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Joint Committee of Inquiry into the Banking Crisis

Witness Statement of

Matt Moran

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

Joint Committee of Inquiry into the Banking Crisis

Submission of Statement

Matthew E. Moran

6th August 2015

Chairman and Members of the Committee

Please find herewith my statement as requested by the Chairman of the Committee.

For the benefit of all Members, this opening statement provides some background to the areas you have highlighted where I may be able to assist. Specifically, you requested my input in respect of a number of themes and key lines of inquiry each of which I have outlined below.

Introduction

In January 2009 I was selected by the new government appointed board of Anglo Irish Bank as Director of Group Finance. This followed the nationalisation of the Bank and the departure of previous senior management. This was a promotion to a second line executive position within the management hierarchy and I became overall head of the group finance function.

During the period prior to nationalisation I was one of several deputy department heads of function within the Bank's various finance functions, specifically the Irish group finance function based in Dublin. Heads of function sat below the Executive Management Team. The Executive team comprised, the Group Chief Executive, the Executive Director of Lending, Ireland; the Chief Executive of the UK, the Chief Executive of North America and the combined position of Group Finance Director and Group Chief Risk Officer. This structure had been put in place in early 2008, the effect of which was to place four lenders and one non-lender as the executive team responsible for running the Bank.

This serves to highlight the pre-eminence of lenders and lending in the Bank's culture as indeed was the case for most commercial banks. In the year prior to that reorganisation, for a brief period, the senior management committee comprised of five experienced senior lenders and four who were from outside of lending functions. Three of the four non-lenders, including myself, were removed from that committee in the reorganisation. An overview of the governance and operating structures of the Bank is provided separately at Appendix 1.

The finance function of the Bank was primarily responsible for financial reporting, management accounting and regulatory returns. Each area had a specialist leader and team with the requisite experience and expertise the various disciplines demanded. Within the Bank, reporting to the Group Finance Director, there were five finance directors covering the areas where each business operated. These included, the UK Director of Finance & Operations (including Northern Ireland); the Head of Finance in the Isle of Man and respective Finance Directors in each of Austria and Switzerland.

The key role of the finance function in Dublin was to gather the information from the various Irish and North American businesses in order to prepare reporting. Similarly, the Dublin finance function also liaised with auditors in relation to the Bank's Republic of Ireland and North American operations. Finance functions in each of the other geographies were responsible for the preparation and audit of the accounts of their respective entities. A second role of group finance in Dublin was to collate the accounts of each of the overseas businesses and consolidate the results in order to get a full picture for the Group.

In addition, group finance Dublin had a role for the preparation of regulatory returns for the Irish market and for incorporating the regulatory return data provided by other finance functions within the group for the purpose of drafting group consolidated reporting. Regulatory returns were reviewed and approved by a statutory Board Director and submitted on a monthly, quarterly and annual basis as prescribed by regulations. Specific analysis and information concerning risk assessment and provisioning levels pertaining to the Bank's loan book was prepared and signed off by Group Risk.

From early on in the global financial crisis, the regulator instigated additional daily and weekly reporting in respect of funding and liquidity. This was prepared and submitted directly by Treasury and Group Risk Management.

Monthly management accounts for the Board were also prepared by group finance in Dublin. These incorporated the management accounts prepared and submitted by each of the overseas business units. All input on loan loss provisioning was provided to finance by Group Risk.

One of the key objectives of the Bank from the middle of the decade was to ensure that management accounting, and regulatory and financial reporting kept pace with the rapid development and growth of the Bank. Between the years 2003 and 2007, more than twenty experienced accountants were recruited by the Dublin finance function.

The Group Finance Director was additionally appointed as the Group Risk Director in 2008 with a separate executive team that reported outside of the finance function ensuring that finance function was not linked with Group Risk and accordingly had no role in respect of the Bank's risk function. Group Internal Audit was also entirely independent and separate from the finance function, reporting directly to both the Audit Committee and the Group Chief Executive. With its own ring-fenced team it served to provide oversight over the business divisions and other support functions of the Bank alike.

The period from August 2007 through 2008 and 2009 was a traumatic period for all of the Bank's stakeholders. Nobody within the Bank anticipated the depth or length of the economic crisis Ireland would suffer. The economic crash stemmed, at least in part, from the Global Financial Crisis. This was initially signalled by the rescue of Northern Rock on the 14th of September 2007 and the forced takeout of Bear Stearns the following March. It was further exacerbated by the previously unforeseeable decision to allow Lehman Brothers to fall in September 2008 - almost twelve months to the day since the Northern Rock failure.

Official indicators did not signal the scale of issues to come. On the contrary, save for some exceptions, most commentators predicted a soft landing.

