Swap Hidden Credit & Regulatory failure!

The Largest Financial Fraud in Recent History!

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BankConfidential

TTF Event – 1st April 2021

Q. What were Swaps?
A. PPI For SME's…

- Sold as an 'insurance'
- Costs of circa 25-30% additional to the loan cost
- High Street Banks would collect this along with your loan costs over the term
- The 'protection' was not intended to pay out
- Huge balance sheet benefits for the banks
- A sales Scam but far more dangerous than PPI…

What is an Over the Counter (OTC) interest Rate Swap?

A Swap is NOT

- A loan product
- A protection against interest rate risk on commercial loans
- A flexible or ‘no premium’ product with unknown risks

An OTC Swap is

- An **investment contract** with gains or losses based on a ‘gamble’ over future interest rates (Base, Bank Base or LIBOR)
- A **‘BESPOKE’ contract** sold by most high street banks mainly 2-3 years prior to & several years after the Credit Crunch to tens of thousands of SME’s & Corporate Businesses
- Where you are advised to **Swap variable rates for a fixed rate** by a banking ‘expert’ who will later say they didn’t advise you
- To exit in theory there will be a potential gain or penalty depending on forecasts for future interest rates (**break gains or costs**)
- A high risk multi currency, cross border deal traded be by **Professional Investors & Counterparty’s** under **ISDA** (International Swaps & Derivatives Association) Rules

Over the Counter Swap – A Bilateral Contract

Party A

The Bank

Party B

The Customer

Resources to Forecast Interest Rates
Economists
Global investment Experts
Derivative Traders
Bloomberg Systems
LIBOR Panel setting interest rates
Access to Bank of England

Resources to Forecast Interest Rates

- The Bank's Treasury expert

Bank Gains = Your Losses

- Every £1 you lose on a trade is £1 profit for the Bank
- A bespoke deal that cannot be sold in any market
- Whilst banking ‘experts’ stated that rates going up was a real risk, their internal systems and analysts forecast the opposite
- The parties involved would calculate your expected your losses (their gains) before selling a Swap, the higher your losses = the higher their gains and commissions
- The bank manager would apply for and get approval for an **‘undisclosed’ or ‘hidden’ credit** facility covering your expected losses (Margin Credit)
- This hardcore liability would be secured against your Assets without your knowledge

Why enter **a Heads I Win Tails you lose** Bet against a bank?

Why bet against a Bank & their experts on Interest Rates at all?

Why You Will Lose

- From late 2007 on Swap trades were sold at rates where the customer had large expected losses
- The banks sold the higher fixed rate because the interest rates were forecast to decrease
- The banks set LIBOR rates and their own Bank Base rate
- The Bank of England protects the City & they control Base rate

