. 1, page 16.

Mr. Michael Buckley: Sixteen.

Deputy John Paul Phelan: The only thing that's not redacted is the reference to Jim O'Leary's comment.

Mr. Michael Buckley: Okay. I ... so what the minute says is on the suggestion of Mr. O'Leary it was agreed that policy in respect of lending to the building and construction sector should be reviewed by the board in the near future. So, I would just say that what it doesn't say is that Mr. O'Leary expressed serious concerns about our approach to property and construction. He wanted a presentation, a complete presentation, so that-----

Deputy John Paul Phelan: Do you believe it was satisfactory that ... I have only four seconds left-----

Mr. Michael Buckley: Sorry.

Deputy John Paul Phelan: -----that it took nine months for an action to be taken on what was an issue being flagged at least at that time?

Mr. Michael Buckley: Sure. But I don't know that it was being flagged in such an urgent way that it required a presentation the next month. I don't know, Deputy. I mean, I think you make a fair point. I just don't remember why it took eight or nine months but when it came it was an incredibly detailed presentation, which is maybe one part of the explanation, and the credit people as well as the business development people were there together so that everybody on the board could get a sense of the balance.

Deputy John Paul Phelan: Were there actions taken on foot of the presentation?

Chairman: Your final question now, Deputy.

Mr. Michael Buckley: Well, when the presentation was made, there was an opportunity for the board to discuss any aspect of it, and the board did not look for any change in policy or anything of that nature as a result of the presentation, and that includes the person who asked for the presentation in the first instance.

Chairman: I just want to-----

Mr. Michael Buckley: So I'm assuming they were all happy.

Chairman: -----just return to the issue of the earning per share there that Deputy Phelan raised with you. Would it be fair to say, just as an outsider, who may be analysing a bank's performance, that the earning per share that a bank would be delivering would be a key performance indicator by which investors might actually judge the relevant attractiveness of a company as an investment opportunity?

Mr. Eugene Sheehy: I think among the analyst community it was by far the most important one.

Chairman: Top of the pyramid, you reckon, yes.

Mr. Eugene Sheehy: In the dialogues that you would have with them in investor meetings it was very important ... because it was a reflection of everything that happened in the organisation.

Chairman: Okay. So in that regard, was it your view that the levels of earnings and the ... in earning per share growth targets set by the board, given the maturity of the market, what was your view on that? You were setting quite significant targets as to what the return should be in this, which would be attracting investors.

Mr. Eugene Sheehy: Well, in the first instance I reduced the targets and the board accepted the reduction.

Chairman: Okay.

Mr. Eugene Sheehy: At the time the market ... we would have been coming in at below the averages in the market. We weren't as fast growing as the medians and that was another one of the reasons why the long-term incentive plans never vested. So, the commentators and investors would have regarded our guidance to the market as moderate.

Chairman: And was the earning per share in terms of how the dividend would be arrived at, was that driven or did it have a reliance on the property and construction lending that AIB were engaging in? How related or relevant would it have been to that?

Mr. Eugene Sheehy: The property and construction was obviously a component of it but, you know ... so 43% of profits came from ROI, one quarter of them came from the Irish property book. No matter what way you look at it, it wouldn't have been significant enough in a weighting to drive the number significantly. I mean, we were actually growing faster throughout this period in capital markets and Poland than we were in Ireland.

Chairman: Okay, thank you. Deputy Joe Higgins.

Deputy Joe Higgins: Gentlemen, can I ask you if you're aware of the testimony of Professor Bill Black to the inquiry?

Mr. Eugene Sheehy: I am.

Deputy Joe Higgins: Yes. In his testimony, Professor Black, who was a renowned regulator and prosecutor of financial institutions that failed in the United States, said that there was a recipe which banks followed which ... that if banks followed, which would "produce the worst losses and is most likely to cause hyper-inflated bubbles" and that recipe includes grow like crazy, and he mentions 25%, and he mentions growth way ahead of economic growth nationally, and also make terrible quality loans. And Professor Black, you will have seen, said three sure things follow: record profits from the institution, then, quote, second: "Under modern executive compensation the senior leadership will promptly be made wealthy" and three, catastrophic losses. Now, gentlemen, can I ask you both, in view of the fact that Allied Irish Bank's growth in 2004 in its balance sheet was 25%; 37.5% in 2005. The bank made record profits in those years. The remuneration of senior personnel was at record levels and then there followed a huge crash. Do you recognise Professor Black's analysis in terms of Allied Irish Bank and do you agree with it?

Mr. Eugene Sheehy: Thank you, Deputy. I think most of Professor Black's observations were based on his US experience, and he did make references to liar loans and the like. In general terms, you know, he is trying to transfer the ... his US observations into the Irish market. When you look at, you know, what he said, if you do grow loans and there is a market crash, which is a one-in-100-year event, banks are going to suffer greatly. Banks absorb the risk between short money and long money and when there's a problem of that nature, it will materialise in falling asset values and problems for banks. So, in general, I agree with his observations. In AIB, our economy was, in those years, held up as probably the highest-performing economy in the world. Our demographics were totally different to the market that he was drawing reference to. So, some of his analogies, you know, are right, but I think the basis from which he is extrapolating one observation to another is fundamentally unsound because it was a different, totally different, economy.

Mr. Michael Buckley: Deputy, would you like me to-----

Deputy Joe Higgins: Yes, briefly, thanks.

Mr. Michael Buckley: -----talk about my time in respect of that. I'll be very brief. The point I would make, I've made it in my opening statement, which is that in the period that I'm talking about, up to this time, 2005, you know, we were in - we, as in the economy - was in a big, big catch-up phase. I mean, you can't ignore the fact ... sorry, one can't ignore the fact that the population did increase by a million over that period of '71 to 2001; that the labour force had increased by 32%; that the employed population had increased by 49%. I mean, people had to be housed, they had to go shopping. They were moving into urban areas from the country on a continuous basis, so I think the Irish economic situation was a bit different to, if you like, the model that ... I haven't read his testimony, but-----

Deputy Joe Higgins: Can I put it to you, gentlemen, that already by the 1990s there was a substantial body of study of banking crises internationally, which had all the features, virtually, of what happened in Ireland? Mr. Black, for example, supplements ... or his analysis is supplemented by an article written in 1993 by two Berkeley professors, one of whom, George Akerlof, in a Nobel laureate. I don't expect you or I ... my question isn't predicated on you having read this article. It is referred to by Professor Black in his evidence. The article in question, "Looting: The Economic Underworld of Bankruptcy for Profit", lays out precisely the strategy I have discussed. I quote from that article:

> Our theoretical analysis shows that an economic underground came come to life if firms have an incentive to go broke for profit at society's expense (to loot) instead of to go for broke (to gamble on success). Bankruptcy for profit will occur if poor accounting, lax regulation or low penalties for abuse give owners an incentive to pay themselves more than their firms are worth and then default on their debt obligations. Bankruptcy for profit occurs most commonly when a government guarantees a firm's debt obligations.

That was in 1993. Mr. Sheehy, could I ask you why, considering the substantial body of literature that exists and analysis, which I don't have time to go into, why were you chief regulators, or risk officers, and indeed yourselves, as senior officers, were you aware of this analysis of banking crises? Even Sweden, a few years before you came in to-----

Chairman: Deputy, I'm going to have to allow time for a response as well for the questions made.

Deputy Joe Higgins: Yes. Why would you not have been aware of this, or were you?

Mr. Eugene Sheehy: The premise of your question was that people go into banks to loot the bank or loot the shareholders or loot the State.

Deputy Joe Higgins: I was just quoting the-----

Mr. Eugene Sheehy: Yes, but you quoted it to me and you framed the question from that quote. That is not the case, never was the case. The people in the bank that I had the privilege of working with, by and large, almost entirely, totally committed to doing a good job and having a long career in the bank. That was what people ... that's what motivated people. I've never met anybody in the bank, or in any of ... most of the other banks that I've met who had anything other than a long-term, stable, repeat business, grow your market share, stay there for the long haul, that's the way people operated in the bank and all the records and all the references in any of the documents you'd have seen would confirm that.

Deputy Joe Higgins: Mr. Sheehy, Professor Black says that there is a perverse incentive for senior executives to increase the balance sheet because it's linked to their salary and bonuses. The record of AIB, annual reports will show, that your remuneration substantially increased, along with a substantial increase in the balance sheet growth. Was Professor Black correct?

Mr. Eugene Sheehy: He wasn't. As I explained earlier on, the remuneration of the chief executive officer - me, when I was there - was based on market comparisons and norms. I told the remuneration committee and the board - and they knew it very clearly, as did the director, as did the chairman - that I wanted my salary to be the lowest in its peer group, relative to the size of the bank, and that's in the Nyberg report, page 7, there's a chart of it there. So, there was no relationship, none whatsoever, between my salary and the size of the bank's balance sheet. That's a fact. You can look up the remuneration committee notes. You can look up the terms of the remuneration committee. The factors that went into it, the discussions at the board, there is no connection or validity to what you're asserting.

Deputy Joe Higgins: Mr. Sheehy, between 2005 and 2009 you earned, in salary and bonuses, €7.6 million, which would take an industrial worker 190 years to earn. In view of the apology you made and the mistakes that were made, which you said, did you consider giving a contribution-----

Chairman: Last question, Deputy.

Deputy Joe Higgins: Did you consider giving a contribution to the taxpayer from that amount of money? And, lastly, you were obviously a substantial lender to homeowners, owner-occupiers. The fact that the price of a home was increasing by the equivalent of the average industrial wage each year from '96 to 2006, putting young people, by common consent, in a dreadful situation of up to 40-year mortgages, unsustainable loans-----

Chairman: Deputy, ask your questions, please, because you're going to run out of time and the Deputy won't have time to respond.

Deputy Joe Higgins: -----did that ever occur to you, as a moral issue, the difficulties that young generation was being put in by the profits that were being made?

Mr. Eugene Sheehy: Well, there's ... you're asking me five questions, I'll try to ... I paid tax on everything I earned. I made a voluntary reduction in my pension after I left. In relation to the creditworthiness of first-time buyers, we followed a strategy of not following the market. We had, I think, 151,000 mortgages; 2,660 were 100% finance, which is less than 2%; the market was 8%. We monitored, on a monthly basis, what a standard application coming into our counter would be, *vis-à-vis* all our competitors and it was always the lowest. We changed it a little bit towards the end and, if you looked at the published information as at 31 December 2010, in AIB, the 90-day-past-due rate for mortgages, and that's ... 90 day past due is not an opinion, it's a fact - you have to be 90 day past due to be 90 day past due - was 2.5%, which was by far the lowest in the market. Subsequently, it changed when the bank merged with EBS, who had a different rate, but I think the mortgage process in AIB was best in class. The numbers substantiate that.

