

**Independent Valuation
under the Northern Rock plc
Compensation Scheme Order 2008**

Final Document
March 2010

by Andrew Caldwell

**Independent Valuer appointed under Part 3 of the Northern Rock
plc Compensation Scheme Order 2008**

Table of contents

Chapter	Page
1. Introduction	3
Purpose of this document	3
Reconsideration	4
Shareholder register	4
2. Summary of responses to the consultation	5
Summary of representations	5
3. The effect of these representations on my provisional views set out in the Consultation Document	17
4. My final determination as to the amount of any compensation payable by the Treasury	18

1. Introduction

- 1.1. I was appointed by HM Treasury (“the Treasury”) on 8 September 2008 as Independent Valuer under the Northern Rock plc Compensation Scheme Order 2008 (“Compensation Order”).
 - 1.2. It is my role to determine the amount of any compensation payable by the Treasury to persons affected by the transfer of Northern Rock plc (“Northern Rock”) into temporary public ownership (“TPO”) at the beginning of 22 February 2008.
 - 1.3. The transfer into TPO was effected by the Northern Rock plc Transfer Order 2008 (“Transfer Order”), which was made under the Banking (Special Provisions) Act 2008 (“the Act”). The following categories of persons will have been affected by the Transfer Order:
 - those who held ordinary, foundation or preference shares in Northern Rock;
 - those whose rights to receive shares in Northern Rock (whether by subscription, conversion or otherwise) were extinguished by Article 4 of the Transfer Order; and
 - those whose “consequential rights” were extinguished by Article 12 of the Transfer Order.
 - 1.4. The above persons are called “Affected Parties”.
 - 1.5. I am required to determine the value of Northern Rock's shares, and the value of any rights to receive shares that were extinguished by virtue of Article 4 of the Transfer Order, immediately before the transfer of Northern Rock into TPO at the beginning of 22 February 2008. I refer to this point in time as the “Valuation Date”.
 - 1.6. I have not received any claims for compensation by anyone who could show that they had been affected by Article 12 and it has therefore not been necessary for me to assess any entitlement to compensation in respect of Article 12. As such, in this document any reference to determining whether any compensation is payable to Affected Parties should be read as a reference to determining whether any compensation is payable to former shareholders and those whose rights to receive shares were extinguished by Article 4.
 - 1.7. I set out my provisional views in the Consultation Document which I published in December 2009 (“Consultation Document”).
- Purpose of this document***
- 1.8. This document has been prepared alongside the Assessment Notices which I am now issuing to Affected Parties.
 - 1.9. The purpose of this document is to set out:
 - a summary of the substantive points arising from the representations I received in response to the Consultation Document and my comments on them;

- the effect of those representations on my provisional views set out in the Consultation Document; and
- my final determination as to the amount of any compensation payable by the Treasury.

Reconsideration

- 1.10. Any person who is affected by the determination set out in an Assessment Notice may seek reconsideration of the determination within 5 weeks from the date of the Assessment Notice, i.e. no later than 4 May 2010.
- 1.11. Any such request for reconsideration should be submitted to me, together with any evidence you wish to submit to support your request, as follows:
- by post to Andrew Caldwell, Northern Rock Valuer, BDO LLP, 55 Baker Street, London, W1U 7EU; or
 - by email to northern.rock@bdo.co.uk, noting your postal address.
- 1.12. Where a request for reconsideration is made, I shall reconsider my determination and then issue a Revised Assessment Notice to the person who has made the request for reconsideration.
- 1.13. This Revised Assessment Notice will contain the following:
- the date on which it is issued;

- notification that the original Assessment Notice has been upheld or varied, as the case may be;
- the amount of any compensation determined by me as being payable; and
- the reasons for my decision.

- 1.14. The Revised Assessment Notice will also contain details of the period within which and means by which any person affected by a Revised Assessment Notice, and who is dissatisfied with it, may refer the matter to the Tribunal.

Shareholder register

- 1.15. Northern Rock's registrars, Capita Registrars ("Capita") maintain the database of names and addresses that I use for my mailings. It is therefore important that Affected Parties continue to update Capita about any change in their personal details at:
- Capita Registrars
Northern House
Woodsome Park
Fenay Bridge
Huddersfield
HD8 0LA
Telephone: 0871 664 0340
Fax: 0871 664 0350
E-mail: northernrock@capitaregistrars.com

2. Summary of responses to the consultation

- 2.1. The purpose of this section is to summarise the substantive points arising from the representations made in response to the Consultation Document and to set out my comments in respect of them.
- 2.2. I invited written representations on the Consultation Document by 29 January 2010.
- 2.3. All representations have been made in written form. I have not met with any Affected Parties since the issue of the Consultation Document.