Throughout 2008 the international crisis escalated. The inherent difficulties surrounding the entire banking industry, and specifically Anglo Irish Bank's position as a small player in the banking pool, was compounded by the shareholder issues. By these I refer to Sean Quinn's CFD investment in the Bank and problems arising from its unravelling.

Investor relations was an important support function within finance. It became a much larger part of the agenda for many of the executive management and functional heads from early in 2006 onwards, when the Bank raised significant equity capital from international markets on two occasions. The high growth rating given to the Bank began to weaken towards the end of 2007 and early 2008. Investor relations became even more important during 2008 as speculation grew relating to the size of the Quinn exposure. Strenuous efforts were made to resolve this situation through capital market avenues throughout the first half of 2008.

During this time the market was awash with rumours of losses, funding lines being pulled, and so on. Share prices swung violently and were viewed as a proxy for risk. Throughout the financial crisis, the Bank's funding was negatively impacted. However, given the range of markets it had developed, the Bank was able to maintain funding throughout and up to the collapse of Lehman Brothers. As a result the Bank was capable of operating during the crisis for longer than many other institutions in the UK, Europe and the US. The length term available, like for most institutions, became shorter and shorter and hence the liquidity issue became more acute. The prolonged nature of dislocation in funding markets and the ever increasing sense of fear amongst investors, eroded the quantum and tenor of liquidity in all of the Irish banks, and indeed most smaller players globally.

This was a tumultuous period and it is impossible to cover all dimensions of the extraordinary level of activity and the extraordinary happenings of the time. This statement covers areas of which I have a knowledge and endeavours to give the Committee an overview concerning the themes and key lines of inquiry requested.

SPECIFIC THEMES ON WHICH COMMITTEE HAS REQUESTED MY INPUT

The first area of inquiry that the Committee has specified is:

B1 - Effectiveness of Bank's board governance, client relationships and business models

(b) Integrity of financial reporting

The Bank had a number of finance functions in Ireland, the UK and within subsidiaries overseas. Each was staffed by experienced accountants with expertise in financial reporting, treasury, lending and wealth management. These functions had been strengthened by the recruitment of high calibre staff with specialist banking accounting knowledge.

The data for financial reporting was provided by the relevant areas of the Bank, namely treasury, lending and wealth management. This was supplemented with accounts and information from the independent finance functions in each of the other operating geographies. Additional input was provided by the Group Risk Department and other stakeholders. Group finance in Dublin then consolidated the information into the format needed for financial reporting.

The draft consolidated accounts were subject to review and interrogation at several levels both within the Bank and externally. The scrutineers included the Group Finance Director and members of the Board, the Board Audit Committee, the Group Risk Department (for all matters pertaining to risk) and the Group's auditors, all of which were comprised of experienced and senior professional accountants or bankers.

The external auditors had open access to all areas of the Bank's operations. They also met privately with the Audit Committee and its Chairman, for an independent review of the accounts. In addition, at the initiative of the auditors, the accounts were subjected to particular scrutiny by their specialist banking experts, both locally and at an international level, in view of the growing uncertainty about banking sector. The accounts were also presented to the Regulator in advance of publication. This was an intensive process that extended over several months.

Having independently reviewed the accounts, the Board Audit Committee reported to the Board of Directors whose responsibility it was to assess the accounts to ensure they were prepared in accordance with all applicable law and financial reporting standards.

The Board comprised people with deep expertise in financial reporting and accounting standards and banking more generally. Board members, both executive and non-executive, were vastly experienced in their capacity as statutory directors and highly familiar with the working application of the relevant laws and accounting standards. Similarly, the Board had experts who had previously served as consultants to the sector and members with specialist treasury knowledge.

Combined, these factors were designed to underpin the integrity of the Bank's financial reporting.

(c) Quality of the business model setting process

The Bank had a consistent business model over some two decades that focused on a particular niche: lending to individuals, and typically unlisted, private companies. These segments were deemed less well served by universal banks.

Typically, niche focused businesses perform strongly in a robust economic environment. During this time, the Bank was complimented by market participants for sticking to its focused strategy.

The Bank diversified through developing lending activities in the UK and North America, therefore expanding its geographical, rather than its product, footprint. In terms of business focus and risk, bringing the existing proven product line to new markets was seen by the Board as a significantly less risky strategy than any of the alternatives. The business model delivered uninterrupted growth and returns for in excess of 20 years. However, especially in the latter years, the absolute level of loan growth, and associated credit risk, assumed by the Bank reached new levels.

The work ethic of the Bank was goal oriented and provided high levels of customer service. From what I observed, there was a strong camaraderie and a close-knit culture, especially amongst lending professionals.

When the global credit crisis began in August 2007, the severity and rapid nature of the economic meltdown in Ireland exacerbated the credit risk situation without sufficient earnings from other markets to provide cushioning.