Deputy Joe Higgins: Do you agree that the level of-----

Chairman: Deputy, you're completely and totally out of time, and I need to come back to a question now that we need to ask, which is related to this. And that is the appropriateness or the credit policies operating ... because the grow-fast model ... or whether a sustainable model is in place, a bank will always want to be profitable and the ... as does any other business ... and to do that it has to grow its business, and in banking terms that means issuing loans. Mr. Sheehy, if I could put the issue of AIB Group's large exposure policies, this is the GLP as it's referred to, and the limits as to whether there were hard limits or soft limits ... and how exceptions would be granted. And, it could be suggested that exceptions were sanctioned regularly by sub-board committees. Could you explain to the committee what processes and actions were taken to monitor - and I'm referring to core document AIB 2, pages 25 and 35 to 37 - so if you could explain to the committee what processes and actions were taken to monitor and remediate the regular approval of exceptions to the group large exposure policy limits? This would be, kind of, "There is exceptional circumstances here, loan shouldn't be granted, but let's look at it again and maybe grant it"?

Mr. Eugene Sheehy: Okay, Chairman, just at the start there you said about banks want to grow by growing loans. They don't actually.

Chairman: Okay.

Mr. Eugene Sheehy: The less loans you have, and the more profit you make, the better.

Chairman: I stand corrected.

Mr. Eugene Sheehy: You want to grow by margins.

Chairman: Yes.

Mr. Eugene Sheehy: But anyway, the group large exposure policy ... clearly there was a stratification of risk and levels, and it was built on a principle of the loan originator and the loan sanctioner being separated. So what the escalation of sanctioning - if you go through the various committees - meant was that in each case, first of all, you were going through the committee process because the loans were getting larger, and that's a fact. And, you know, we talked about a big loan earlier on. But to me there was a benefit of ... in this process, which was you got fresh eyes at each level, and feedback and interaction. So the group large exposure policy, and the passing on of when people went over certain limits into their next level was, I think, is a positive process in looking at risk. It's a positive process. It can look, because the loans are bigger, as just some kind of a default thing that as it gets bigger it just goes up and gets approved. That's not the case. As it goes up, it gets further and further interrogated before it's approved.

Chairman: Mr. Daly, in his testimony to this inquiry last week, gave a testimony as to what he saw the banking model actually was, and, as has been stated here this morning, when the whole thing came crashing ... the debt for AIB, regardless of any other bank's behaviour, was approximately €20 billion. And I'm asking you to comment upon Mr Daly's testimony when he says:

> While internal bank lending documentation may indicate that the loan-to-value ratios were, typically, less than 100% when the loan was drawn, the reality, in many cases, was that a developer's equity contribution was in the form of a rolling-up of unrealised, paper profit from other developments. This was presented as an equity position. Rarely, if ever, was it in the form of cash.

So basically what Mr Daly is implying there ... that as a development was under way, its equity was growing probably beyond the original valuation of the purchase or development at the site; therefore, the equity then could be offset against a new development. He then goes on to say:

> In effect, therefore, the banks were providing all of the real cash funding for both acquisitions and development. It's safe to say that quite often the borrower's paper equity position never paid for an acre of land or concrete or scaffolding or a worker's wage at the end of the week. The safety zone of borrower equity usually existed only on paper. The result is that the borrower was typically not the first to lose. In the event of a crash the banks stood to take 100% of the losses, and that's what happened.

Is that what happened in AIB?

Mr. Eugene Sheehy: No. I understand exactly what Mr. Daly was saying. And if you look at a loan application, where an individual could have been in business for 20 years in a trade, i.e. property construction, and has developed a net worth in that business, there are a couple of options open to the individual. They could say, "I'll cash out here and take my cash off the table," and try to continue on with non-recourse lending ... trying to get that ... "Or I'll leave everything I have in the business". By and large, to my recall, almost all of the developers we'd have dealt with left everything in the business. Now, then you come to the kind of intellectual argument about is leaving everything in the business the same as committing to the business? It is. I mean, if you have made money over decades and you leave it all in the business, and that is then recognised by the bank as equity, not cash, but as equity, I think that's entirely correct. And I'll just go ... add a little bit to it. I mean, when I was a branch manager I dealt with a lot of SMEs and start-up businesses, they never had cash. People who go into business rarely have cash, because when you go into a town you'll see banks lined up on one side of the street, you won't see "private equity" or "vulture fund" over somebody's door. The banks provided equity for people who wanted to ... provided cash for people who wanted to take risks. And, by and large, that came from a trust-based, personality-based decision, a personal guarantee from parents or supporters. So, you can imagine if everybody ... and we had nearly 40% SME customers and builders ... if the bank had a view that we would not back anybody unless they had hard cash, and disregard their equity, the person coming to the bank who wanted to start a business, had a house worth €150,000, a mortgage of €75,000, wanted to get seed capital to start off, and we said, "You know what? Go away, we don't recognise that." Society wouldn't be-----

Chairman: In fairness, Mr. Sheehy, that's not the question I'm asking you.

Mr. Eugene Sheehy: But that's the question ... that's what he said.

Chairman: No, no, what Mr. Daly is implying is the exposure that your practice actually created. It's not that you're giving a few bob to an SME here, or a video shop here, or a health club here. What you were doing was giving compound lending into one sectoral area, one loan after another, after another, that led to an exposure. So a developer built the shopping centre, the equity value in that - no cash transaction - maybe increased by 20%. That 20% then - no cash transference - was used as a notional concept to securitise a new loan to build another development. This was all construction. This wasn't SMEs, this wasn't some guy setting up some carpet shop down the road, these were developing loans that ultimately resulted in all these major borrowers having to go into NAMA with massive loans that your bank had provided. So this is an exposure issue. And what Mr. Daly is indicating in his statement - and Mr Daly may well be back before the committee and we'll get further clarification from himself, and we may call other witnesses back as well - is that the business model operated by banks was creating an exposure in property without any down payment or cash being made. The securitisation was notional equity. Does that reflect the business model that AIB were using? And did it create an exposure?

Mr. Eugene Sheehy: It wasn't a business model. It did happen. And most of the uplift in valuation came from the investment side property. So, if you somebody who was a residential developer, but they had a successful let investment property, you would take an uplift value in that and pass it on. But I agree with Mr. Daly, you know, that it would've been a lot better off if the structure ... the industry structure in Ireland around property, had more private equity, you know, and I think that's happening now. It would have been far superior, and it did increase the bank's exposure, the fact that we released funds on the basis of valuations of uplift.

Chairman: Thank you. Deputy Michael ... Senator Michael D'Arcy.

Senator Michael D'Arcy: Thank you, Chairman. Mr. Buckley, the AIB loans transferred to NAMA, had a discount of 56%. Were you surprised and can you comment on that reduction, please?

Mr. Michael Buckley: I wouldn't have had a view, to be honest, because I didn't know the circumstances, you know. This was, I don't ... I forget when those loans were transferred to NAMA, it was probably 2011, so six years after I retired. I wouldn't have had a basis for determining really whether those loans were transferred at fair value or not fair value, so I'm sorry.

Senator Michael D'Arcy: The reason I ask you Mr. Buckley was because you had 53 months in as CEO or thereabouts and I think Mr. Sheehy you had a little bit less.

Mr. Eugene Sheehy: Yes.

Senator Michael D'Arcy: Yes. You seem very arms length in relation to everything. In relation to AIB.

Mr. Michael Buckley: I don't intend to be. I have to say okay ... that ... I'm sorry if I come across in that way. I mean I'm very happy to explain what happened during ... during my time. Six years after my time I think I am entitled to say I don't really have the information.

Senator Michael D'Arcy: Mr. Buckley have you ... did you have any retail banking experience in Ireland?

Mr. Michael Buckley: No I didn't. But I did in Poland-----

Senator Michael D'Arcy: Did-----

Mr. Michael Buckley: Which was a high risk market.

Senator Michael D'Arcy: Did Mr. Forde, who was appointed head of retail Ireland, have any retail banking experience?

Mr. Michael Buckley: He had moved from AIB capital markets possibly when I was in Poland. I can't remember but around maybe 1998 or something like that so before he was made managing director he would have been in the retail side of the bank in Ireland for about four years.

Senator Michael D'Arcy: And, Mr. Sheehy, how long were you in retail Ireland?

Mr. Eugene Sheehy: From 1971 until 1993 in branches then-----

Senator Michael D'Arcy: You came up through the system.

Mr. Eugene Sheehy: Well I then got involved in ... basically technology, and then business change and then managing the franchise, yes.

Senator Michael D'Arcy: Mr. Buckley, did you agree with Mr. Gleeson's statement that retail banking Ireland ... the retail banking sector of in the Republic of Ireland bankrupted the AIB?

(Interruptions).

Senator Michael D'Arcy: He made that statement last week-----

Chairman: Yes indeed and if Mr. Buckley is aware of it he might wish to give a comment.

Senator Michael D'Arcy: Are you aware of it?

Mr. Michael Buckley: I didn't actually follow his testimony ... and ... and I wouldn't again, I have to say, he was talking about something that happened quite a distance after my time as CEO and I think it's a judgment that I wouldn't be in a position to make.

Senator Michael D'Arcy: You didn't follow last week's ... Mr. Gleeson's-----

Mr. Michael Buckley: I didn't tune into his testimony.

Chairman: I need you to be specific in your questions rather than ... did someone tune in last week then open up a line of questioning. So follow a line of inquiry please, Senator.

Senator Michael D'Arcy: Deputy Higgins quoted Bill Black and Bill Black said that one of the aspects that are crucial for the structure of the banks was "grow like crazy." Okay. You say, ''Grow fast.'' That was the term that was used.

Mr. Michael Buckley: By me?

Senator Michael D'Arcy: I'm sorry. AIB ... and I'm putting it at the both of you gentlemen. ''Grow fast''. And the figure I want to give you -----

Chairman: I need you to be referencing now if you are using comments now back and forth and to put a question to somebody maybe to comment upon it rather than give them the dialogue and then put a question on it.

Senator Michael D'Arcy: Chairman-----

Chairman: Yes.

Senator Michael D'Arcy: Let me go at a different line of inquiry then, Chairman. In 2001 you were appointed CEO. And at that stage then Mr. Sheehy the head of retail was moved to the States.

Mr. Michael Buckley: That was the year after in the wake of the Allfirst fraud. Yes.

Senator Michael D'Arcy: Figures that we have for AIB's growth rates were 29-----

Chairman: Please ...

Senator Michael D'Arcy: Briefing document 1, Nexus 1.

Mr. Michael Buckley: Is this B1?

Deputy Pearse Doherty: No, it's a briefing document.

Senator Michael D'Arcy: It's a briefing document-----

Chairman: Sorry, my apologies.

Senator Michael D'Arcy: It's a briefing document-----

Chairman: Has it been supplied to the witness, has it?

Senator Michael D'Arcy: Pardon?

Chairman: Has it been supplied to the witness?

Senator Michael D'Arcy: Well the figure that we were given, Mr. Buckley, was 29% per annum or from '01 to '08 ... compound.

Chairman: If the witness isn't familiar with it, Senator, and if it hasn't been supplied to the witness I'd like ... there is a due process situation here. So maybe if you can ... you're quite willing and prepared to ... and you're quite free to respond to it ....

Senator Michael D'Arcy: I'll move on then Chairman.

