

**IN THE MATTER OF A REPORT TO THE OVERSIGHT COMMITTEE
OF THE BANK OF ENGLAND**

SUPPLEMENTARY OPINION

- 1** The Bank of England in its public testimony on 3rd March 2015 has taken the position that the review process which culminated in Lord Grabiner’s November 2014 report was “*thorough and comprehensive*”. In that context, I am instructed to advise Jesse Norman MP as one of the Select Committee’s members on legal matters relevant to that issue. In particular Mr Norman wishes to know what differences there are between the two types of question which I referred to in my Opinion of 2nd March.
- 2** My Opinion of 2nd March set out and explained the narrow focus of the Bank’s terms of reference for the review process. (1) The terms of reference were subjective and required investigation only of whether Bank officials actually knew¹ of market manipulation or other similar matters². (2) This standard of scrutiny was significantly narrower than the standard legal test applied for professional misconduct in other areas of public interest, i.e. was there serious negligence measured by objective professional standards.³
- 3** Based on the narrow subjective focus of the terms of reference, I concluded that Lord Grabiner’s report met the general legal tests for a legally valid report into the questions asked. English law has a well understood set of rules (i.e. the law of judicial review) governing when courts can intervene in public functions, including a report of the kind here. The scope for intervention is limited because the role of the courts is only to provide a backstop. Provided the investigator has correctly interpreted the questions he has been asked, has followed due process, and not reached a result which is perverse on the evidence, the exercise conducted will not be judicially reviewable.
- 4** If comparing an enquiry into the question “Has there been serious professional misconduct in not taking steps to uncover problems?” with the question “Did employees actually appreciate there were problems?”, then there are numerous differences of principle and practice between the two types of investigation. Many recent examples of investigations clearly draw the distinction, but embrace both questions. A report aimed at the first type of question will typically be able to consider many other factors.
- 5** *First*, there is a basic difference between asking “Should someone have known something?” and “Did someone actually know something?” The Bank’s terms of reference asked not only about awareness of actual manipulation of the market but also

¹ Knowledge includes both actual involvement (which necessarily presupposes awareness) and deliberately turning a blind eye (which is generally accepted as equivalent to actual knowledge).

² Including knowledge of activities which created the potential for manipulation.

³ Para 7 of my 2nd March Opinion.

about awareness of activities which created the potential for manipulation. This, of course, is an enquiry which still involves considering whether somebody actually knew facts and actually appreciated their significance. It is therefore different from an enquiry into whether somebody ought to have appreciated certain facts and their significance. Serious professional misconduct is a concept which covers both types of question.

- 6 *Second*, it is typically much harder to reach findings about whether a fact *was actually* known, especially if knowledge of it required an appreciation of malpractice, than it is to reach a finding on whether a problem *should have been* appreciated. This difficulty is a major reason why modern professional conduct regimes take the broader, objective, approach. It goes to the heart of Lord Hoffmann’s distinction in the *McCandless* case between “*genial incompetence*” and “*deliberate wrongdoing*”. The problems of establishing actual knowledge are even greater in a large corporate context where responsibilities are inevitably distributed between many people. Only individuals, not institutions, can know things.⁴
- 7 *Third*, it is not unknown for major institutions to get caught up in some way in wrongdoing by others and to launch investigations into their role in what went on. Many well-known investigations have been based on terms of reference which explicitly acknowledged the distinction between actual knowledge and objective failures, and asked the investigator to consider both:⁵

7.1 Lord Justice Bingham’s enquiry reporting in 1992 was given the overall task of enquiring into the Bank’s role of supervising BCCI⁶. Extrapolating from that overall task, the report defined its remit as including “(1) *What did the UK authorities know...? (2) Should they have known more? (3) What action did the UK authorities take...? (4) Should they have acted differently?*” Notably in Chapter 2, Section 14 the Bingham report considered two instances where third parties had presented information alleging fraud at BCCI. The report found that the Bank did not suspect fraud but still criticised the Bank for, in effect, a seriously negligent omission in not taking further action in response.

7.2 Dame Janet Smith’s current enquiry into the BBC will include “2. *investigate the extent to which BBC personnel were or ought to have been aware of inappropriate sexual conduct by Jimmy Savile in connection with his work with the BBC, and consider whether the culture and practices within the BBC during the years of Jimmy Savile’s employment enabled inappropriate sexual conduct to continue unchecked”.*

⁴ The Bank’s terms of reference for Lord Gribner referred to “*whether any Bank official... was... aware*”.

⁵ Emphasis added in each case.

⁶ Under specific supervisory duties in banking legislation.