The Bank's funding model is dealt with under a later section.

B2 Effectiveness of Banks' credit strategies and risk management

(a) Appropriateness of property-related lending strategies and risk appetite

I was not a lender and I provide this answer as broad background. Property related lending may be split into two categories; investment related lending and development related lending.

Investment property lending is where an investor or operator purchases a property from which to run their own business or to let to tenants. The objective here is for rental or business generated income to be sufficient to service the loan and repay the debt over time. Therefore, whilst banks typically took security over the property, the income generated was the critical factor for loan servicing. The property security was a fall-back position in the event that income reduced or ceased altogether.

Development related lending assumes greater risk and hence attracted higher returns. Here, it is critical to have developers with the requisite experience to handle the planning and construction risk as well as the sales cycle.

Whilst both sectors were impacted, the development sector has resulted in the most severe loss levels. Local market characteristics exaggerated losses in Ireland. Concentration risk, amongst a small number of developers, partly due to the size of the economy, is now understood to have been too high and the ready availability of funding to banks led to too high a concentration of activity in such a small market.

Risk appetite crept up; loan to value levels increased; margins reduced; equity releases were facilitated as people became numbed by the unabated rise in asset values. This was further fuelled by the focus of all banks on growth, as driven by investor and economic policy.

Central banks, regulators and international capital market participants everywhere failed to anticipate the deep, prolonged nature of the liquidity crisis which followed the Lehman Brothers collapse. This was a new, previously unimaginable, paradigm. Bank risk strategies were found to be deficient in these circumstances.

(b) Analysis of risk concentrations in the base, the adverse economic scenarios and the impact on the capital base

The Board Risk and Compliance committee was responsible for setting and overseeing the Bank's risk appetite and risk policy as set out by the Board. In turn, the Group Risk Department was responsible for implementing this risk appetite and policy within the day-to-day operations of the Bank. Within the Bank's Group Risk Policy, limits were set defining risk parameters.

There were up to 200 staff members who could serve on a credit committee. Credit committee meetings were held by relevant teams from within this coterie on a regular basis, almost every two days and sometimes daily, in order to review and assess new credit applications and amendments. These committee meetings were typically chaired by the Group Chief Risk Officer and member of the Board, or one of his deputies being the Risk Director responsible.

B3 Effectiveness of banks' funding, liquidity strategies and risk management

Funding strategy was determined by the Board. The implementation of the funding strategy was the responsibility of the Group Treasurer. The Group Treasurer role was amended in 2006 when three Directors of Treasury were appointed. Funding became the responsibility of two of those Directors, being the Director of Customer Funding and the Director of Capital Markets. The third Director of Treasury, was responsible for treasury trading activity and day-to-day operations with interbank parties. For a period in 2006 and 2007, I also had an oversight role in respect of treasury trading.

The Bank's funding model had a limited degree of geographic client diversity with main sources from within the Irish and UK markets. It also operated a reasonably well developed array of capital market instruments - money market instruments, commercial paper, repo facilities, medium term note programs and floating rate note programs amongst others. This diversity offered a significant degree of protection to the Bank throughout the early stages of the crisis in the third and fourth quarters of 2007 and up to September 2008.

Group Risk was a key function within the Bank. This department was responsible for assessing, monitoring and managing all risks across the entire Bank. This included a Treasury Risk Management Division that was independent of the operating business and set Treasury risk limits in accordance with Risk policy. This Division had expertise in interest rate and liquidity risk; compliance subject matter; treasury risk modelling and scenario testing and analysis.

(a) Appropriateness of funding sources, the mix, maturity profile and cost

The Bank, not being a retail bank with a wide branch network, did not naturally have a customer funding franchise linked to current accounts. Retail customers would, in general, choose 'by default' a universal bank for their daily banking requirements.

Similarly, companies would typically use universal banks, which offered cash management facilities for clearing and payment facilities for their everyday banking requirements. Another point of note, is that the direct cost of such deposit balances was nominal for the universal banks. Anglo Irish Bank did not have this option with only six regional offices in Ireland for example where some universal players had well in excess of 100.

Without the costs associated with a branch network or clearing infrastructure, the Bank did have a lower cost-to-income ratio that enabled it to offer customers more attractive deposit rates than typically provided by universal players. Client monies were often term deposits of between one week and two years. Treasury and Group Risk Management experience was that these deposits typically remained with the Bank following expiration of the initial contract.

The same approach was adopted for corporate and institutional depositors. However, by nature, these deposits were more price sensitive and could be switched for very small differentials in interest rates. Five basis points, or just five one hundredths of 1%, might have been enough to win or lose such deposits as they matured. The Bank sought sectoral diversification by targeting retail, corporate and institutional customers and also depositors in Ireland, the UK, the Isle of Man. It also targeted, to a limited extent, North America.

