Tithe an Oireachtais
Houses of the Oireachtas

Joint Committee of Inquiry into the Banking Crisis

Witness Statement of

Gary McGann

Session 59b

03 September 2015 (a.m.)

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[1] *See s.37 of the Houses of the Oireachtas (Inquiries, Privileges and Procedures) Act 2013*

Banking Inquiry Statement

Gary McGann

Introduction

This written statement addresses the categories/issues which I have been asked to address by the Inquiry in its Direction.

I was a non-executive director of Anglo Irish Bank from 2004 to 2009.

During my time as a director of the bank, I believed the Bank was a properly run organisation. We have all since become aware of certain practices in the bank, which have [redacted] me and which, having regard to pending or potential criminal proceedings, I assume from evidence before the Inquiry to date, I may not address.

Looking back, the bank misjudged the risks that built up in the expansion of lending, particularly property lending, in the years up to 2009. Other banks in Ireland and around the world did too. Factors that seriously compounded the risks to the bank's business model were the Quinn CFD build-up and then the worldwide liquidity collapse in autumn 2008.

I look back with great regret at the collapse of the bank and what that has cost its employees, shareholders and Ireland.

B1 a): Composition, experience and skills of board:

During my time on the Anglo Irish Bank board, it had at all times at least four executive directors who were experienced bankers and there was always a non-executive director who was an experienced former banker. During my period on the board the first of these non-executive directors was Patricia Jamal, who joined the board in January 2003, and was a former Managing Director and Senior Executive at Barclays. Noel Harwerth, who joined the board in February 2007, was the former Chief Operating Officer of Citibank International Europe. These bankers brought perspective from their significant banking experience abroad. The other non-executive directors were well qualified, experienced business people of the highest calibre who brought a wide range of perspectives to the board.

Over my business career I have held a number of senior executive positions and I have also served as a non-executive director and chairman on a number of boards.

B1 c): Quality of business setting model:

The bank had a robust process in relation to the setting of strategy and its business model. There was an annual budget and strategy meeting at which budgets for the year ahead and a strategic review of the bank were presented and discussed. The presentations made by management were extremely detailed. From my experience in other companies, the bank had an appropriate process for setting budgets and reviewing strategy.

In relation to the business model itself, the bank was widely praised right up to 2008 winning many awards including in January 2007, when Oliver Wyman named the bank as the best-performing bank in the world over the previous 5 years. The rating agencies also gave it high ratings. Clearly, with hindsight the bank's lending strategy was unduly orientated to property lending which, as an asset class is cyclical.

B1 d): Adequacy of board oversight over internal controls:

There was a clear and appropriate system of oversight by the board, modelled on best practice at the time, which was reviewed by PWC, who were not the auditors of the bank, in 2004 and 2007. The board performance was reviewed by Hanson Green a firm based in London specialising in Board Effectiveness Evaluation in 2007. The results of these reviews were positive and the board satisfied itself that it had experienced professionals in the areas of finance, control, treasury, legal, risk and compliance and had confidence in the executive team.

Anglo Irish Bank also had a strong internal audit function and retained an experienced external audit firm of high standing, E&Y. To my knowledge, none of these or indeed the regulator raised any material issues with the board's oversight.

B2 a): Appropriateness of property lending strategies and risk appetite:

The board had no role in approving individual loans. The role of the board was to set policies and strategies. It had no role in implementation, which is appropriate. The bank's lending strategy was based on a "triple lock" of cash flow lending, secured on property and with cross collateral and guarantees from other assets/income sources.

The bank's lending strategy and risk appetite should be viewed in the context of the environment in which the bank, and other banks, were operating, including a very strong economy, high employment levels, and the availability of wholesale funding for banks globally.

The bank's property lending strategies were not the only cause of its difficulties. When liquidity froze, the impact was global, economies failed worldwide, the inter-connectivity was exposed and all financial institutions, including the bank, faced serious problems at the same time. In my view the unique combination of the freeze on liquidity and inter-bank lending coupled with huge deposit withdrawals was not anticipated. Its scale and reach impacted globally across the widest range of industry and commerce, and not just banking. In the case of Anglo Irish Bank, the position was exacerbated by the overhang in the market of the Quinn shareholding.

B2 b): Appropriateness of credit policies, delegated authorities and exception management:

Given that the role of a board is to approve rather than to implement policy the approach of delegating the responsibility for lending to the executives with a Board Risk Committee whose role it was to oversee risk management and compliance, was deemed appropriate. During my time on the board I did not serve on the Risk Committee.