Summary of representations

- 2.4. I set out below a summary of the substantive points arising from the representations I have received and my comments on them. I have not commented below on those representations which concern the Government's approach to Northern Rock and its decision to place it into TPO or any other matters falling outside the scope of the valuation which I am required to undertake.

Withdrawal of financial assistance

- 2.5. The primary legislation that governs the exercise of my functions (Section 5(4) of the Act) requires me to make two interrelated assumptions:

- (i) that all financial assistance provided by the Bank of England (“BoE”) or the Treasury to Northern Rock has been withdrawn (whether by the making of a demand for repayment or otherwise) (the “*withdrawn assumption*”); and
- (ii) that no financial assistance would in future be provided by the BoE or the Treasury to Northern Rock (apart from ordinary market assistance offered by the BoE subject to its usual terms) (the “*no further financial assistance assumption*”).
- 2.6. The words “*financial assistance*” are defined in Section 15(1) of the Act, as follows:
- “*in relation to any person, includes –*
- (a) *assistance provided by way of loan, guarantee or indemnity,*
- (b) *assistance provided by way of any transaction which equates, in substance, to a transaction for lending money at interest (such as a transaction involving the sale and repurchase of securities or other assets), and*
- (c) *assistance falling within paragraph (a) or (b) provided indirectly to or otherwise for the benefit of the person (including the provision of assistance within paragraph (a) or (b) to any group undertaking of that person),*

whether provided in pursuance of an agreement or otherwise and whether provided before or after the passing of this Act”.

- 2.7. The Explanatory Notes to the Act say that these assumptions “ensure that any value that is dependent on public support provided to the deposit-taker is disregarded when compensation is determined”. I accept that this is a good summary of the purpose of Section 5(4), read in its statutory context.
- 2.8. The Compensation Order further circumscribes the nature of the valuation exercise I must undertake. It provides, by paragraph 3(2) of the Schedule, that the amount of any compensation payable in respect of shares in Northern Rock is an amount equal to their value “immediately before the transfer time” (i.e. immediately before the start of 22 February 2008) and, by paragraph 6 of the Schedule, requires me in determining that value, to assume that Northern Rock is unable to continue as a going concern and is in administration.
- 2.9. So, the exercise I have to carry out is one to determine the value of the shares (or the right to receive shares, as the case may be) in Northern Rock immediately before the start of 22 February 2008, disregarding any value dependent on the continuation of the public support that was provided between September 2007 and that time, and assuming that Northern Rock is unable to continue as a going concern and is in administration.
- 2.10. There are three preliminary matters to make clear about the nature of this exercise.
- 2.11. First, it is not – as some consultees initially seemed to suggest – an exercise directed at discovering what the value of Northern Rock was or would have been in September 2007 if no public support had ever been offered.
- 2.12. The legislation is clear that I must conduct the valuation as at the Valuation Date and for that purpose must assume that the support “has been withdrawn” (which necessarily connotes something that was initially provided having been taken away).
- 2.13. Northern Rock’s position undoubtedly changed to some extent in the six months between September 2007 and February 2008. The exercise I am required to undertake is an assessment of value as at the Valuation Date, rather than at some earlier date.
- 2.14. Secondly, and contrary to some of the representations I have received, the purpose of the Valuation Assumptions is not to replicate a “realistic” scenario, but to establish a conceptual framework within which to assess that part of the value of Northern Rock, as at the Valuation Date, that was not dependent on the public support provided to it.
- 2.15. A view has been put forward that it is unrealistic to suppose that a Government that had supported Northern Rock to the tune of £25.38 billion would simply withdraw that support immediately before the Valuation Date, knowing that this would cause Northern Rock to fail. It is however clear that

the legislation requires me to assume that the financial assistance provided by the BoE and the Treasury had been withdrawn.