The other main source of funding for the Bank, over and above retained earnings and equity capital raised from investors, was international capital markets. Bonds or other funding instruments were issued in centres such as the UK, mainland Europe, North America and Asia. Funds were also raised against pools of loans, thereby providing access to secured funding markets through instruments such as covered bonds. These provided fixed term funding from very deep pools of liquidity in international markets.

Looking back to funding markets post the introduction of the Euro and the greater financial integration that ensued, the availability of money and the different sources available in capital markets was unprecedented. The ample supply of money made it relatively easy for banks to access funding. This is undoubtedly one of the core factors which set the environment for the root of the crisis experienced across Europe. Its impact should not be underestimated.

Some banks relied on a narrow range of sources only, derived primarily from capital markets. These banks were most quickly impacted by the crisis. Several examples resulted in the first bank runs in modern times arising in neighbouring countries. Debt capital market funding providers gained a very small net margin for funds in this heretofore highly liquid market. When markets abruptly froze they were amongst the first to recognise the dramatic change at the onset of the financial crisis and began to pull liquidity from counter-parties. This terminally damaged several banks and related financial institutions.

Throughout the financial crisis the Bank's funding was negatively impacted but never more so than late in the third quarter of 2008. There was a much greater emphasis placed upon share price movements and the potential read-across to risk. The VIX index, or the *fear index* as it became commonly known, sought to measure volatility of S&P 500 index options and share price movements in the forthcoming 30 days. It gyrated wildly. Additionally, considerable attention was given to Credit Default Swaps or CDS spreads. Previously a little followed index, except by professional investors, it measured the cost an investor would have to pay to insure a bond against default. The interplay between share prices and CDS spreads became markedly apparent.

However, given the range of markets the Bank had developed, it was able to maintain funding access at most points up to the collapse of Lehman Brothers. The terms available, like for most institutions, became shorter and shorter and hence the liquidity issue, and its day-to-day management, became more acute. Liquidity may be explained as the other factors, outside of the absolute quantum of funding, that define the quality of the money raised. For example, consider Euro 10 million raised overnight and the same amount raised for a five year term. The amount of funding is the same but the liquidity benefit of the five year term money is significantly greater.

During a period of a changing liquidity environment the Bank, like every other Irish bank, was far too small to control its destiny in this area. The "Market" set the mix, maturity profile and cost.

From 15 September 2008 onwards, it was very difficult to raise any funding in the markets. What was available was of very short duration. Many depositors withdrew funds from the Irish banks and capital markets were totally dislocated. This occurred after already going through 13 months of intensely severe funding conditions.

(b) Analysis of liquidity risk under adverse scenarios

Group Risk Management were responsible for stress testing and performing analysis of liquidity under adverse scenarios.

(c) Interest rate risk appetite setting and monitoring

Recognising this long before the onset of the crisis the Bank's policy was relatively conservative in that it sought to hedge most interest rate risk arising. It thereby reduced the cost, or benefit, associated with fluctuations in interest rates.

Lending arrangements were typically structured at a set margin differential, say 2 percent, over and above market benchmarks. Hence, if interest rates went up, commercial borrowers assumed the market risk as gross lending rates increased in line with such market movements. Where a borrower had a fixed rate loan the interest rate risk would typically be offset, by putting in place a risk management derivative, like an interest rate swap.

On the liability side of the balance sheet, the Bank strategy was to pay close to market rates. Hence, if market rates were say 3 percent, deposit products often offered a similar rate. This policy was feasible given Bank's very low cost-to-income.

At the onset of the liquidity crisis, a huge divergence developed between central bank interest rates and market rates. Deposit and funding rates in general increased significantly so the cost of funding increased as access eroded. The Bank was also exposed to the fact that certain lending clients struggled to cope with the increased funding costs, legitimately passed on to them, whilst the economy nose-dived and the income from their businesses began to suffer in an extreme fashion.

(e) Capital structure and loss absorption capacity

Capital policy was set by the Bank's board. Capital adequacy was monitored and assessed by Group Risk. Loans were classified based on risk categories. Group finance collated the information from the banking system as adjusted by Group Risk and classified the data in accordance with regulatory requirements for onward submission to the regulator.

At end September 2008, the Bank had customer loans of some Euro 74.1 billion, risk weighted assets of Euro 85.8 billion against a capital base of approximately Euro 10.3 billion.

The Bank's capital requirements were calculated in line with the Basel II standardised approach. Regulatory requirements stipulated the Bank to hold Core Tier 1 capital, being the amount of capital versus risk weighted assets (primarily loans in the case of the Bank), of 4%. The Bank's actual ratio was nearly 50% in excess of the required regulatory level at 5.9%. Its total Tier 1 capital ratio stood at 8.4% and total capital base at 12% of risk weighted assets, also well in excess of regulatory limits.