Chairman: Okay, so then if you could just quote core document AIB B1, page 13, item 6 - 14 to 1917 - that may actually be sufficient.

(Interruptions).

Chairman: Yes. I really would be ... if documentation is going to be provided at these hearings that they come through the system so that we can actually have them -----

(Interruptions).

Senator Michael D'Arcy: That document that was available to me was available to the witness as well-----

Chairman: Okay if you could just cite what it is so now and we will use it

Senator Michael D'Arcy: I'm using the AIB briefing document.

Chairman: Okay.

Senator Michael D'Arcy: That 29% increase, Mr. Buckley ... there seems to have been a change in AIB's strategy, which was to grow fast. Could you comment upon that?

Mr. Michael Buckley: In my opening statement this morning I ... among the things I said was ... a point I made that if you rely on percentage numbers when you are looking at growth rates ... I'm talking about lending now ... that it may be misleading. Because ... in my time at the beginning of my time our actual exposure to property and construction overall started at the number of €6 billion ... this was for the whole group and it went up during those four and a bit years to €19 billion. And on the Irish side of it within that number it went from €4 billion to €11 billion. And I said this morning that ... and I would repeat it again .. that in the context of the demographic situation to which I alluded which was unprecedented in the history of the State, that I felt that at that point we were not significantly running ahead of what was required in terms of infrastructure in the country. So the percentages don't ... how do I say ... I don't work off the percentages. I mean what kills a bank is pounds, shillings and pence lent rather than percentages lent so that's really my answer. I hope it ... it meets your question.

Senator Michael D'Arcy: It doesn't really but-----

Mr. Michael Buckley: Doesn't it?

Senator Michael D'Arcy: No.

Mr. Michael Buckley: What-----

(Interruptions).

Senator Michael D'Arcy: Mr. Sheehy, you made the point that the bank took too much risk. In relation to-----

Mr. Eugene Sheehy: I did yes.

Senator Michael D'Arcy: Mr. Buckley, did the bank take too much risk in your time?

Mr. Michael Buckley: No. In my view.

Senator Michael D'Arcy: It didn't?

Mr. Michael Buckley: No. In my view.

Senator Michael D'Arcy: From '01 increase of the balance sheet for your period to mid-2005-----

Mr. Michael Buckley: From ... in ... property overall from €6 billion to €19 billion ... I would say "No". And from €4 billion to €11 billion in the Republic of Ireland I would say "No" in the context of what the economy required and what customer needs were at the time.

Senator Michael D'Arcy: €6 billion to €19 billion, a trebling of the loan book in your period.

Mr. Michael Buckley: Well ... your into percentages again now.

Senator Michael D'Arcy: That was the numbers.

Mr. Michael Buckley: So I'm saying in money terms that's what it was and in relation to the requirement to build infrastructure of housing, roads, schools, shops, offices, that was not an irrational amount of money to be lending into that marketplace.

Senator Michael D'Arcy: Can I ask Mr. Buckley also were senior management conflicted by the bonus system and the remuneration that Deputy O'Donnell discussed earlier? And were the focus upon earnings by share and the document I am quoting is AIB B1, Vol. 1, page 45, 31 March 2015.

(Interruptions).

Mr. Michael Buckley: This is a document written in 2009 looking back over the whole period.

Senator Michael D'Arcy: The Good Times - AIB (1988 to 2007). AIB B1. Vol. 1-----

Mr. Michael Buckley: Oh sorry. B1, Vol. 1. I have that. Page-----

Senator Michael D'Arcy: Page 45.

Mr. Michael Buckley: Page 45 sorry. That I thought there was a document written in 2009.

Senator Michael D'Arcy: It says, "Reported EPS [earnings per share] Growth 2003: AIB: 3%-----

Mr. Michael Buckley: That-----

Senator Michael D'Arcy: ... percent

Mr. Michael Buckley: Yes sorry-----

Senator Michael D'Arcy: -----Anglo 30%."

Mr. Michael Buckley: Sorry. I misunderstood you. It's a document written in 2009 looking back over the whole period from 2001 to 2009. I mean the page you are refer to says reported EPS growth in AIB, in 2003, 3%, and EPS growth forecast 2004, 6%. They are small numbers particularly relative to those produced by the bank that is lined up underneath the AIB numbers.

Senator Michael D'Arcy: Can I ask Mr. Buckley ... you say that ...

(Interruptions).

Senator Michael D'Arcy: You say that you didn't think the bank took on too much risk in your period as CEO. Was there any reckless lending occurring? And was that reckless lending rewarded by AIB?

Chairman: Reckless is leading now. You can ask as to the quality and the-----

Senator Michael D'Arcy: But can I qualify last weeks-----

Chairman: Yes, please.

Senator Michael D'Arcy: Mr. Donal Forde who was head of retail did say that there was reckless lending.

Mr. Michael Buckley: But he did not say that there was-----

Chairman: Sorry, unless you are using a quotation from somebody, Senator, I need you to pull up the document and say that is somebody saying that like, you know.

Senator Michael D'Arcy: I did say that, Chairman.

Chairman: Yes but we reference it and produce it.

Senator Michael D'Arcy: I don't have the reference in front of me.

Mr. Michael Buckley: First of all, I did watch his testimony. I don't think he used the phrase "reckless lending", but that's a matter of record. The second ... what I would say is that ... looking at this from my point of view, for that period that I am talking about - I had absolutely no evidence, nor is there evidence in any of the core documents that I have got and received, that there was reckless lending or anything that could be described as reckless lending during those years, 2001 to 2005. That's a categorical answer, no evidence whatsoever.

Senator Michael D'Arcy: Just to finish off, Chairman. Are you satisfied, Mr. Buckley, that AIB was properly ran during your tenure as CEO?

Mr. Michael Buckley: It was run to the very best of my ability and my colleagues. That's not to say that there weren't issues and I have talked about them when asked during the morning, and we did our best at all times to fix any issues that arose at the time and to do it a very open and transparent way *vis-à-vis* our customers and *vis-à-vis* our regulators. So, there were issues. There were not issues relevant, I think, to the core of what this committee is enquiring about and we did our best to fix them. And there was no evidence, is no evidence, in any of the books I've got that there was reckless lending, or anything that could be approaching reckless lending, in my time as CEO.

Deputy Eoghan Murphy: Thank you, Chairman. Thank you to both the witnesses. Mr. Buckley, if I may I wanted to talk to you about the new accounting standard, IAS 39, that was introduced in January 2005. Mr. Forde told us that he had a view at the time that this new accounting standard wasn't an appropriate formula. Did you hold that view?

Mr. Michael Buckley: I did, and I'd say 99% of people in the banking industry held the view as well, the same view.

Deputy Eoghan Murphy: Was this discussed with management in the bank and with the board at the time in AIB?

Mr. Michael Buckley: It was very definitely discussed with ... amongst senior management. It was discussed with the auditors, in my time. And I can't refer you to a board minute where it was discussed but I would be morally certain it was discussed with the board. It would have come up as part of our views about why we had to implement this particular regulatory requirement, etc., and the difficulties it would cause us.

Deputy Eoghan Murphy: And did you discuss this then with other banks as well? I mean, was this discussion happening in the banking system as far as you were aware?

Mr. Michael Buckley: I think it was happening very actively in the banking system for the simple reason ... would you like me to tell you why? Would it help if I were to tell you why it was discussed so actively?

Deputy Eoghan Murphy: If you could, yes.

Mr. Michael Buckley: Well, traditionally in banking, you know, people working in banks know that there are good times and bad times, and that there are cycles, that there are lending cycles. And the old way of dealing with all of this was in the good times, you put aside money for the bad times. And what this was doing, essentially, this new accounting standard was saying, "No, you can't put away money in the good times to help you deal with the bad times".

Deputy Eoghan Murphy: Thank you. We have had evidence in relation to cross-cyclical provisioning. I'm sorry, I wasn't sure what you wanted to discuss. Were you aware that the Spanish banks at the time were not implementing this new accounting standard?

Mr. Michael Buckley: I was and that was because the regulator had somehow been able to take a view, which somehow we - it would seem our regulator couldn't - that irrespective of that accounting standard which was coming in 2005, that they would put additional provision and requirements on the banks. My view would have been, you know, if that could happen here .. but we were told - I can't remember why - we were told it couldn't happen here.

Deputy Eoghan Murphy: So you communicated this to the Financial Regulator?

Mr. Michael Buckley: Yes, it would have been in discussion ... yes, it would have come up in discussions with auditors and with the regulator, yes.

Deputy Eoghan Murphy: And, sorry, the nature of that communication ... would it have been a formal communiqué from the bank? Would it have been in a meeting-----

Mr. Michael Buckley: I can't remember, this was ... this was ... I can't remember, Deputy, to be honest, in what form. I would say it came up regularly over all of my period as CEO because this was something coming down the tracks at us in 2005 that we were having to prepare for.

Deputy Eoghan Murphy: And, Mr. Sheehy, in your period then?

Mr. Eugene Sheehy: Yes and I've two views on it. I was on the board of a US bank at the time and they decided to ignore it and the regulator over there said, "You're supposed to do it, but in actual fact you can ignore it" and that's what happened over in America. Here, when like ... I agree with everything Mr. Buckley said, it's a totally nonsensical accounting standard from a banking point of view. It may be appropriate for other industries but for banking it was totally nonsensical. There was a board discussion during my period there. I haven't seen it noted but I did talk to an official in the bank who would have been an executive director at the time and we did discuss it. And we discussed whether we should go to the regulator with our concerns and given that no European country other than Spain had deviated from it, we decided there was no point. Now, I then tried to research what had happened in Spain and why it happened in Spain and there is a very particular reason. For historical reasons, Spanish banks were required to hold very large shareholdings in large Spanish companies. When their tier 1 was being calculated, the equity value of those holdings, which are basically stocks and shares, were included in their total capital. That didn't meet the international standard for tier 1 because of its volatility so the Spanish authorities were able to make the case that, "We have this historical volatile piece of capital in our banks balance sheets - we need the extra comfort of not changing", in effect and having cross cyclical provisions to bolster their resilience.

Deputy Eoghan Murphy: Sorry, just to clarify, Mr. Sheehy. Did AIB go to the regulator or not?

Mr. Eugene Sheehy: No.

Deputy Eoghan Murphy: No, AIB did not go to the regulator?

Mr. Eugene Sheehy: No, I don't recall it, no.

Deputy Eoghan Murphy: Mr. Buckley, do you recall expressing these concerns to the regulator?

Mr. Michael Buckley: I don't recall any approach made to the regulator formally in the case ... in the form of a letter or a paper or whatever. I mean, a lot of these discussions we would have had with the auditor, you know.

Deputy Eoghan Murphy: But given maybe the level of concern that you expressed just previously. Banking institutions were talking about this, you were talking about it, the bank ... why wouldn't you express it formally to the regulator if it was a nonsensical standard?

Mr. Michael Buckley: Because the regulator knew already that that was the case. I mean it was in the ether, you know, in every country really. It was an issue.