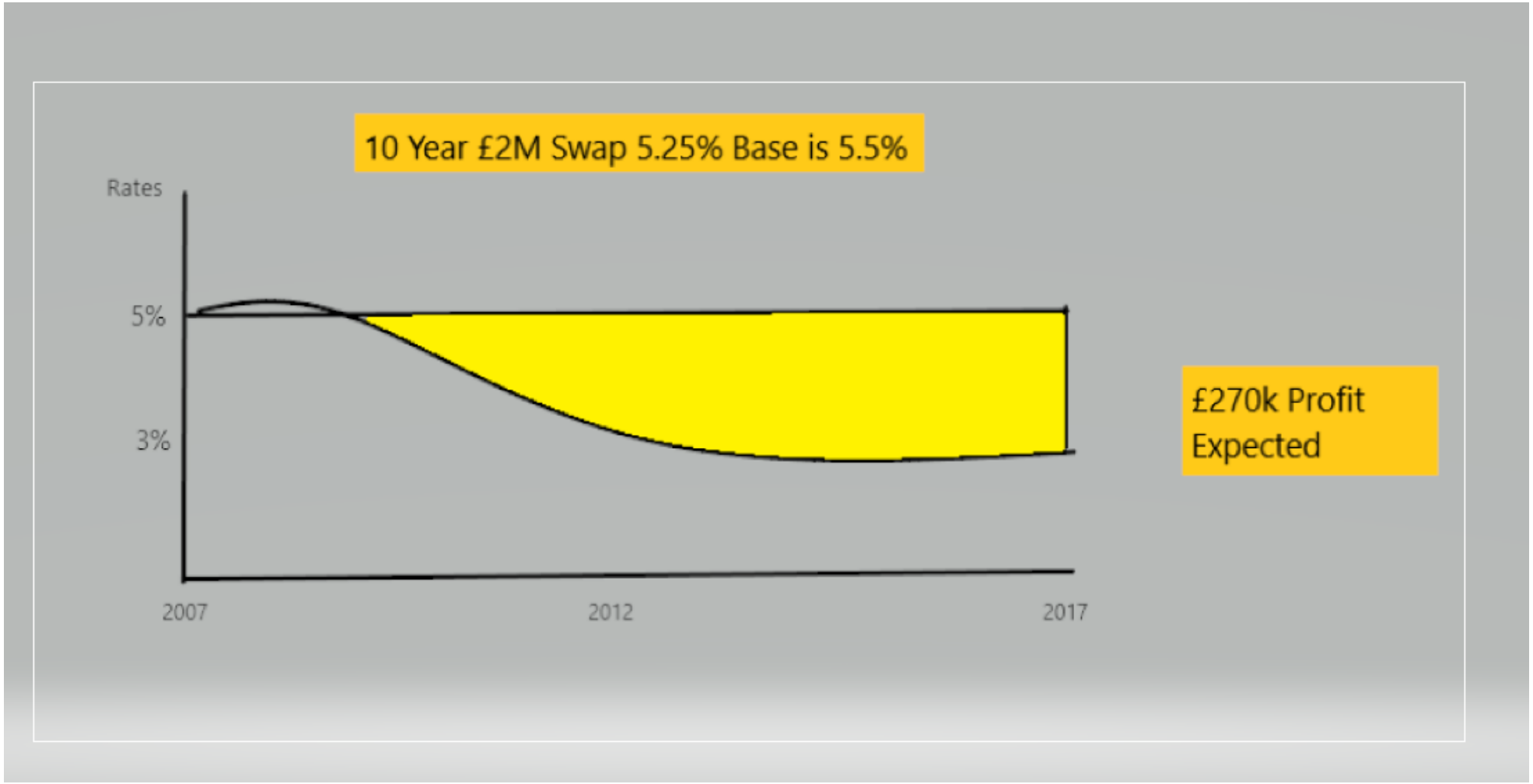
But What if rates had gone up?

Then the bank could rely on vague clauses in the Swap & Loan contracts to close out the deal

YOU COULD NOT WIN!

Expected Customer Losses (and Bank Gains)

Example of a **NatWest** £2M 10 year trade of late 2007.
Gains/losses are classed as a **Contingent Liability**



What the Trader & Bank Manager knew but failed to disclose to you

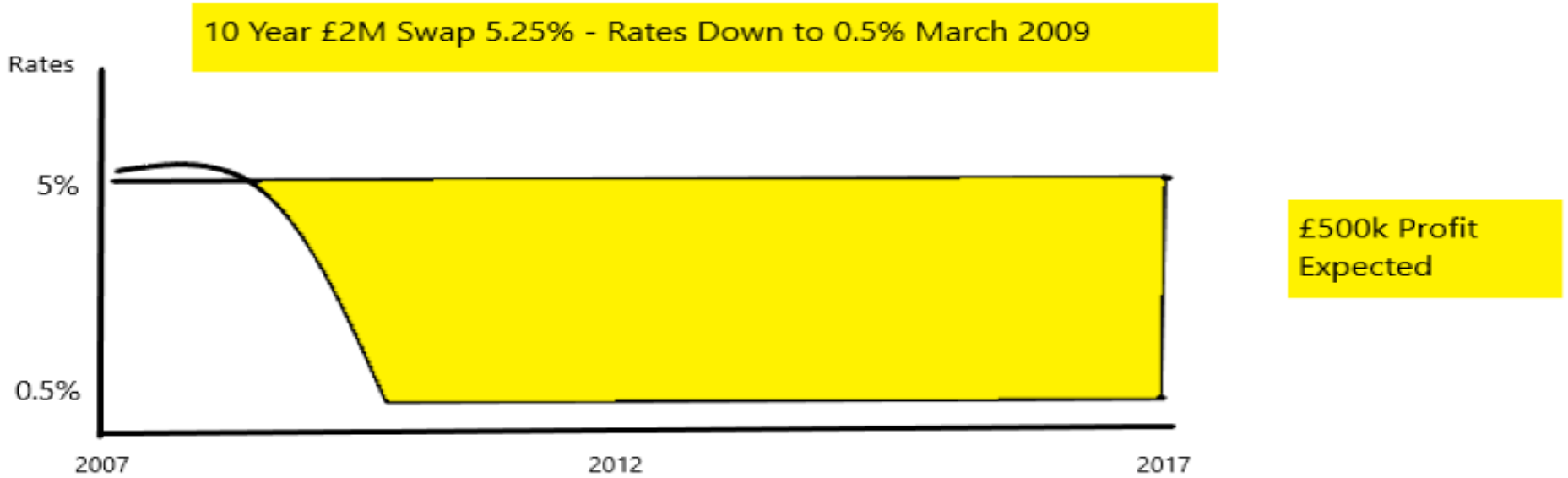
Page 2 of a NatWest Trade confirmation (withheld from client) confirms Contingent Liability & Commission (AV).