- 2.16. My task is to assess the value of the shares (or the right to receive shares, as the case may be) on the Valuation Date. The legislation provides that the amount of any compensation payable is an amount equal to the value as at the Valuation Date, having first deducted that proportion of the value that is dependent on public support.
- 2.17. Thirdly, there could be little doubt about how this deduction was to be effected if Northern Rock had sufficient cash reserves to repay the £25.38 billion of public support: an equivalent amount of cash would be deducted from Northern Rock's balance sheet. But Northern Rock did not have sufficient cash to meet its liability to the BoE: it had assets which had been given a particular book value on its balance sheet but whose value in the market was considerably lower than that book value.
- 2.18. Some consultees have submitted to me that, in those circumstances, the correct approach is to deduct assets whose *book value* is equivalent to that of the public support given to Northern Rock. Putting the matter another way, I am asked to assume that the actual value of the assets in Northern Rock's balance sheet as at the Valuation Date is the same as their book value. I see no reason why I should make that assumption; indeed it would clearly be a breach of my duty in that I would not be determining the actual value of the shares (or right to receive shares) in Northern Rock in the

light of the hypothetical assumptions that I am required to make. My task, as Independent Valuer, is to assess the *actual value* of the shares (or right to receive shares) in Northern Rock as at the Valuation Date assuming that all public support has been withdrawn.

- 2.19. Against that background, I consider that the only way of giving proper effect to the withdrawn assumption is to deduct from Northern Rock's balance sheet, immediately before the Valuation Date, assets which, if realised at that time, would actually yield the £25.38 billion necessary to repay the BoE.
- 2.20. A number of consultees submitted to me that this interpretation was incorrect; one consultee suggested that I should seek a ruling from the court on the interpretation of the Withdrawn Assumption. I have considered the arguments, but I am not persuaded by them. I set out below my brief response to the main points made by the consultees. For the reasons set out below I consider that the interpretation of the Withdrawn Assumption is clear and that I should not put the valuation process on hold to seek a ruling on this issue.
- 2.21. Some consultees submitted that my approach contradicts the language of Section 5(4)(a). They drew particular attention to the words in brackets ("*whether by the making of a demand for repayment or otherwise*"). They said that these words showed that all that was required for financial assistance to be withdrawn was that a *demand* for repayment had been made, but that repayment itself would take place only at the end of an administration. If this were correct, I would be

- valuing Northern Rock on a basis which gave it the benefit of Government money throughout a potentially protracted administration.
- 2.22. The withdrawn assumption requires, by contrast, that I assume that financial assistance “*has been*” withdrawn and is not provided for in the future. The reference to a demand for repayment is simply one of the mechanisms by which the Government can trigger the withdrawal of financial assistance; the withdrawal of that assistance and its cessation for the future is complete only when the demand is satisfied.
- 2.23. Some consultees refer to withdrawal of “*support*” rather than the withdrawal of “*financial assistance*”. The latter is the expression used in Section 5(4) of the Act and defined in Section 15(1). It is important to understand what I am required to treat as withdrawn by applying that definition. The definition requires me to assume that the loan provided by the BoE has been withdrawn, rather than merely that the availability of further funding has been brought to an end. For the reasons given above, the withdrawal of the loan requires that I must proceed on the basis that it has been repaid.
- 2.24. Consultees offered in support of their arguments the factual and legal submissions made by the Treasury during the judicial review proceedings, the judgments of the Divisional Court and Court of Appeal and certain Parliamentary statements made during the passage of the Bill which became the Act.
- 2.25. The judgments were not directed at the question under consideration here. However, having considered the Court of Appeal’s judgment carefully, it seems to me that, far from being inconsistent with my proposed approach, it supports it. The Court of Appeal endorsed the proposition that the purpose of the assumptions was “*to put shareholders in the position they would have occupied had no LOLR support been provided*”. The expression LOLR means the Lender of Last Resort.
- 2.26. The only way of putting Northern Rock in that position, whilst at the same time staying faithful to the obligation to value the shares (or the right to receive shares) as at the Valuation Date (rather than on some earlier date), is to remove from its balance sheet assets sufficient in fact to repay the totality of the financial assistance.
- 2.27. Consultees also offered in support of their arguments the wording of the Explanatory Note quoted at paragraph 2.7 above. The Explanatory Note is consistent with the approach I have taken – by giving effect to the withdrawal of financial assistance in the manner described in the Consultation Document, I have ensured that any value dependent on public support provided to Northern Rock has been disregarded when conducting my valuation.
- 2.28. Finally, I have considered what was said in Parliament at the time of the passage of the Bill which became the Act. Even if that were a legitimate aid to the construction of the Act, I can see nothing in the extracts relied upon by consultees that casts any light on the question with which I am concerned.