Deputy Eoghan Murphy: You knew that the regulator knew that this was an accounting standard that the banks had a problem with?

Mr. Michael Buckley: Yes, I am absolutely confident that the regulator knew that it was an accounting standard that the banks everywhere were unhappy with.

Deputy Eoghan Murphy: Okay, thank you. I will move on then please, Mr. Sheehy, in relation to NAMA's evidence to us last week. They gave us evidence on the extent to which banks were tending to collect income that was going to the debtors and not to the bank once the crisis began - about rental income from office blocks, from shopping centres - and this was in the millions. They gave us two figures. They said that 20% of income from investment assets were being mandated to the banks but 80% of income was being diverted away. And NAMA said that nobody seemed to be following up on it. NAMA then went after this income themselves. Is it the case in AIB that no-one was following up on this income?

Mr. Eugene Sheehy: Well, I was long gone before any assets were transferred to NAMA so I really can't answer it, so I don't know. I accept the evidence obviously, if that's what they say, but I wasn't there.

Deputy Eoghan Murphy: So you can't have a view on it.

Mr. Eugene Sheehy: Well, you know, everything should have gone to the right place, you know ... I don't know because I wasn't there.

Deputy Eoghan Murphy: In relation to relationships then, you mentioned earlier that your own relationships with, say, large developers, people taking large loans, that you had none yourself. So those loans would be made by people underneath you?

Mr. Eugene Sheehy: Correct, yes.

Deputy Eoghan Murphy: And how did you keep track of how those relationships were developed, how they began, how they were managed?

Mr. Eugene Sheehy: Well, these relationships ... in AIB, almost all of our relationships were historically based, you know - we didn't go out looking for new relationships. So these were customers that had been with the bank for a long time. So those relationships were managed and evolved over time. Customers got loans, they paid them back, more loans, they paid them back. So there was a confidence level there. There was a constant change in personnel at the bank. We changed the way these relationships were managed by centralising the management of these sector teams, moving it away from the front line. There is always ... the nearer the banker is to the customer, the greater the risk. That's just a golden rule in banking, okay. So you try to set up structures, processes, reviews and procedures that interject between that risk.

Deputy Eoghan Murphy: What does it tell us about the impairment on the loans that were transferred to NAMA ... that the greater impairments were on the lower level of loans, the lower in terms of value?

Mr. Eugene Sheehy: I was surprised when I saw that in the comptroller's report. I don't know of the cases but it didn't ... it may stand to reason when you look back at it, the bigger the operator, the more likely they were to have non-Irish assets in their portfolio. That would be one definite fact. The bigger the portfolio, the more likely you would have a good chunk of investment property pre-let. So the most problematic asset was residential development land. So the bigger you were, the smaller the proportion that is likely to be in the portfolio. So I think that's probably the cause of that.

Deputy Eoghan Murphy: My final question, and again it's relating to Mr. Forde's appearance before us. Mr. Gleeson said that the Republic of Ireland division brought the bank down. They are his words. And you were chief executive of the group at the time. Mr. Forde told us that in January-February '09, he was completely removed from discussions at executive management level and board level and then, without objectives or direction in terms of a work agenda in his new position, nine months later he then left the bank. What happened there?

Mr. Eugene Sheehy: Mr. Forde reported to me and I decided, and I communicated with him in ... you know, it was a difficult communication. I have had, and I still have, great respect for him and all his professional abilities. I felt it was time for change in the ROI division. We needed to totally reorganise the amount of resources we were going to deploy around the problem and I had to change some personnel. My plan was that I would give Donal a strategic role, because we had so many strategic issues in front of us, and I had such regard for his abilities in that area - he was head of strategy before - that I was confident he could do a great job for us there. However, at that time, I was tasked with so many changing agenda items that I never really got round to give him the direction and accountabilities that I should have had.

Deputy Eoghan Murphy: And was anyone else redeployed at that time?

Mr. Eugene Sheehy: There were a huge number of redeployments. I mean, basically-----

Deputy Eoghan Murphy: At management level?

Mr. Eugene Sheehy: At management level, yes. I mean, there was hundreds of people pulled in out of the business to get onto the cases, particularly trying to get the data right, trying to get the accounts reviewed. Accounts are normally reviewed, by arrangement, quarterly or half-yearly or annually. We now had to try to review everything ASAP. So there was a ... almost every aspect of the way the bank did its business was changed in those months.

Deputy Eoghan Murphy: Thank you.

Chairman: Mr. Sheehy there, Deputy Murphy had raised the NAMA loan book with you. Could I maybe ask you, just to round that off, in relation to the loans acquired from AIB by NAMA, the overall discount rate amounted to 56% eventually. Would you like to comment upon that discount and do you think it was a high or low figure? Was the 56% haircut that was applied justified?

Mr. Eugene Sheehy: There were no loans transferred when I was there because the process hadn't started. Now, I was surprised at the level. I had been expecting, you know, from the ... some statements by the Minister, and when you take into account the first loss position in all these loans was what the customer input was and then there was the bank's LTV ... basically the bank's LTV, and then there was going to be another drop after that, and I honestly thought when I was leaving that the number was going to be 30%, that range. So I was surprised when I saw it. However, I don't know exactly what the process was. The market absolutely collapsed at that point. There was no market. And you could actually, technically, make the point: why had they any value at all? There was no market. You know, if you used IFRS 39 it must have been very difficult to arrive at a number. So I was surprised but the market was so bad, I suppose, nothing will surprise me.

Chairman: Okay. Thank you. Deputy Pearse Doherty. Deputy, ten minutes.

Deputy Pearse Doherty: Go raibh maith agat, a Chathaoirligh, agus cuirim fáilte roimh an bheirt chuig an coiste fiosrúcháin. Can I just ask you, to start off with, Mr. Sheehy, to your knowledge, was there a practice of restructuring criticised loans, you know, for example, agreeing to moratoriums, interest-only, interest roll-up or extensions in the terms and conditions in the period of 2006 to 2008?

Mr. Eugene Sheehy: Restructuring loans, both criticised and uncriticised, is absolutely standard practice. A customer comes in, change of circumstances, "This is what I thought was going to happen; it's not happening", and the bank would look at it. Sometimes it would refuse the request; sometimes it would go along with it but it's standard practice.

Deputy Pearse Doherty: That's fair enough. In normal times it's standard practice in banking to do this. In relation to that period, 2006 and 2008, did you see an increase of the type of restructuring in the way that I've outlined for large property ... commercial property exposures?

Mr. Eugene Sheehy: Well, could I say, in normal times there are always customers in trouble. It doesn't matter whether you have a global problem or not, but there definitely was an increase in 2008, I would say. There wasn't any ... not that I recall, any significant spike before then.

Deputy Pearse Doherty: And would this ... by restructuring the loans, would this put these loans ... would they move them from a category of criticised to uncriticised loans?

Mr. Eugene Sheehy: Well, when a loan is restructured or criticised, it's almost always one event. Cash flow is not coming as expected. So that's ... so you're dealing with a reality ...

Deputy Pearse Doherty: That's not the question. Which ... by doing this, by rolling up interest, by restructuring them, does it move it from a category of criticised loan to a performing loan?

Mr. Eugene Sheehy: In general, it moves them into watch, vulnerable, or impaired. It moves them onto that path.

Deputy Pearse Doherty: But it moves them-----

Mr. Eugene Sheehy: But it may not ... it may not always do so.

Deputy Pearse Doherty: But it moves them out of criticised.

Mr. Eugene Sheehy: Yes.

Deputy Pearse Doherty: Yes. Okay. In-----

Mr. Eugene Sheehy: Not always, but generally, yes.

Deputy Pearse Doherty: Okay. In relation to the position of your bank in the run up to September ... or during September 2008, the liquidity pressures that institutions were facing, but in particular AIB ... did the liquidity pressure for AIB ease during the second part of September 2008 or did it further tighten?

Mr. Eugene Sheehy: From 15 September onwards, i.e. the Lehman bankruptcy, everything got worse. Prior to that I would say, you know, the market was tightening but it was ... we were able to get, you know, adequate funding and we had a good ... as I say, we always had a good piece of leeway in front of us because you know the liquidity hurdles that we ... there was two regulatory hurdles. We were comfortable there.

Deputy Pearse Doherty: But from the 15th, liquidity starting to tighten. Is that your evidence?

Mr. Eugene Sheehy: From the 15th, the world financial system was different.

Deputy Pearse Doherty: Okay. The reason I ask you that is ... and I reference Vol. 2, AIB, C3b as core documents here, and we're on page 50. In the minutes of the board meeting that was held in Baltimore, Maryland, USA, it's reported ... and you reported your interactions with the Central Bank and the Financial Regulator since 7 September. This meeting took place on the 17th, so two days after you report that liquidity pressures increased at that point. You say that there was a systemic need for term debt of up to €15 billion in the Irish market. You go on to say that AIB would breach its regulatory liquidity ratio by the end of October 2008 if market conditions did not ease and term funding became available. It goes on to say Central Bank has been informed of that. The chairperson goes on to indicate that in the absence of a response from the regulators to the systemic funding problem, the matter would be pursued at a political level. The reason I ask you this here is you're making it clear in this board minutes that AIB would have a liquidity problem at October if circumstances didn't change or pressures didn't ease. You've confirmed to the committee that pressures not only didn't easy but actually tightened. So was it the case that AIB was running into a severe liquidity problem?

Mr. Eugene Sheehy: We were in better shape than most. Now, when I say ... when you say October, as I said earlier on, we have the liquidity requirements, the regulatory requirements, and you always have a date which is point in time versus the end date, and that assumes nothing happens in the meantime. There was always going to be funding in the meantime so that date would keep on moving out, but there were real concerns after Lehman's that even offering better prices on term debt would have no effect because people were running to avoid risk everywhere. So we didn't know what was going to happen. The term debt of €15 billion was the kind of money that would be rolling over, kind of three and six month money that would be rolling over, and if that didn't materialise or roll up, it would have had to be replaced somewhere else.

Deputy Pearse Doherty: The point I'm making is, the minutes reflect, is that if pressures ... liquidity pressures didn't ease, you would breach liquidity ratios by the end of October.

Mr. Eugene Sheehy: If we got no more money.

Deputy Pearse Doherty: Yes, if they didn't ease. You have informed the committee that liquidity pressures didn't ease, indeed what happened after this meeting is they tightened. So the question I put to you is, was AIB facing a seriously liquidity problem in October or after that point?

Mr. Eugene Sheehy: I believe we were facing a manageable liquidity problem. We had, you have to think of the way our funding was made up, I mean we ... half of our resources were in retail deposits. We were very stable there. And we also had a huge amount of assets that we could turn into self-funding assets. So we would have had to change things to be better equipped, but we could have done it.

Deputy Pearse Doherty: But you also say in these notes that this matter would be pursued at a political level. This is how serious the matter obviously was being reflected at the board meeting.

Mr. Eugene Sheehy: I thought that ... I think it would be irresponsible if our bank of our... if an institution of our size and importance in the economy didn't give a very honest appraisal.