This trade led to an undisclosed £300k Credit Line risk on the day of the Trade & £47k commission

Structure	See Attached
Additional information	You have a Base rate Geared Collar. Your interest rate is capped at 6.00% and has a floor at 5.00%. If 3 month average Base rate remains within 5.00% and 6.00% you would pay the prevailing Base Rate. If 3 month average Base Rate is above 6.00% then Rbs will compensate you the difference to 6.00%. If 3 month average Base Rate falls below 5.00% you would pa one move above Base rate but capped at 6.00%. For example at 4.75% you would pay 5.25%, at 4.50% you would pay 5.50% at 4.25% you would pay 5.75% and at 4.00% you would pay 6.00%. If Base Rate is below 4.00% you would pay 6.00%
Client rate	6.00 cap 5.00 floor 4.00 lower floor
Credit reserve	122.00
Contingent liability	267000
Premium paid	0.00
AV	47000.0000

Expected Customer Losses (and Bank Gains)

The same **NatWest** £2M trade in 2010



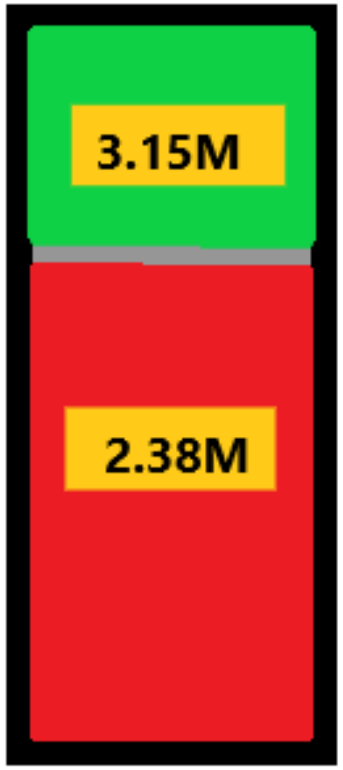
Swap Credit Lines – Contingent or Real?

Customers Bank Statements in 2010

PROPERTY VALUE

75% Loan to Value

DEBT



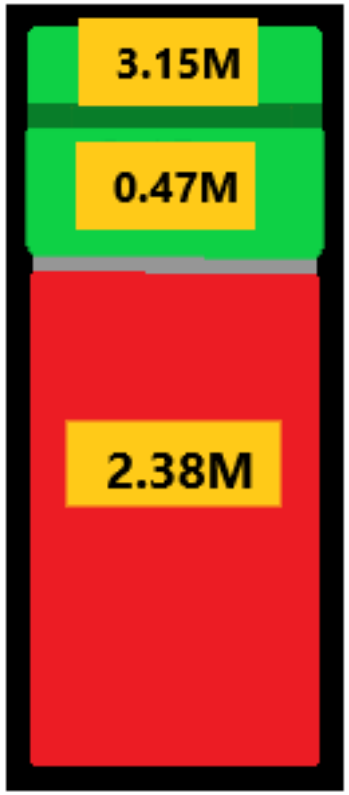
Bank's Credit System in 2010

PROPERTY VALUE

91% Loan to Value

SWAP Credit Line

DEBT



The Real Effects of Hard Core Credit lines…

NATWEST BANK MANAGER's EMAIL TO CUSTOMER WITH THE £2M 10 YEAR SWAP:

Date: 10 September 2010

good afternoon - hope all is well up there.