The Bank also held *Incurred But Not Reported* provisions (referred to as IBNR or collective provisions). These provisions had the highest possible loss absorption characteristics, in effect a collective provision which could be used against losses identified in the future. Combined with equity capital this resulted in a proforma Tier 1 capital level which was one of the highest in the sector.

In early 2008, the Regulator introduced new capital requirements, which warranted higher capital requirements in respect of development lending. The capital ratios already in place were sufficient to comply with the more onerous regulatory capital requirements.

The leadership within the Lending divisions reviewed loans on a regular basis in each geographical market, typically between two and four times per annum. Group Risk also carried out independent reviews of existing loans. These reviews assessed the likelihood of loan loss, the actions required to deal with changing circumstances and ultimately mitigating risk. The role of Group Risk was to evaluate actual losses and ‘work out cases’, as well as future potential economic losses. International Financial Reporting Standards and Irish law, did not permit financial reporting to account for any potential economic losses. This is now recognised as a significant weakness of financial reporting requirements extant in 2008.

In late 2008, a more detailed and intense review was undertaken by lending divisions and Group Risk, reflecting the worsening economic conditions. Allowing for a more stressed environment, this identified potential future losses over the following three years to end 2011, from recollection, of up to Euro 2 billion.

Also, at the request of the Group Board of Directors, a second review was independently undertaken by a team of Non-Executive Directors of the Board. I believe this again looked at future potential losses over the three year period 2009 to 2011. The highest estimate of future potential losses, again from my recollection without having access to Bank files, was in the range of some Euro 2.3 to Euro 2.8 billion.

Against total capital resources of Euro10 billion, this implied that Group Risk and the Board of the Bank, including non-executive directors, believed that as of late 2008, the Bank had sufficient capital for a range of potential losses based on future economic forecasting. The interim accounts issued in May 2009 following the nationalisation of the Bank, showed that the Bank would have sufficient capital for to absorb estimated current and future losses.

B4 Impact of property valuation methodologies on banks' credit risk management

(a) Adequacy of the valuation policies and assumptions to accurately assess loan security

I have very limited information to give on this issue. As I recall, Group Risk developed lending policy, which included valuation policies, and limits on loan to value levels permitted for lending. These were in turn subject to assessment by the Board Risk and Compliance Committee.

In addition to Group Risk evaluation, the Bank also had a practice of having valuations undertaken by independent valuers who formed part of the Bank's chosen valuation panel. The panel comprised of valuers with relevant experience and expertise covering the geography and sector of the relevant asset.

B6 Impact of banks' internal audit processes in supporting effective risk management

(a) Effectiveness of internal audit oversight and communication of issues related to governance, property-related lending strategies and risks, and funding and liquidity risks.

(b) Effectiveness of the oversight of the prevailing risk culture

As explained above, Group Internal Audit was an independent function, separate to finance. It reported directly to the Chief Executive and separately to the Audit Committee. Their function was to test the operational risks and controls in the Bank and report to the audit committee with recommendations for improvement.

The effectiveness of the oversight of the prevailing risk culture was the responsibility of Internal Audit, the Audit Committee, the Board Risk and Compliance Committee, Group Risk and the Board.

B7 Impact of banks' external audit processes in supporting effective risk management

(a) Impact of prevailing accounting standards in recognising risks

There has been much debate about the impact that compliance with accounting standards had on the onset of the financial crisis. Excerpts from a UK parliamentary committee on the topic includes the following:

"Accounting standards were not at first within our intended scope for this inquiry. But we included them after witnesses made trenchant criticisms of the effects on audit of the International Financial Reporting Standards (IFRS) adopted in recent years in the EU and the UK."

Mr Timothy Bush, Investment Management Association nominated representative on the Urgent Issues Task Force of the Accounting Standards Board, argued that the relevant IFR standard, IAS39, is in conflict with clause 19 of UK accounting rules under the Companies Act 2006 which requires accounts to be prepared prudently, and without crediting any unrealised profits, while recognising any contingent liabilities. (NB - the relevant Irish provisions are similar.)

...Mr Bush went so far as to describe the bank crash in the UK and Ireland as "a crisis largely caused by accounting."

In respect of the Bank, the most important impact was in relation to loan loss provisions. The Bank had historically followed what was regarded until 2005 as a relatively prudent approach of charging a 1% general provision on all new lending. This has the effect of building a provision to absorb future losses. However, this was not permitted following the introduction of IFRS. General provisions, for future losses not yet incurred, were strictly prohibited.