Deputy Pearse Doherty: Okay, so two weeks later you had, or within two weeks you had the meeting with the Taoiseach and the finance Minister looking for a guarantee for your bank and three others.

Mr. Eugene Sheehy: Yes.

Deputy Pearse Doherty: Okay, the notes ... the memo that you took on 2 October, is there any reason for this committee not to judge them as true and accurate reflections of what happened on those nights?

Mr. Eugene Sheehy: That is what I wrote a couple of days later.

Deputy Pearse Doherty: So you don't dispute anything in the memo.

Mr. Eugene Sheehy: No.

Deputy Pearse Doherty: You may not remember or recall certain events but the memo is correct.

Mr. Eugene Sheehy: It is six and a half years ago. I wrote that two days later. It is as close as I can get to recall.

Deputy Pearse Doherty: So can I ... can I ask you a question in relation to the memo that you took? First of all you say, and this is the same book, page 37, "The Government submitted a form of guarantee, copy attached."

Mr. Eugene Sheehy: Yes.

Deputy Pearse Doherty: Do you have the copy of the form of guarantee that the Government submitted?

Mr. Eugene Sheehy: I don't.

Deputy Pearse Doherty: What did you do with it?

Mr. Eugene Sheehy: Well I obviously must have had something when I wrote the minute.

Deputy Pearse Doherty: Yes.

Mr. Eugene Sheehy: If I said copy attached. When I read that I think, maybe that was what the Government actually announced the next day.

Deputy Pearse Doherty: No, it's just ... let me maybe clarify this here.

> The Government submitted a form of guarantee, copy attached, which in our view, while inspirational in terms, is not what we were all looking for and fell short of lack of specificity. We had drawn up an alternative which included language that was more specific.

So it is very clear from this memo that you took a number of days afterwards that this is not the guarantee that was announced.

Mr. Eugene Sheehy: Yes, it reads like that, but look, I don't have a copy of what it was. I couldn't find it, the bank couldn't find it in its records. And perhaps the Department of Finance have a copy of it.

Deputy Pearse Doherty: So the memo that you took, did you just keep it for yourself personally? Or did you give it to AIB or-----

Mr. Eugene Sheehy: Oh no, that's ... that's a bank document.

Deputy Pearse Doherty: Okay, so it's clear from this memo that there was a copy of the draft guarantee attached.

Mr. Eugene Sheehy: That's what I said.

Deputy Pearse Doherty: And that's not ... that's just not to be found at this point in time to your knowledge?

Mr. Eugene Sheehy: Correct.

Deputy Pearse Doherty: Okay.

Mr. Eugene Sheehy: But I ... and I don't recall what it was either.

Deputy Pearse Doherty: Okay and we had drawn up an alternative form, and again the alternative form is not available to anybody at this point in time either.

Mr. Eugene Sheehy: Unfortunately, no.

Deputy Pearse Doherty: And in relation to the point where, I think it was the fourth interaction, which was the bilaterals, you say that:

> there were also issues in the Government's draft which we were uneasy about relating to the attestations by the Financial Regulator that the system was solvent and that all banks were solvent. We felt that there was clearly a risk in this statement. Subsequently the Government deleted this reference.

So did you see a piece of paper that included a reference, in the Government's guarantee, saying that the banks were solvent?

Mr. Eugene Sheehy: I think it was only verbal.

Deputy Pearse Doherty: Verbal?

Mr. Eugene Sheehy: I don't remember reading anything ... I don't remember a document being on the table.

Deputy Pearse Doherty: Okay.

Mr. Eugene Sheehy: And the reason ... the reason, there was a very specific reason why, I can speak for myself, I was against including that, was that, you know, in market communications you have to be very specific about what you are communicating. This was a liquidity guarantee, it didn't, the solvency issue wasn't relevant as far as I could see-----

Deputy Pearse Doherty: Yes that's quite interesting, because you say it now, and I'll point out the point that you say that it was the Government's draft that you were uneasy with and not verbal communication but that has just been noted. You say ... you give a reason why you were uneasy with the statement of solvency and you said that "if market participants purchased shares in companies, once the guarantee was issued and it subsequently transpired that these companies were not as strong as contended". Why would you be concerned about these companies not being as strong as contended?

Mr. Eugene Sheehy: Well Deputy, I used to spend hundreds of hours every year going over form 20Fs, thousands of pages of communications to the market. And there is a discipline about communicating to the market. You communicate exactly what is factually being dealt with. This is-----

Deputy Pearse Doherty: Did you believe it was un-factual to say that these were-----

Chairman: Just let him respond, Pearse, I'll bring you back in again.

Mr. Eugene Sheehy: It was speculative, you know ... I mean to say something that wasn't related to the communication the Government was making, wasn't necessary.

Deputy Pearse Doherty: But Mr. Sheehy ... Mr. Sheehy, when you left that meeting, and correct me if I am wrong, but from the evidence we have heard, when you left that meeting and when you asked for the insolvent ... the statement of solvency of the institutions to be deleted, that you believed that you were only referring to four institutions that were going to be guaranteed by the Government. And the question I have to ask you again is, did you have suspicions that any one of the four ... because you only believed that the four were going to be guaranteed, but you asked them not to make a statement saying that those four were solvent. Did you have any concern in relation to any of the four institutions that you thought were going to be guaranteed by the Government on that night?

Mr. Eugene Sheehy: In the discussion, we said that this is an unnecessary addendum to a bank guarantee statement. And is unnecessary. And I expressed a view, one of the views, I don't know if I expressed that view at the meeting, but maybe I did. But it was unnecessary.

Deputy Pearse Doherty: You say in this memo again-----

Chairman: You are running out of time, Deputy, so I need your final, final question so I can close now.

Deputy Pearse Doherty: I'll finish now. You say that the reason that you wanted this deleted was that, if company ... participants purchased shares in companies, once the guarantee was issued and it subsequently transpired that these companies were not as strong as contended.

Chairman: Final question, final response Mr. Sheehy.

Deputy Pearse Doherty: Now we heard evidence last week-----

Chairman: Deputy.

Deputy Pearse Doherty: That this was in relation to Anglo and Nationwide. But I put it to you, that you left that meeting believing that Anglo and Nationwide was not going to be guaranteed, so that statement couldn't have referred to those two institutions.

Chairman: Okay, thank you. Final question, final response. I need to move on.

Mr. Eugene Sheehy: Yes and it was unnecessary to have a solvency statement in a bank guarantee statement.

Chairman: Can you just clarify ... just this single point for me. Did AIB have to be guaranteed? Forget about other banks' behaviours, other banks' balance sheets, other banks' position on the night. Did AIB require a guarantee that night?

Mr. Eugene Sheehy: Yes.

Chairman: Okay, thank you. Senator Marc MacSharry.

Senator Marc MacSharry: Thanks very much. During your tenure as CEO, Mr. Sheehy, how much time would the board have allocated to strategy and business model development and its monitoring, as opposed to other work?

Mr. Eugene Sheehy: The board schedule, obviously there was a monthly schedule and a lot of the time in the monthly schedules was taken up with kind of business reviews and updates and scheduled items that would be there for some time. And then every ... every year we had a strategy session, which was normally an off-site, two-day session where we would look at what the issues were for the business going forward.

Senator Marc MacSharry: And at no time was it identified, say going back to the Jim O'Leary issue mentioned earlier, to say that look we are over-focusing. You yourself earlier said that you were happy enough up to early 2008. Were there anybody around the table during the period that said "Look"?

Mr. Eugene Sheehy: Actually one of the off-sites ... one of the strategic meetings we had, I think it was up in north County Dublin, we had Professor Ahearne and Dr. FitzGerald, and that was specifically an off-site about what's the shape of the Irish economy, how does it relate to property and values. So very specifically, some of the strategic thinking and board input would have been around the whole future of this stage.

Senator Marc MacSharry: And following that then, was there any specific actions taken to cool the AIB pursuit of more enthusiastic lenders, let's say?

Mr. Eugene Sheehy: We definitely ... we definitely were quite cool on the mortgage market in terms of the amount ... the amount of people who could borrow ... that could borrow from us and the way we used our debt service calculator. So that remained cool, we were cool on intermediary-driven business. On the other ... on the other side, the commercial and residential property development, we were applying the stress tests and the Basel model, which we thought mitigated the risk.

Senator Marc MacSharry: But didn't, as we know. Can I ask ... you mentioned that you were a branch manager for a period of years in your career. Can I ask, would you have had targets for lending when you were a branch manager?

Mr. Eugene Sheehy: Yes, so I was a branch manager for ten years between, kind of, early 80s to '93. Mostly in Dublin branches quite ... quite large. There was targets.

Senator Marc MacSharry: I get the picture, so there was targets?

Mr. Eugene Sheehy: Yes there was targets.

Senator Marc MacSharry: Would your remuneration be reflected by your performance versus those targets?

Mr. Eugene Sheehy: In those days, there was virtually no bonuses.

Senator Marc MacSharry: Okay, so as CEO, would branch managers have lending targets?

Mr. Eugene Sheehy: Yes. Can I give you a top-down-----

Senator Marc MacSharry: No, it's okay, I just need yeses and nos. It is a very specific line of questioning.

Mr. Eugene Sheehy: The answer is "No". They had targets on three levels and it was called the people performance index. They had to have a profit outcome, they had to have a people index outcome which was a stat survey, and they had to have a customer service outcome, which was a customer service initial shopping survey. I introduced that process in late 2001 in conjunction with HR to actually deal with the issue of a more holistic approach to management in branches.

Senator Marc MacSharry: In reality, and I appreciate that there was this approach, were there targets given to branch managers which manifested themselves in volumes of money lent?

Mr. Eugene Sheehy: Branch managers had no sanction; they couldn't lend. Lending was centralised and credit scored. They could introduce and try to capture the opportunities they found in their franchise. That was their job, but they didn't make the decision

Senator Marc MacSharry: I didn't say they did and the question is not in relation to underwriting. The question is relating to ... are there volume targets?.

Mr. Eugene Sheehy: They had no control over the outcome -----

Senator Marc MacSharry: No, are there volume targets specific to lending for branch managers?

Mr. Eugene Sheehy: No.

Senator Marc MacSharry: So how do you measure the performance of a branch?

Mr. Eugene Sheehy: You measure it three ways ... the profit-----

Senator Marc MacSharry: You mentioned the model there that you had ... What I'm trying to say-----

Mr. Eugene Sheehy: But the bonus was linked to those three measures and they were mechanised and scored-----

Senator Marc MacSharry: So let's say you lent nothing and you took on no investment in increased deposits, how could you reach your target? Was it possible to reach your target by lending less and accepting less deposits? So, say, I'm the branch manager and my branch had a run and I lent nothing. Could I reach my target?

Mr. Eugene Sheehy: Yes ... you would then not be able to trigger an element of your reward.

Senator Marc MacSharry: Okay, so is it reasonable or not to assume that in order for me as a branch manager to reach my targets that, I along with other issues, would have to increase deposits and increase lending? Yes or no?

Chairman: He can answer any way he wants.