Assuming that this is the best that can be achieved, we will be looking at an emerging position of …

£3.150m total ascribed security values

£2.388m Loans

£0.477m Hedging liability

£2.865m debt = LTV 91%

…am I missing something here ?

…the position has been skewed considerably and my concern is that **at this level of gearing**, **the bank will want to pass on control to GRG…**

Details of facilities under review on this application

Ref	Facility Type	BS / Risk Holder	Decision	Reason	Limit	Interest	Fees	Review Date	Expiry Date/Term
A3	Overdraft	Natwest	Approved	Approved as proposed	20.000	B+1.00, B+5.00	0.300	30-Sep-14	
B2	Interest Rate Swap/Hedging	Natwest	Approved	Approved as proposed	3,474.000		0.000	30-Sep-14	01-Sep-38
B23	Loan	Natwest	Approved	Approved as proposed	5,268.691	GBPLI+1.00	0.000	30-Sep-14	02-Sep-34

Total	Existing Limit	Proposed Limit	Change(+/-)
Total facilities under review	8,762.691	8,762.691	0.000
Total facilities not under review	0.000	0.000	0.000
Total Direct Exposure for Connection	8,762.691	8,762.691	0.000
Total Group Settlement Risk	0.000	0.000	0.000

£3.5M Credit Line is it a **Real Debt**?

(SCREEN SHOT FROM RBS RMP CREDIT SYSTEM)

How the sting works

1. The Set Up / Inducements

The Trusted

Bank Manager

= Offers Low Margin rates of circa 1 to 1.5%

= Offers Low set up fees

= Allows Friendly informal Valuations

Customers were told;

- Rate are at an all time low but there is financial uncertainty
- Remember the recession and 12% interest rates?
- You can protect yourself with some simple products
- I am no expert, but I know someone from the Bank who is

2. The Con(vincer)

The Treasury Expert

- **We can provide you with ways to protect against high interest rates**
- **The average interest rates over 30 years is 9%**
- **We could sell you expensive Caps or instead provide solutions with no upfront premium (Swap)**
- **There is a break cost or benefit if the trade is broken but we don't know the level of that risk**

WHAT THEY DID NOT TELL YOU

They do not work for the Bank (NatWest) they work at RBS Markets in a separate firm

RBS will make a substantial commission from the sale which will be shared with NatWest

They know your expected losses over the term of the trade, having instructed your bank manager to put credit in place for that amount & losses are unlimited

Their forecasts show interest rates going down soon & staying down long term (circa 15 years +)

Rather than lend you the money for a Swap (Margin Credit) the Bank could lend you the money for a much less costly and less risky cap instead

3. The STING

Customer Sees - A Charge on property Title for the Bank Loan.
But this is now an **ISDA** deal with Property Title being collateral for the Swap liabilities.
The Customers assets are now controlled & secured by the Bank and their Broker under the ISDA.
These processes are possible because 2 FCA firms in a Group collude to cover up the credit risks.

DEBENTURE - Applies to all 'Group Liabilities'
ALL MONIES CHARGE - Includes Actual or Contingent Liability Wording

How the Bank Actually Used your **ASSETS**

Customer

£2M Loan

£300k Credit Line
(Undisclosed)

BANK

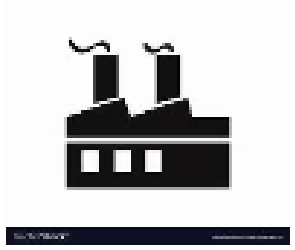
NatWest

COLLATERAL
PLEDGED

BROKER

RBS

The Royal Bank of Scotland



LEVERAGE £15M
PLUS?

1. When you undertake the ISDA trade you put your assets up as **Collateral**
2. The assets cover the **undiclosed credit** line (Margin Credit) as well as the Loan debt
3. If you have failed to **disapply** it the Bank can use your assets as its collateral
4. The Bank will **Pledge** your assets to its broker in the Group & finance them
5. The avregae leverage in 2007/08 was **4.5 times the asset value** (rehypothecation)

What do the Rules Say?