B5 a): Adequacy of incentive and remuneration arrangements to promote sound risk governance:

The incentives and remuneration arrangements were structured to incentivise profitability and shareholder value creation within defined policies and subject to appropriate accounting, reporting and audit. Given the significant performance by the bank relative to peers and the markets, the support and validation by many (rating agencies, lenders, investors, business commentators etc.) of the bank's performance, the remuneration was consistent with good market practice at that time.

B5 b): Impact of shareholder or lending relationships in promoting independent challenge by the board and/or executives:

The board operated in a robust and independent fashion without suppression of questioning or challenges, and at no time did I sense that people were inhibited in expressing their views because of any shareholder or lending relationships, or for any other reason.

B6 a): Effectiveness of internal audit:

At no time did I sense that the internal audit function was inadequate or that it was failing in its role or remit. On two occasions during my time on the board, PWC were asked to evaluate the remit and workings of the Audit Committee, of which internal audit was an important interface. With the exception of some small comments, the committee and the internal audit function were found to be satisfactory on each occasion.

There was a separate risk committee in the bank whose remit covered the lending area. One observation from PWC resulted in the risk and audit Committees meeting jointly once a year. There were no material issues that emanated from those sessions that gave cause for concern.

B6 b): Effectiveness of the oversight of the prevailing risk culture:

Oversight of risk was the remit of the Risk Committee. The board and committees, including the Risk Committee, took their remit very seriously, worked hard with strong attendances, significant pre-reading, long specialist committee meetings and regular questioning of the business and the management/executive directors. There were regular presentations of various aspects of the bank's activities including external reviews.

B7 a): Impact of prevailing accounting standards in recognising risks

It is clear in hindsight that accounting standards, as well as many other factors, did not help in identifying and reporting on risks. As the crisis deepened from autumn 2008, the inability under accounting standards to properly reflect the belief of management and the board about the appropriate level of provisioning for bad and doubtful debts added to the bank’s problems.

My sense is that the accounting standards, along with many other aspects of business/society did not ever contemplate the 2008 scenario.

B7 b): Effectiveness of the external audit processes:

During my time as a director of Anglo I considered the bank’s internal audit processes to be very good and this sense was fortified by the positive independent external reviews carried out. My impression at the time was that the bank worked hard to stay on top of its changing regulatory obligations, for example the Basel II requirements.

During my time on the board and audit committee I have no recollection of the external auditors raising any material issue about risk exposures in areas such as property, lending or liquidity. It wasn’t until very late in the day when the macroeconomic environment was imploding that these issues were raised. When normal times prevailed, the fundamental systemic stresses that the bank encountered in the two years before its nationalisation were not apparent.

R1 a): Appropriateness of the regulatory regime:

I have no recollection of the board having received any correspondence directly from the regulator's office and I was not aware that the management received any correspondence from the regulator outlining any material concern or dissatisfaction about how the bank was operating, its business model, its risk profile or its lending practices.

As I understood it, the regulator routinely had reports from the bank (such as quarterly returns). One significant interaction of which I am aware is that under the board’s instructions, the regulator was fully briefed from the outset on the Quinn CFD's and the bank's efforts to deal with them. I was aware that there were significant exchanges with the regulator during the Quinn CFD period. If the regulator had wanted to bring any matter or concern to the board’s attention, my expectation was that he could have written to the Chairman or Senior Independent Director and it could have been dealt with promptly.

I had no reason, at that time, to believe that the regulatory regime was inadequate.

R2 b): Effectiveness and appropriateness of supervisory policy and powers:

As referred to above, the line of communication was with the executives in the bank rather than with the board and I am, therefore, not in a position to comment on the effectiveness or appropriateness of supervisory policy and powers at the time.

R3 b): Nature and appropriateness of the relationship between the Central Bank (including the Financial Regulator), the Department of Finance and the banking institutions:

During my time as a non-executive of Anglo I was not directly involved in any exchanges between the Central Bank and the bank, or between the Department and the bank. As I have said, I was aware of some business as usual reporting between the bank and the regulator and significant exchanges during the Quinn CFD period. Towards the end of 2008, and particularly around the bank guarantee time and the nationalisation of the bank, there was significant activity between all three parties.

R5 d): Appropriateness of the relationships between Government, the Oireachtas, the banking sector and the property sector:

During my time on the board I did not have any reason to believe that the relationship between Anglo Irish Bank and the other parties referred to above was anything other than appropriate.

Gary McGann

6 August 2015