(b) Effectiveness of the external audit processes to identify and report to the board and management, any concerns related to significant risk exposures, including property, funding and liquidity

Auditors were appointed by the shareholders almost invariably on the advice of the Board of Directors. Their statutory role was to report to the shareholders. Group Finance in Ireland coordinated the day-to-day interaction with auditors for the Irish and North America operations, a functional responsibility of the Head of Group Finance within the department. Responsibility for the UK was separately managed by the Bank's UK finance function.

Auditors had full, unfettered access to all management and functions of the Bank including all Executive and Non-Executive Directors. They spent a significant amount of their audit work engaging directly with Lending, Treasury and Wealth Management staff. In addition, they worked directly with Group Risk in order to identify, discuss and assess all risks.

Regular update meetings were held with senior members of the external audit team. The external auditors attended certain meetings of the Board Audit Committee. In addition, they were invited to private sessions with the Board Audit Committee in order to discuss sensitive matters where no executive directors were permitted to attend.

The auditors initiated a "higher risk" audit of the Bank in 2008. This high-risk approach was presented as a direct result of the market conditions and the potential impact on the Bank rather than specifics to do with the Bank itself. This process meant increased audit procedures for the year ended 30 September 2008, involving significantly more detailed audit testing and analysis. It also led to more active involvement by the concurring or second reviewing audit partner and significant involvement and review of audit work and areas of judgement by the auditor's local and international risk functions.

At the time, whilst economic conditions appeared to be more difficult than at the end of September, neither the Audit Committee nor other functions appeared to communicate any sense of any long-term risk to the Bank. The introduction of the bank guarantee had a material positive impact on the funding and liquidity position of Irish banks, as well as providing significant going concern risk comfort to all stakeholders. The work carried out by Group Risk, together with the independent future loan loss assessment undertaken by the independent group of non-executive directors showed, at this point in time, that the Bank had sufficient capital to survive the economic downturn as they had assessed it. Furthermore, whilst many banks in Europe and the United States were making huge write downs for subprime and other highly structured assets, the Bank's exposure in this area was relatively small. Hence large impairment charges for treasury assets were not arising at this time.

C2 Role and effectiveness of the policy appraisal regime before and during the crisis

(c) The liquidity versus solvency debate

Liquidity progressively became the daily focus of the Bank from August 2007. Month by month this focus became more and more intense with the event labelled as the St. Patrick's Day massacre marking a new level.

Certain characteristics heightened the risk perceived by the market: size of a bank with smaller entities seen as less systemically important and therefore less likely to be supported by the state; banks relying on wholesale funding; those with narrow operating margins; non-clearing banks which didn't provide current accounts; those below double AA rating; less diversified entities; and banks with high exposure to subprime or highly structured assets, to mentioned but some of the key factors.

I referred earlier to the rumours of losses arising in the market and the impact of volatile share prices and CDS spreads.

Two other factors are noteworthy. Legislation introduced in Europe and Ireland pertaining to covered bonds, allowed mortgage lenders to provide their mortgage loans in massive blocks to the European Central Bank (ECB). In turn the ECB would provide immediate funding. Picture two banks, both with Euro 100 billion in assets. One is a mortgage lender with 75% of assets being residential house loans, the other a business lender with no house lending. The first bank could convert a significant portion of mortgage lending back into cash by providing them as collateral to the

ECB. This was a huge advantage enjoyed by mortgage players, which the Bank did not enjoy.

Finally, according to market players, the Bank's position was complicated by the rumours of Sean Quinn's economic interest. This manifested itself in two ways. Some market participants believed that Quinn was under financial pressure. If true, they could seek to exploit his weakness by driving the Bank’s share price lower. Through selling short the shares, it placed immediate downward pressure on the price which caused other investors to sell, further weakening prices creating a negative spiral. The secondary, and critical knock on effect was on funding. With the volatility in the Bank’s share price certain funders were less willing to provide the same quantum or duration of deposits.

Accordingly, the focus of management was on liquidity. Liquidity hit first as a risk whilst solvency became a serious issue on a more gradual basis thereafter. This is due in no small part because the economy and businesses therein suffered with the general lack of liquidity.

As well as the reviews referred to above, several outside advisors were mandated by State bodies, including IFSRA and the Department of Finance to undertake exercises relating to bank liquidity and solvency. These exercises were designed to provide an independent view on the solvency of Irish banks. Whilst the assumptions adopted were more severe than those used internally, the outcome of work undertaken indicated the Bank's ability to withstand anticipated material losses, based on the criteria set by the independent reviewers, over the following 12-24 months and beyond.

The decision by the Government to recapitalise the Bank by Euro 1.5 billion in State underwritten preference shares due to be voted on at the Bank's special EGM called in January 2009, serves to highlight the perception of solvency risk by the Board and other stakeholders as relatively low at this point. The amount represented just 15% of total capital but it had a significant signalling effect to the market that the state was behind the Bank.