Senator Marc MacSharry: I have asked my question and I have asked that it be answered in a certain way. And no doubt he'll respond without your help.

Mr. Eugene Sheehy: If I'm a branch manager, and as I can't sanction loans, that is a factor that is beyond my control so I have to grow the business through a whole myriad of revenue lines. Lending is one of them and the only function I play in lending is bringing that proposition to the decision makers elsewhere.

Senator Marc MacSharry: Would branch managers be expected to cross sell the products of the branch ... of the bank?

Mr. Eugene Sheehy: Absolutely.

Senator Marc MacSharry: And would they be volume-related or would it be -----

Mr. Eugene Sheehy: Well, there is a very strict code on selling and you can't sell products on volume it has to be on the suitability of the client's needs and that's a documented, regulated process

Senator Marc MacSharry: Would you accept or not that in order for branch staff to reach their targets that they would focus on increasing the volumes of sales of bank products, including loans?

Mr. Eugene Sheehy: They would generally try to drive the revenue in their business through all the different lines of business available-----

Senator Marc MacSharry: Including increased lending.

Mr. Eugene Sheehy: They had no control over that but, yes-----

Senator Marc MacSharry: No, they had no control over underwriting, but in terms of numbers of applications-----

Mr. Eugene Sheehy: Numbers of applications, yes.

Senator Marc MacSharry: Okay, so would it be possible, therefore, that an unintended consequence of the targeting approach of the bank may have led to a volume of applications of a lesser quality? Would it be or not?

Mr. Eugene Sheehy: Because of the way we centralised the management of these relationships, the branches were, by and large, divorced from the volume business.

Senator Marc MacSharry: Okay, I have to move on as I have 2.4 minutes left, not including the leniency that you gave Mr. Doherty there ... so whatever I get for that.

In terms of the interaction with the regulator and the loan-to-values, Mr. Buckley you mentioned earlier on, and I'm quoting, "applicants who are in a special place" ... for example ,you said they may have got help from family and so on, so were there any developers or commercial customers that were ever in a special place, to use your own word?

Mr. Michael Buckley: Well ... let me ... No, to my knowledge in my time is my answer.

Senator Marc MacSharry: And Mr. Sheehy in your time? Were there any applicants of a commercial nature that were in a special place to use your predecessor's -----

Mr. Eugene Sheehy: No.

Senator Marc MacSharry: No. So when Mr. Gleeson last week mentioned that on one occasion the board increased lending, say, and these were his figures, by €200 million from a €700 million position, would that person have been at a special place?

Chairman: Can you just refer to the transcript there if you are using that, Senator MacSharry?

Senator Marc MacSharry: I don't have the exact page but it's there.

Mr. Eugene Sheehy: The case you're referring to was a board decision with a 64 page mark-up accompanied by professional evaluations and net worth statement of €3 billion net of debt. The special place, the name of the individual was irrelevant. It was a financial transaction that was examined forensically as to whether it was a good risk or reward proposition for the bank.

Senator Marc MacSharry: And there was an established process that one would follow in those instances, would there be?

Mr. Eugene Sheehy: Yes.

Chairman: I will give the Senator a bit of time because Mr. Buckley is indicating -----

Mr. Michael Buckley: Just on a point of clarification because I may not have been 100% clear ... the phrase you used about ,"in a special place", could be misinterpreted maybe.. What I was referring to is that in response to a general request from the regulator to all banks to review their lending policies in relation to mortgages, one of the things that came up before the AIB board, and which was reported back to the regulator, was that we have a particular approach which we applied to the generality of people looking for mortgages, and that includes certain formulae to do with loan-to-value ratio and repayment capacity. What we do then is that in certain cases where we believe, and we're talking about categories rather than individuals, in certain cases where we believe that people's repayment capacity will grow quite rapidly in the future or where they have family support, we are prepared to go to a higher LTV then we generally would, that's what I said. So it wasn't about special cases; it was about categories.

Senator Marc MacSharry: I get the point, thanks very much. Right, just three very quick questions, Chairman. First of all, last week Mr. Gleeson again referred to a private conversation with Mr. Lenihan in which he was given the clear understanding, he said, that Mr. Lenihan was of the view that Irish Nationwide and Anglo should be nationalised. Did you ever have - and this is to Mr. Sheehy - any personal conversations or telephone calls with either Mr. Lenihan or Mr. Cowen?

Mr. Eugene Sheehy: Only meetings when there was officials present, no private.

Senator Marc MacSharry: And was that view expressed?

Mr. Eugene Sheehy: The only time it was expressed, it was expressed by me on the night saying that they should be nationalised.

Senator Marc MacSharry: And was there agreement or no response?

Mr. Eugene Sheehy: We weren't the decision-makers; we were dismissed after that.

Senator Marc MacSharry: Okay, before you were dismissed were you given a clear impression or anything like that?

Mr. Eugene Sheehy: No, they were listening.

Senator Marc MacSharry: But you were shocked the next day? Yes or no?

Mr. Eugene Sheehy: That's correct. That's what I said.

Chairman: Next question, Senator-----

Senator Marc MacSharry: I'm nearly there ... Also last week, Mr. Gleeson made reference to article 14.3 in his opening statement of the ECB statute which says that they can intervene with central banks effectively and direct them how to act, and he seemed to think that interest rates should have been using the Taylor rule between 6% and 12% during the boom years. Have you a view on whether the ECB should have intervened? What should they have done if you do have that view? And, very finally, tomorrow we have the opportunity to speak with Mr. Trichet, the then head of the ECB, and I'd be very interested to know any recommendations you might have about what we might ask him?

Mr. Eugene Sheehy: The Taylor rule is a rule that often comes up when people are looking back and saying, "Oh, it would have been good if we had the Taylor rule". Ireland at that time was trying to promote itself, including the Irish Financial Services Centre, as a place to do business that was mainstream European and compliant with all the international standards of Basel, IFRS and everything else. I think it would have been difficult, very difficult for the Irish authorities to carve out a special case while wanting to drive in a general direction of being really pro-central European. I don't know what you would ask Mr. Trichet.

Senator Marc MacSharry: ECB. It is not that the Irish authorities-----

Chairman: Do you have a question?

Senator Marc MacSharry: We know what we did, and could have done, and did not do. What I am asking is, your then chairman had a very specific view, which he articulated last week, that the ECB had authority to direct the Central Bank to act in particular ways to, as he put it, mitigate against the unsustainable nature of low interest rates. I think I am quoting precisely so I am interested in your view on that.

Chairman: Okay Senator, can we get the answer because I need to move on? Mr. Sheehy, if you do have an answer that is.

Mr. Eugene Sheehy: If the national Central Bank ... of the Central Bank tried to increase interest rates here to forestall strategic problems that could have happened in the future, I do not think they would have got much public support.

Chairman: Thank you very much. Deputy McGrath please.

Deputy Michael McGrath: Thank you very much Chair. I would like to welcome Mr. Sheehy and Mr. Buckley. Mr. Sheehy, you passed a comment earlier on that the guarantee did not cost anything. That would be quite different to the commonly-held view about the guarantee so can you just elaborate on what you mean by that?

Mr. Eugene Sheehy: The question was in relation to AIB. The guarantee of the depositors and the bondholders in AIB did not have a direct cost. The cost to the State from AIB was when the assets were transferred. They were less than the value that we thought they were. But the funding of the bank during the tenure of the guarantee was paid for out of the charge that was ordained by the ECB.

Deputy Michael McGrath: Had you any bonds that matured during the two years in question?

Mr. Eugene Sheehy: No. The earliest one was 2013.

Deputy Michael McGrath: Did AIB have senior debt?

Mr. Eugene Sheehy: We had nothing maturing. Senior debt is perpetual so it never matured unless you decided to call upon it. Obviously you would not call upon it during the tenure of the guarantee. There was substantial equity created obviously when the bank put those debt instruments back to investors in offer for other ones, I think over €3 billion of equity created in the AIB book and €15.9 billion in the State overall, in burning the bondholders if you want to use that phrase.

Deputy Michael McGrath: You said in response to the Chairman that AIB did need a guarantee at the end of September 2008, so by extension would the bank not have survived if there had not been a guarantee intervention?

Mr. Eugene Sheehy: I do not think any Irish bank would have survived if there was not a guarantee. Including AIB.

Deputy Michael McGrath: How quickly would it have become fatal for AIB if there had not been a guarantee?

Mr. Eugene Sheehy: Well, we were still in reasonable position five or six weeks out and we had not used any of the other mitigants. For instance, we could have got all our mortgages and turned them into self-funding assets. We could have sold down our corporate loans, probably taken a loss on it. It is speculative to say how long. I would say months and months and maybe over a year. But I do not know, it would depend, it is pure conjecture.

Deputy Michael McGrath: I suppose what I am asking is, if the Government had sent you home that night and said, "Look, we are not getting involved, sort out your own problems", what would the future have been for AIB and how quickly would matters have developed in your opinion?

Mr. Eugene Sheehy: On the liquidity side, I would say and it is pure guesswork, six months to 12 months period or something like that. But you would have a lot of opportunity to do different things during that time, which may or may not have worked. It is pure theory.

Deputy Michael McGrath: You have opened up a question mark there, so just to put the question again, would AIB have survived without a bank guarantee, in your view?

Mr. Eugene Sheehy: The bank could not have survived if it had no liquidity. That is the answer.

Deputy Michael McGrath: And the guarantee provided that liquidity.

Mr. Eugene Sheehy: I think the guarantee was critical in providing liquidity. There was always some liquidity but the guarantee was obviously critical.

Deputy Michael McGrath: Can I just ask about the issue of a four-bank guarantee, because your testimony and that of Mr. Gleeson is quite consistent on that issue? You had the clear impression that a four-bank guarantee was being considered, not a six-bank guarantee. On what basis did you have that impression? The only direct reference in the notes you took on the night is to Mr. Hurley, for example, saying it was impossible to bring down a bank of that size in the middle of the week and could lead to a fumble etc., which is the same word Mr. Gleeson used. So can you be specific? How did you have that clear impression that it was going to be four banks and not six?

Mr. Eugene Sheehy: Principally because we were asked to get €5 billion to Anglo because it could not meet its obligations. So there was no need to say it. That was over.

Deputy Michael McGrath: That was to get it to the weekend. That was your understanding.

Mr. Eugene Sheehy: Yes. My note, my note in the board meeting of the previous evening where I referenced a discussion with officials saying that a four-bank guarantee would be needed if the other two failed or did not get a white knight. So ... it was just assumed really.

Deputy Michael McGrath: You say, again in the notes you took on that night, that you felt ... the view that AIB took in relation to Anglo and presumably INBS was of being closed down, nationalised or put into some sort of run-off position and ring-fenced from the rest of the institutions. They are all very different things in some respects. What were you saying should have happened to Anglo and INBS in your view at that time?

Mr. Eugene Sheehy: Technically, it was totally beyond our experience and competence to even have an idea of what to do, to be quite honest. There was no statutory mechanism. Liquidating a bank is an entirely different process to liquidating other going concerns, because it is a public event. Quite honestly, we did not know what the best thing to do was. We just knew that if they could not fund their obligations the following morning, there was no way forward.