The Financial Conduct Authority (FCA) COBS 14 state;

A Firm must explain enough about any investment containing *'Margin Credit', 'Leverage'* & '*Contingent Liabilities*' for a Retail Client to make an *'Informed Decision*' before committing to such an investment…

WHY?

Because the FCA's CASS Rules also allow these processes (emphasis added);

'*arrangements covered by this [1]chapter[1] are those under which the firm is given a right to use the asset, and the firm treats the asset* ***as if legal title*** *and* ***associated rights to that asset*** *had been transferred to the firm…'*

'Examples of the arrangements covered by this [1]chapter[1] include ***the taking of collateral by a firm, under the ISDA*** *English Law (transfer of title) … Credit Support Annexes (****assuming the right to rehypothecate has not been disapplied****)'*

'The ***firm may exercise its right to treat the asset as its own*** *by, for example, clearly so identifying the asset in its own books and records'*

Why the IRHP Review Failed to Deliver Fair Compensation

IRHP Review was a **Point of Sale** Review	**Credit Lines were put in place prior to the sale, so were not considered**
Rules on contingent liabilities were replaced by **Sales Standards**	**This allowed focus on break costs rather than the credit line liability**
Foreseeability compensation based on **Point of Sale**	**Focus was removed from expected losses on products to explanation of break costs**
Tame 'Skilled Persons' were informed by files produced by instructing banks	**Little or No independent investigation of sales & credit processes**
There was expected to be **£30B** Compensation from the Scheme	**ONLY £3B WAS PAID OUT…**

DID the FCA Mislead Swap Victims?

Email from David de Souza (FCA Swap Expert) to me 3rd June 2016 (emphasis added):

"The IRHP review does of course consider whether the banks sufficiently explained to the customer the risks of potential future (contingent) liabilities"

NatWest bank classed the customers Credit Line as the Contingent Liability but extracts from a KPMG Project Rosetta File on the NatWest £5.5M loan case with a £3.5M credit line state:

*"There is **no evidence that the details of the contingent liability** were discussed with the customer prior to the trade"*

Which should lead to full redress HOWEVER, the KPMG Reviewer then sates:

"The setting** and monitoring **of the contingent liability is not**, however **covered in the IRHP review"

And:

*"The setting of any contingent liability is a credit risk function carried out as part of the operational process. **The process is not related to the sales standards agreed with the FCA** in respect of the past Review of IRHP's."*

DESPITE £5M LOSSES NO REDRESS WAS AWARDED TO THIS SWAP VICTIM

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ARE THE FCA ACCOUNTABLE?

I RAISED A FORMAL COMPLAINT OVER THE REVIEW FAILINGS TO THE FCA & ALLEGED I WAS MISLED BY MR DE SOUZA IN DECEMBER 2019, I AM STILL AWAITING THE FULL FINAL RESPONSE OVER 16 MONTHS LATER.

MR DE SOUZA CANNOT RESPOND IN PERSON AS HE NO LONGER WORKS FOR THE FCA…

DAVID DE SOUZA IS NOW MANAGER OF CORPORATE GOVERNANCE AND REGULATORY AFFAIRS AT THE **NATWEST GROUP**.

HIS ROLE IS TO **MANAGE** AND SUPPORT **RISK**, **FINANCE**, LEGAL AND SERVICES ENGAGEMENT **WITH THE FCA**, PRA AND BANK OF ENGLAND

Was it Really a Fraud?

NatWest Whistle-blowers have disclosed to me;

'RBS bonuses earned by selling Swaps were so large that a Commercial Manager could double their earnings or more, so the bonus rate was capped at 110% of basic salary.'

'A Commercial Manager on £60k pa could increase that to circa £132k pa from just 2 or 3 good Swap sales.'

'We were told not to mention the credit line risk to customers or ever disclose that was the cause for sending them to GRG or into administration.'

Home Office Counting Rules for Recorded Crime — With effect from April 2020

NFIB18 Fraud by Failing to Disclose Information Classification (1 of 1)

53/41 Fraud by failing to disclose information
(V) Fraud Act 2006 Sec 3

Definition - Legal: Fraud by Failing to Disclose Information

Fraud Act 2006 Sec 3

"…dishonestly fails to disclose to another person information which he is under a legal duty to disclose and intends by failing to disclose the information to make a gain for himself or another, or to cause loss to another or expose another to a risk of loss".