However, in the relatively short period up to the release of interim accounts in May 2009, the situation of the economy had worsened to such an extent, that the State decided to proceed with a significantly larger recapitalisation to help stabilise the Bank. Total losses as announced by the new government appointed board, taking at what the time was perceived as a very prudent approach, amounted to some Euro 4 billion.

C3 Appropriateness and effectiveness of the Department of Finance actions during the crisis

(b) The appropriateness of the bank guarantee decision

The difficulties faced by those involved in making this decision were formidable. I first learned of the guarantee after it had been announced on national radio and have no knowledge of the specific background to the guarantee decision. It had a hugely positive, stabilising impact in the market for Irish banks.

C4 Appropriateness and effectiveness of the domestic policy responses

(c) Decision to recapitalise Anglo, Allied Irish Bank (AIB), Bank of Ireland (BoI), Education Building Society (EBS), Permanent TSB (PTSB) and the alternatives available and/or considered

The decision to recapitalise Irish banks was announced by the government on the 21st of December 2008. Given the short period that had elapsed since the introduction of the government deposits guarantee at the end of September, it served to highlight how significantly and rapidly the deterioration had occurred in Ireland's economic outlook.

It was clear from equity markets that investors needed to see concrete action from the State in order to demonstrate that banks would be supported through the economic cycle. However, the size and nature of capital offered, together with the timing of actual capitalisation, limited the benefit impact desired.

R1 Effectiveness of the regulatory, supervisory and governmental regime structure

(a) Appropriateness of the regulatory regime

(b) Effectiveness and appropriateness of the supervision policy and powers

The role of group finance in relation to these bodies was primarily to collate financial information for the purposes of making financial and regulatory returns. Any other interaction was limited.

The information requested by the Irish regulator was broadly similar to that requested elsewhere in the Group.

Everybody involved in the crisis struggled to deal with unprecedented situations. It was my perception that the authorities worked strenuously to attempt to manage the never ending series of complex issues arising.

R3 Clarity and effectiveness of the nexus of institutional roles and relationships

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

As stated above, the role of Group Finance in relation to these bodies was primarily to collate financial information for the purposes of making financial and regulatory returns. Any other interaction was limited.

From 2009, the authorities dealt almost exclusively with the government appointed board which comprised a mix of deep professional and political experience. I believe this was invaluable to both the Bank and the various authorities.

Dated this Thursday the 6th day of August, 2015

Matthew E. Moran

Appendix 1 - Governance Structure

The Bank was a listed, regulated entity with multiple subsidiaries and associated operations in Ireland, the UK, mainland Europe and North America.

A summary of the core governance structure of the Bank is depicted below.

		Governance Structure		
Board		Chairman of the Board		
Board		Board of Directors		
		12-14 Directors, majority of whom were Non-Executive Directors		
Board Committees	Board Risk & Compliance Committee	Board Audit Committee	Board Succession & Nomination Committee	Board Remuneration Committee

		Board Executive Committee		
Board		Group Chief Executive		
Other Members	Executive Director of Lending, Ireland	Chief Executive, UK	Chief Executive, North America	Group Finance Director & Group Chief Risk Officer

The Bank had a Statutory Board of Directors led by the Chairman, comprising a majority of non-executive Directors. Four Board Committees, with set responsibilities outlined in the Bank's Annual Report and Accounts, reported directly to the Board. These were made up mainly of non-executive directors and included the Board Risk and Compliance Committee and the Board Audit Committee.

The Group Chief Executive was the most senior Executive Director. Below him were the executive directors which included the Executive Director of Lending in Ireland and the Chief Executive of the UK responsible for lending and overall management of UK activities. The roles of Group Finance Director and Group Chief Risk Officer were consolidated into one in 2008. The Chief Executive of North America, whilst not a statutory director, also attended the Board. These people made up the Executive Committee of the Bank and all operations in all geographies fell under their responsibility.

Below these, there was a group of 30 to 40 functional heads (normally given the title of director or associate director) who were responsible for the day-to-day operational management of various functions or sub-departments in the Bank. I was one such function director in 2008 with responsibility for the Bank's Dublin based group finance team.

Operating Structure of the Bank

The Bank was a niche player focused on business lending and comprising three core business activities which may be summarised as follows:

1. Raising money - which was undertaken by Treasury
2. Managing money once it had been gathered - again, this fell within the remit of Treasury where deposits and other funding raised was looked after on receipt prior to it being lent to customers
3. Lending money - providing loans to the Bank's customers typically for the purchase of assets and also for their development

A simplified overview of the Bank's operating structure, core support functions, and finance governance structure are shown below.