Deputy Michael McGrath: Even with the guarantee of your liabilities, could AIB have survived a disorderly wind up of Anglo? If Anglo had been allowed to collapse the following day and you had a Government guarantee for the four banks, how do you think that would have played out?

Mr. Eugene Sheehy: If we had the four-bank guarantee-----

Deputy Michael McGrath: But Anglo was allowed to fold.

Mr. Eugene Sheehy: There would have been ... I have some notions of what might have happened. There would have been a credit downgrade of all Irish institutions. There would be a systemic mark on Ireland which would have made funding much more difficult immediately, even with a guarantee. There is no doubt about that in my view. But the market would, I think, then have said there is a problem in Ireland and they are addressing the core of it, there would have been a distinction made in due course. It may have taken a number of weeks for that distinction to be accepted by the market.

Deputy Michael McGrath: So the outcome in your view is unclear or not in that scenario?

Mr. Eugene Sheehy: I think we would have managed it with difficulty over a number of weeks. The guarantee would have kept the other four institutions funded.

Deputy Michael McGrath: Okay. Mr. Buckley, can I ask you what was your view on the earnings and EPS growth targets set by the board of AIB, given the maturity of the market? I refer to AIB B1, Vol. 1, pages 43-55, which is a board paper from a seminar. If you wish to comment on that issue - the earnings and the EPS growth targets that were set.

Mr. Michael Buckley: This is over the period, Deputy, to-----

Deputy Michael McGrath: Of your tenure, yes.

Mr. Michael Buckley: -----2005. I felt that - just to give an overall comment - I felt that achieving double digit growth was a realistic target, that it was stretching to some extent, but that it was realistic and if I may take that in the context of the Republic of Ireland division, I suppose to summarise the reason why I would have thought that there was good growth available in the Irish division. Twofold: one, the demographics that I referred to before. Second of all, a point I mentioned in my opening statement, that, while we had a big share of the current accounts of households and individuals and of the working accounts of companies and the strong position with the SMEs that, on a product-by-product basis, we actually had a much lower market share. So let's say in mortgages, while we had 30% of all the current accounts in the country, we had 16% market share in mortgages. So, there was inherent growth potential and when we made an assessment of what would be the net result of doing better on that front, but also reorganising ourselves, for instance by centralising the way in which we dealt with producing mortgages and producing a better proposition, that we would get there. Double digit growth in the sense of 10% or 11% or 12% per annum, in the context of the economy we had, was not a wild or strange target to have would be my view, even still looking back at it now.

Deputy Michael McGrath: Mr. Sheehy, you made reference a few minutes ago to taking a voluntary reduction in your pension. Do you wish to reveal to the committee what your annual pension from AIB is?

Mr. Eugene Sheehy: It was public ... there was a public statement on it. That's on the record.

Deputy Michael McGrath: Okay. Do you wish to confirm the figure?

Mr. Eugene Sheehy: €250,000.

Deputy Michael McGrath: €250,000. And the amount of the voluntary reduction that you took? If you wish to reveal it.

Mr. Eugene Sheehy: I don't wish to reveal it because it is subject to a non-disclosure with the trustees.

Deputy Michael McGrath: Okay. And you took a reduction from the level that ... that you would've been contractually entitled to, is that the case?

Mr. Eugene Sheehy: Subject to a non-disclosure with the trustees at the pension fund who have separate duties ... legal duties, so I have to honour it.

Deputy Michael McGrath: Okay.

Mr. Eugene Sheehy: I did make a ... obviously, I did respond when the bank made a request-----

Deputy Michael McGrath: Sure.

Mr. Eugene Sheehy: -----quickly agreed to it, but you know that's just one constraint-----

Deputy Michael McGrath: Sure. Mr. Buckley, do you wish to reveal your annual pension from AIB?

Mr. Michael Buckley: I'm in a similar position. I have a non-disclosure agreement with the pension fund but I did take a significant reduction in my pension ... substantial reduction in my pension several years ago.

Deputy Michael McGrath: Okay.

Mr. Michael Buckley: And that continues to be the case.

Deputy Michael McGrath: And the non-disclosure requirement provides that you can't disclose the amount of the reduction, is it? Or that you can't disclose your-----

Mr. Michael Buckley: Well, there-----

Deputy Michael McGrath: -----pension?

Mr. Michael Buckley: ------was a general ... I ... I'm trying to remember the precise terms of it, but the general tenor of the non-disclosure was that the pension and the amount of the reduction is a matter between me and the defined ... the trustees of the defined pension scheme.

Deputy Michael McGrath: Thank you.

Chairman: Thank you very much Deputy. I just want to tidy up a few matters, I'll bring in the two leads to conclude and then we'll conclude. Just very specific to yourself, Mr. Sheehy, just your own description, as to how you would briefly characterise AIB's relationship under your stewardship with the Financial Regulator in the period of 2003 and 2008?

Mr. Eugene Sheehy: 2005 to 2008?

Chairman: Yes. 2003 to 2008.

Mr. Eugene Sheehy: Well I wasn't there.

Chairman: Oh sorry.

Mr. Eugene Sheehy: Yes.

Chairman: Okay.

Mr. Eugene Sheehy: So, 2005 to 2008. Professional and robust in every way that I dealt with them. You know, I think they did as well as they could have. They were short of resources when the problems hit and that obviously affected the situation.

Chairman: All right, and just a ... on to round off some stuff on the guarantee, a ... you ... AIB brought a formula of words of some description on that night, as Mr. Gleeson said last week. And it ... this may have been covered already, but should sub-bondholders ... should sub-bondholders have been asked to bail in, by your view?

Mr. Eugene Sheehy: Well I can only talk about AIB. There was no bond ... no bond enhancement for the AIB bonds. And I don't know how the ... you know, what negotiations took place between Government and the EU ... I have no idea. Mr. Trichet will-----

Chairman: And correct me if I am wrong here, by your own testimony today, you seem to have had the impression when you went home that evening, very late into the early hours of the morning, that the guarantee was going to be of one construction to be surprised the following morning to have been shaped in a different way. Do you have a current view as to the appropriateness of the guarantee and how it was put in place?

Mr. Eugene Sheehy: I don't think it's fair for me to have that ... I mean, I have my notes, my recall and how I felt on the next day. I wasn't in there when the decision makers were working on it. I don't know who else was in there or what advice they got.

Chairman: A final issue. Earlier this morning, I think it was on the questioning engaged with myself, you said that AIB was, sort of, monitoring itself against Bank of Ireland than maybe Anglo Irish Bank or other monitors. That was the model space you saw yourself in, yes?

Mr. Eugene Sheehy: Traditionally, yes.

Chairman: Traditionally, okay. So, with reference to those earlier comments, can you maybe explain why AIB needed four times more taxpayers' money than Bank of Ireland?

Mr. Eugene Sheehy: Because we were overweight in development land and I think that was connected to our heavier position in the customer base than Bank of Ireland in SME businesses and self-employed people, particularly outside Dublin.

Chairman: All right. I'm kind of moving into the conclusion here and I'll conclude the final speakers if I can maybe get this covered. You mentioned Sarbanes-Oxley Act this morning, Mr. Buckley, that you were involved in that. Could you just explain to the committee what that actually is? That's an American piece of legislation, that's not an Irish-----

Mr. Michael Buckley: No, but it applied ... it applied generally around the world and it is ... was really about introducing the sort of huge piece of legislation of, I don't know, 800 pages or something like that. But essentially, it introduced a whole lot of extremely detailed sign-off processes at all levels in a, for instance, a banking organisation, to get to the point where the board of directors would sign off the accounts to make as sure as possible that the accounts were representative of the state of the business. So it was a whole new panoply, if you like, of sign offs and cross sign offs, and all that sort of thing.

Chairman: Okay, as I understand it, and you ... my interpret ... because this came up in our engagement with Professor Black as well, is that the Sarbanes-Oxley Act, very much what it does, is it ties senior banking officials into signing off on the true and fair record-----

Mr. Michael Buckley: Yes.

Chairman: -----of the bank. Are there criminal sanctions, then, that arise out of that if ... in that act, that are related to it?

Mr. Michael Buckley: I can't ... I can't remember.

Chairman: Yes, sure.

Mr. Eugene Sheehy: Sarbanes-Oxley was a direct outcome of the Enron scandal.

Mr. Michael Buckley: That is correct.

Chairman: Yes.

Mr. Eugene Sheehy: It related entirely in substance, to malfeasance and misrepresentation at a very senior level in organisations about the state of the companies involved. The sign-offs were to link the leadership of a company to all the public information in that company. And, if there is a disconnect there or a misrepresentation or fraud, that is a legal ... that's a legal problem.

Chairman: Do you have a view in, sort of, robust legislation which kind of ties people tighter into the process that would have very, very strong sanctions being applied? Do you see a shortfall in the current situation there and in where something like this could be done?

Mr. Michael Buckley: I feel that that tie-in is very important, Chairman, and in fact, I think I'm right in saying that relatively recently, it has become much more explicit in the UK for financial services companies at least. But the answer to your question is, I do believe that the tighter it is, the better it is. Because the more review there will be at each level-----

Chairman: But specifically to Sarbanes-Oxley, that the senior banking officials would be tightened in more to the accounts that they are signing off on and that would require ... that

... resulting in, if it wasn't done appropriately, would actually have very significant sanctions, would be your view.

Mr. Michael Buckley: I am saying that that is now in the UK, I think, much more explicitly as well, in financial services.

Chairman: Can we wrap up, Deputy O'Donnell? Five minutes.

Deputy Kieran O'Donnell: Thanks, Chairman. Just a very quick question, Mr. Buckley. The fact that your colleague, Mr. Sheehy, has disclosed what his pension is, would you be ... feel that you might disclose what your pension is at the moment?

Mr. Michael Buckley: I honestly don't feel any obligation to do so. I mean, the general terms of a pension that you get is public information in terms of percentage of salary.

Chairman: It has been answered. Five minutes, Deputy.

Deputy Kieran O'Donnell: Can I go back to Project Omega to Mr. Sheehy, about ... Can you just explain the circumstances of Minister Lenihan's approach to the bank, was there a meeting? Were you surprised with the approach in terms of asking that AIB would take over Anglo?

Mr. Eugene Sheehy: I can't remember whether it was a meeting or a phone call. But it was a ... there was a definite request to look at Anglo and see, could you take it over.

Deputy Kieran O'Donnell: Were you surprised?

Mr. Eugene Sheehy: At that time, I think, everybody was looking at every option because the situation was deteriorating rapidly. I knew immediately that it was a non-runner.

Deputy Kieran O'Donnell: Why?

Mr. Eugene Sheehy: Because we were fully tasked with managing our own affairs. We would have to do due diligence on the company. We didn't have the time to do it.

Deputy Kieran O'Donnell: So were you in survival mode yourselves?