7.3 Lord Justice Leveson’s inquiry included “3. *To inquire into the extent of unlawful or improper conduct within... newspaper organisations... within the media...* 6. *To inquire into the extent of corporate governance and management failures at... newspaper organisations...*”

- 8** *Fourth*, the broader question naturally directs attention to possible institutional failings such as a culture of complacency or deference; low standards; low status of a particular department; social and cultural ties between the personnel of the institution concerned and participants in the relevant market; and incentives (such as pay structure or typical career advancement paths) to co-operate in rather than criticise the existing system. Consistently with that approach, the Smith enquiry at the BBC will include consideration of “*the culture and practices within the [the institution]*”.
- 9** Broader topics which might have been addressed on the facts of this case include: (1) What did the Bank know about the FX market? (2) What should it have known? (3) Were any individuals (Mr Mallett or others) to be criticised for not having appreciated facts or risks which they ought to have appreciated, and/or for not having taken steps they ought to have taken? (4) To what extent was it reasonable to expect senior management to take some interest in the functioning of the FX market? If so, what evidence was there of senior management seeking to explore potential risks within the market?⁷ (5) Generally, why did the Bank not know about or suspect the widespread, perhaps endemic, malpractice in the FX market?
- 10** One specific issue which has been considered in the public testimony relating to this investigation concerns the trader conversation of October 2011. As a result, the Treasury Select Committee may wish to consider whether the review process has adequately addressed the question whether the Bank *should have* taken action in response to the trader conversation of October 2011.
- 11** Lord Grabiner’s report at §§57-58 concluded that the trader conversation did not leave Mr Mallett with an actual understanding of any problem. It follows that within the terms of reference for Lord Grabiner’s report, Mr Mallett cannot be criticised for failure to escalate a problem which he did not in fact appreciate. But it is a separate question whether or not a conclusion of that kind is enough for a “*thorough and comprehensive*” enquiry.
- 12** Lord Grabiner’s 28 January letter explains his view that it “*is unclear whether the trader was complaining about conduct which was unlawful and improper, or was only complaining about heavy speculative trading*”⁸. As I read this finding (and as I read the conversation), on an objective interpretation of what was said, the trader could either have

⁷ Lord Grabiner cites one email in which a senior manager asked for a list of “what keeps us awake at night”, although it appears this was sent in the context of a talk to an external organisation rather than as part of e.g. some internal analysis.

⁸ Letter to the TSC of 28 January 2015 further explaining the report’s finding on that conversation.

attempting to blow the whistle or merely making a generalised complaint about market behaviour of a lawful if unwelcome kind.⁹

- 13** If the enquiry had had terms of reference such as the examples referred to in §7 above, it would have been possible, and probably necessary, to consider and report expressly on: (i) whether someone in Mr Mallett’s position acting reasonably, and with the views which he then had about the market generally¹⁰, would have taken the conversation further, precisely because it was ambiguous and open to the interpretation that it was an attempt to blow the whistle; (ii) whether officials senior to Mr Mallett had taken adequate steps to ensure that any knowledge of potential FX market malpractice was escalated within the Bank, something which Lord Grabiner found at §77(a) of his report was a matter of judgment.
- 14** The question whether or not it would have been reasonable for Mr Mallett to take any further steps in the light of the trader conversation is one which was raised in the public session on 21 January 2015 with Lord Grabiner. Lord Grabiner’s letter of 28 January in response to that session stated that he wished to explain the reasoning behind his report in further detail, i.e. his reasons in November 2014. He added at the end that he had listened to the trader conversation and it had not caused him to change his views.¹¹ Lord Grabiner did not say in the letter that since the session with the Treasury Select Committee on 21 January, he had reached a conclusion on the question of what would have been reasonable for Mr Mallett to do.¹²

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⁹ If it had clearly been no more than a conversation about lawful practices, then it would have been odd for Mr Mallett at the end to ask the trader to get back to him “*if you hear more of this*”.

¹⁰ I.e. that traders were engaging in conduct which would be difficult to justify to the regulator. See §18 of my 2nd March Opinion.

¹¹ NB I can see no need for Lord Grabiner to have listened to the conversation when conducting his enquiry, and that point was not mentioned in my 2nd March Opinion. Others in the legal team would have done so in order to check there was nothing exceptional that had not come out on the transcript; and to try to draw any conclusions from the tone or manner used by listening to only one conversation, or even a number, out of hundreds or even thousands of hours of recordings could be dangerous.

¹² As with any other member of the public, my understanding of the extent, outcome and reconsideration of any review process is based on what the Bank publishes, and my assumption is that anything which might add materially to what has already been published will itself be made public.