		Business Operating Structure	
Core Business Divisions	**Lending**	**Treasury**	**Wealth Management**
Locations	Ireland, UK & North America	Ireland, UK, North America, Isle of Man, Austria & Geneva	Ireland, UK, Isle of Man, Austria & Geneva

	Support Functions Overview	
	Group Risk Management	
	Group Human Resources	
	Group Finance	
	Group Legal & Compliance	
	Company Secretarial Department	
	Group Internal Audit	
	UK Finance & Operations	
	Other regional support functions	

			Finance Function Overview		
			Group Finance Director		
	Group Finance Dublin	UK Finance	Finance Isle of Man	Finance Austria	Finance Geneva
Areas of responsibility	Ireland & North America	UK including Northern Ireland	Isle of Man	Austria	Geneva

How the Bank functioned

The Bank raised money from a multitude of sources utilising a wider range of instruments with a variety of features and tenors. Several Treasury teams were in place in Ireland, throughout the UK, the Isle of Man, mainland Europe and North America.

Customer funding derived from retail customers, corporate customers, financial institutions and non-financial institutions across 16 countries in several currencies including, dollar, euro, sterling and Swiss franc to name a few.

Customer deposits included overnight deposits, fixed term deposits for between seven days and five years, guaranteed deposits, capital protected and non-capital protected structures, special feature structures amongst others depending on the market.

The Bank's Treasury Capital Market Division sourced funding from a wide range of markets in multiple currencies under special capital market programs including MTN's/EMTN's, FRN's, repo's using secured and unsecured instruments across the spectrum of tenors available. It also sourced funding and capital through special regulatory compliant structures. These included subordinated and deeply subordinated bonds with special call features and tenors either qualifying either as Tier 1, Tier 2 or Total Capital regulatory capital.

From the mid 2000's onwards, the Bank further diversified funding by accessing the asset backed market through securitising loans or creating covered bonds. These developments proved essential through the latter stages of the crisis as funding availability - when available - was often restricted to secured market instruments.

When money was deposited with the Bank, another division of Treasury, Treasury Trading, was responsible for its day-to-day management. The money attracted a cost immediately, so a specialist team placed it back out in the market in order to generate a return and manage the Bank's cost of funding risk. The return would depend on where it was lent, the currency used, the rating of the counterparty and the period for which it was provided. This area also considered anticipated lending activity in order to ensure sufficient funding was available for customer demand in the coming period.

Customer loans were provided by the Lending Divisions. There were three key divisions that lent money split based on geographical focus - Ireland, the UK and North America. Lenders were responsible for managing relationships directly with their clients. The policy of the Bank was generally to undertake secured lending rather that unsecured lending for the majority of its loans. This should then result in cash flow from the client's activity for the servicing of the loan together with an asset as additional security. In the event that the loan went bad the asset could then be used to repay the loan or reduce the potential loss arising.

Security invariably was made up of real estate - commercial, residential, industrial or office buildings. Hence, the cash flow exposure of the loan may have been to a doctor's surgery, retail shops, or office rent from a company. The building provided security.

Lending Operations captured loan arrangements and were responsible for recording them onto the Bank's core banking system. This specialist middle office function was there to ensure that the all transactions relating to loans were properly booked, including the booking of provisions under the assessment and direction of Group Risk.

The Bank also had a Wealth Management Division, run by one of the longstanding, senior lenders. This business comprised investment product to individuals and operated out of Ireland and the UK. Licensed banks, based in Austria and Geneva, also formed part of Treasury and Wealth Management activities.

Support Functions of the Bank

Surrounding these business divisions, were several support functions. These included: Group Risk, Group Finance, Group Legal and Compliance, Group Internal Audit and sometimes similar functions in other geographies.

Unlike in many other industries, banks have dedicated risk departments as the cornerstone of the business is the proper pricing of risk.

Reflecting its importance status, the Group Risk Department at Anglo Irish Bank was a centralised function responsible for assessment of and management of all risks no matter where assumed. Each of the Directors of Risk responsible for lending in Ireland, the UK and North America, together with Treasury Risk Management, reported to the Group Chief Risk Officer, always a main Board Director.

Group Risk was responsible for implementing the day-to-day risk management policies set by the Board Risk Management and Compliance Committee as approved by the Board.

The Head of the Risk Department, or one of his Directors, was responsible for chairing the Bank's credit committee which approved loans made by the Bank in any region, Ireland, the UK or North America.

Credit Committee was a regular meeting, held on a near daily basis. It had worked successfully for decades and was also seen as a training ground for lenders. It was described as the *heart of the bank*. All lenders were eligible to participate at credit committee as were most senior manager grade staff and up across the entire Group. It was led by Group Risk. Between those in attendance in person and others who dialled in by video conference, some 30 to 60 people would attend each committee out of some 200 potential participants.