Mr. Eugene Sheehy: We were ... we were not in survival mode. We were managing our assets as best we could and we were reviewing everything. The PwC report was in process at the time. But, like, it wasn't even conceivable that we could take on another risk, for starters. We wouldn't have had the people or the resources to do due diligence on a bank like that, would take, I don't know-----

Deputy Kieran O'Donnell: And two quick questions. What was the reason that Minister Lenihan gave that he wished for you take over Anglo and what was his response when you said you were not willing to take it over?

Mr. Eugene Sheehy: There wasn't a reason. There was a request to look at it and the response, I can't remember how that was communicated, but I don't think there was any surprise.

Deputy Kieran O'Donnell: Can I go back to AIB, sorry, C3b, Vol. 2, pages 37 and 38, and I suppose the question, a very quick question I want to ask is, was there a draft provided on the night of the guarantee by the Government to the banks?

Mr. Eugene Sheehy: I can't remember.

Deputy Kieran O'Donnell: Well, you've stated in your proposals, the Government submitted a form of guarantee which was inspiration. So the question, I suppose, I want to ask is, what did you get in the guarantee that in the original draft provided by Government was not there?

Mr. Eugene Sheehy: Well, we didn't decide on the form of the guarantee. We were asked for our input into it.

Deputy Kieran O'Donnell: What did you request?

Mr. Eugene Sheehy: We requested that it would be two years rather than one.

Deputy Kieran O'Donnell: Okay.

Mr. Eugene Sheehy: We requested that the bonds be included and they hadn't been as far as I know ... I think ... I don't think they were in the original... it could have been a verbal-----

Deputy Kieran O'Donnell: So, in essence, the final agreement outside of the fact that it included Anglo and Irish Nationwide and that it included lower tier 2 subordinated debt, in substance was it the guarantee that AIB and Bank of Ireland requested?

Mr. Eugene Sheehy: It was based on the advice that we gave to the questions we were asked.

Deputy Kieran O'Donnell: But in substance was it-----

Mr. Eugene Sheehy: We didn't make the guarantee. We were asked questions. We gave opinions and inputs. Other people made the decision. So you can say in substance, it was what we advised upon, that's true.

Deputy Kieran O'Donnell: : Okay-----

Mr. Eugene Sheehy: Our advice. Yes.

Deputy Kieran O'Donnell: Are you required as a bank ... were you required to file in any shape or form that the bank was solvent at any time in terms of Stock Exchange reporting or other requirements?

Mr. Eugene Sheehy: All the time. I mean, every day.

Deputy Kieran O'Donnell: So therefore why were you unwilling to allow ... sorry ... Well then, what was your objection to the element being put into the statement that the system was solvent and that all banks were solvent? If a guarantee was being put in place and you were filing on various occasions that the bank was solvent and you claim, and you make a statement here, that AIB was solvent on the night, why, by definition then, did you not agree? I would have thought it should have been a welcome development-----

Chairman: We'll get your thoughts later, Deputy.

Mr. Eugene Sheehy: Yes, I've explained a few times. It was a liquidity guarantee we were looking for. Deposits is what we were guaranteeing. I referred to the fact that clarity was so important to the markets. It didn't work in the US because of muddled communication. We wanted a guarantee of the deposits of the bank. That's all. Anything else that was added to it wasn't on the agenda, never came up that night until towards the end of it. It was our view that is wasn't adding anything-----

Deputy Kieran O'Donnell: And finally, when you were leaving, the last meeting you had, what time was it at? And at that time, were you given the impression by Government ... or who were you given an impression by that it would involve four banks with the outline of the type of guarantee that was put in place?

Mr. Eugene Sheehy: We assumed it was four banks. We weren't given any indication from the Government as to whether it was four or six at the end of the day.

Deputy Kieran O'Donnell: What time was that?

Mr. Eugene Sheehy: I don't know, I mean, I don't know. It was ... I don't know how long we were in the room for the final period before we were asked to go home. I don't know.

Deputy Kieran O'Donnell: What time did you go home at?

Mr. Eugene Sheehy: 3.30.

Chairman: Okay, all right. Senator, Barrett.

Senator Sean D. Barrett: Thank you, Chairman and again welcome to our visitors. Was it ever discussed that you might go the ECB or consult Mr. Trichet in relation to these difficulties?

Mr. Eugene Sheehy: There was one meeting with Mr. Trichet some months earlier. I can't name the date but he was in Dublin and there was a meeting of bankers that was facilitated by the Governor and Mr. Trichet came into the meeting. I don't know what month it is.

Chairman: Were you in attendance at that meeting, Mr. Sheehy?

Mr. Eugene Sheehy: Yes.

Chairman: Senator.

Senator Sean D. Barrett: And the crisis hadn't developed at that stage?

Mr. Eugene Sheehy: No, no it hadn't. The market was, you know, beginning to unsettle, but there wasn't a crisis at the time.

Senator Sean D. Barrett: But having broken the ice, so to speak, it didn't arise that you would, in the critical week, involve him?

Mr. Eugene Sheehy: Well, we would only have a relationship with our own regulator. It wasn't open to us to go past our own regulator or it wouldn't be appropriate to go past our own regulator. There were mechanisms, ELA for instance, which was a mechanism that was available to the regulator to give loans to banks, secured loans to banks, for funding purposes but we didn't ... The regulator didn't want that to happen because when a state regulator facilitated banks with ELA, it was published in the European communiqué from the European central banks, and that then, by extension, became a sovereign issue for that country, so I think the regulator wanted to avoid that, if it could.

Senator Sean D. Barrett: Okay, thank you. On B3, Vol. 1, page 6, there's material from

Mr. Treble who was looking at the loan-to-deposit ratio going up to 157% at the end of 2006, which would brought you second only to HBOS, and that is a more risky form of banking than relying on deposits and, in the same volume he said that targets were set not to go to 157% but to be less than 134% at the end of 2006. And the same document you see that coming into 2007, it was already at 162%. Was that not a risky way to respond to Mr. Treble's concerns about that issue?

Mr. Eugene Sheehy: Mr. Treble wrote a report in the spring of '09 as a look back at what went wrong. He also had ... he was a treasurer, you know, for part of his time, so he would have a view on this and a responsibility .... The loan-to-deposit ratio that we had was targeted to be in the middle of our peer group and if you look at Regling & Watson, page 34, table 12, you'll find that AIB was 143%, Bank of Ireland 173%, Anglo 127% and others up to 250% - that's Irish Life and that's ... I just use data points to show you how unreliable a measure a loan-to-deposit ratio is, because the far more important one is the adjusted loan-to-deposit ratio which imposes constraints. You could fund ... you could have huge amounts of deposits that were very volatile and very short.

Senator Sean D. Barrett: Okay, thank you on that. Now, there was .... for Mr. Buckley ... this is the last one, thanks very much, Chairman. The organisation ... On page 4 of your speech, Mr. Buckley: "The organisational reshaping involved centralising as much as positive routine transactional and processing services out of branches, it involved creating a centralised mortgage processing and decision-making centre". Now, if I could direct to B2 on page 8, the internal auditor says: "There were only three staff members in place in the Galway office who had the skills to manage cases on a daily basis, which includes an assistant manager with responsibility for the unit. This could lead to the bank missing significant events or accounts and the subsequent financial loss," which NAMA had said to us, but it is a theory that a solvent bank with a long history like yours went wrong the day it reduced the power of local managers. Mr. Sheehy did refer to the bank being nearer the customer and centralised everything and Galway, in particular, is mentioned, by the internal auditor as having experienced that difficult. And we did find an emphasis on extending new mortgages rather than servicing the old ones.

Mr. Michael Buckley: I think, Senator, you're connecting two different things there if I may say so but I just haven't had ... haven't been able to get at the document here that you are referring to.

Senator Sean D. Barrett: B2, Vol. 1, page 8, if it comes up on your screen.

Mr. Michael Buckley: B2, Vol. 1, page 8, yes, thank you. In my B2, Vol. 1, page 8 ....

Senator Sean D. Barrett: Maybe I got the lucky one .... yes, B2, Vol. 1, page 8-----

Mr. Michael Buckley: Sorry, Senator, I think I'm right in what I'm saying subject to correction. The first thing you mentioned was about centralising our mortgage decision-making processing out of the branches and that was done. And I think that was a good decision and it meant that there was consistency in decision-making and in dealing with any exceptional situation. The second thing ... the audit report from my recollection over the last two months of reading thousands of pages is an audit report which is talking about our work-out teams managing loans ... commercial loans that had gone bad. So the two things are actually not connected, if I may say so, in the way that you're connecting them.

Senator Sean D. Barrett: Well he does say: '"This could lead to the bank missing-----

Chairman: I need a reference, can you just show me, Senator, just put up the booklet a second so I can ... can you just show me the cover?

Senator Sean D. Barrett: It's B2, Vol. 1.

Senator Susan O'Keeffe: It's B2, Vol. 1, page 21, 31 March.

Chairman: Page 21. Thank you.

Mr. Michael Buckley: Yes, it is ... I think I'm right, Senator. The first point you made was about mortgages and how we were organised to make decisions on mortgages. This, I think, is the ... we had, from recollection, three work-out teams on commercial lending in different ... you know, Dublin, I think Cork and Galway is what I recollect, and he is making the point here that there was a resourcing issue in Galway, and it's a factual point, and there's an agreed management action against it. "I agree with the point raised", which is what whoever the manager was said, "and agree to sit down by the 30th of June to develop and agree a staffing action plan." It's signed by the senior executive in lending in commercial banking, so there was a resourcing issue. It could have ... if it was left to continue it could have had those consequences, but the manager concerned or the executive concerned committed to dealing with it and to be honest, I don't know what happened after that but it sounds to me like quite a straightforward situation.

Senator Sean D. Barrett: Except that NAMA also found it a problem much later. Thank you very much. Thanks Chairman.

Chairman: Okay I'm going to bring matters ... just I'm ... not a question, only just a just clarification, yes?

Senator Michael D'Arcy: On the matter of the question that I put to Mr. Donal Forde, on page 125 of the transcript -----

Chairman: Of which transcript now?

Senator Michael D'Arcy: Last week's, Thursday. We had a meeting at 9.30 a.m. I questioned Mr. Forde, "The expansion of the loan book of AIB for property and construction averaged 29% per annum, and that was in the sector that you were in charge of. Would you have considered your growth in that sector reckless?" His response is, "No. I didn't then." I questioned, "Do you now?" Mr. Forde says, "Yes, in hindsight ... reckless is a strong word." Thank you very much.

Chairman: Okay thank you very much. Right, I'm going to bring matters to a close. If Mr. Sheehy or Mr. Buckley would like to add anything further I'll just give you a moment now.

Mr. Eugene Sheehy: No.

Mr. Michael Buckley: No.

Chairman: Nothing. Okay thank you. Okay so with that said I would like to thank Mr. Buckley and Mr. Sheehy for their participation here today and for their engagement with the inquiry. The witnesses are now excused and I propose that we will break until 2.45 p.m. if that's agreeable to members. Okay? Thank you.

Sitting suspended at 1.45 p.m. and resumed at 2.50 p.m.