- 2.29. One further submission made to me was that adopting the approach outlined in the Consultation Document would mean assuming that Northern Rock's directors would act in breach of English insolvency law by repaying the BoE in circumstances where that would place them in breach of their duty to creditors and/or the company itself and in breach of FSA Listing Rules.
- 2.30. In my view, this submission proceeds from a misunderstanding of the role of the assumptions in the valuation process. The purpose of the assumptions is not to model a realistic hypothetical scenario, but to ensure that the value ascribed to the shares excludes value dependent on public support.
- 2.31. Accordingly, my function as Independent Valuer is to assess the value of the shares on the *assumption* that financial assistance "*has been*" withdrawn immediately before the Valuation Date, irrespective of whether it could in fact have been withdrawn on that date, and on the *assumption* that no further financial assistance is provided after that date. The withdrawn assumption is a legal construct whose purpose is to isolate that part of the value of Northern Rock which is not dependent on public support or (putting it another way) to determine what Northern Rock would look like on the Valuation Date if the value of the financial assistance provided to it was taken out of its balance sheet.
- 2.32. For the same reason, the submission that my approach is "*unrealistic*" or "*commercial nonsense*" is, in my view, misconceived.
- 2.33. One of the consultees suggested to me that my approach involves making a further assumption, not provided for in the legislation, about the order in which two events which I am required to assume – the withdrawal of financial assistance and the administration – would occur.
- 2.34. I accept that my approach involves approaching the valuation on the basis that, by the time the valuation exercise comes to be carried out, the financial assistance has already been withdrawn, but I do not accept that this approach involves an assumption beyond those provided for in the legislation. On the contrary, the tense used in Section 5(4)(a) ("*has been withdrawn*") indicates a clear intention that, at the point at which the valuation exercise is carried out, the financial assistance has already been withdrawn.
- 2.35. Another consultee suggested that the Valuation Assumptions should be applied only when determining the amount of any compensation payable, not when carrying out the initial valuation exercise. In my view, the valuation exercise is one and the same as the exercise of determining the amount of any compensation payable. There is no point in carrying out a valuation on some other basis than that which the legislation requires me to adopt and I do not propose to do so.

Status of the shares held by the Northern Rock Foundation (“the Foundation”) in Northern Rock

- 2.36. It has been suggested to me that my valuation of Foundation shares in Northern Rock should be undertaken on the basis that (i) the Foundation held ordinary shares at the Valuation Date; or (ii) that the Foundation's rights should be identical to those attaching to the ordinary shares.
- 2.37. It was submitted that part (ii) of that representation is supported by reference to Article 8.2 of Northern Rock's Articles of Association which states that:

“The Foundation Shares shall rank pari passu in all respects with the Ordinary Shares save as otherwise provided in these Articles or in the terms of the Foundation Shares”.

- 2.38. Given my determination of the amount of any compensation payable by the Treasury to Affected Parties as set out in Section 4 of this document, I do not believe that I have any need to consider further whether I should value the Foundation's shares as though they were ordinary shares (or whether the Foundation's rights should be identical to those attaching to the ordinary shares) as at the Valuation Date. It does not impact the ultimate outcome.

Valuation of the goodwill and brand of Northern Rock

- 2.39. A submission has been made to me that there was some value in Northern Rock's inherent goodwill and brand and I have

been asked to confirm whether I received any professional advice or valuation of these assets.

- 2.40. In the light of my professional experience as a valuer of such assets, and my assessment that their value would not be material in the context of Northern Rock's balance sheet, I did not seek external advice.
- 2.41. None of the representations I received caused me to change my provisional view, expressed at paragraph 10.24 of the Consultation Document, that there was no inherent goodwill in Northern Rock's business, given that I am required to assume that Northern Rock is unable to continue as a going concern.
- 2.42. In addition, I remain of the view that Northern Rock's brand was tarnished by the run on the bank in September 2007, as evidenced in the bids by Northern Rock's management and Virgin, each of whom proposed to re-brand.

Valuation of Northern Rock's property

- 2.43. It has been put to me that there was considerable value in Northern Rock's property portfolio and that this should be considered in my valuation.
- 2.44. I have taken into account the value of the commercial property portfolio and included in my valuation the book value of that portfolio as shown in the Management Accounts.

2.45. As far as the continuing property development is concerned, none of the representations I received has caused me to change my provisional view, expressed at paragraph 10.21 of the Consultation Document, that any such enhancement is not material to my valuation. Even if the full impairment charge for such was re-instated this would only affect the valuation by approximately £56 million, which would make very little overall impact on the deficit.

Termination payments to senior executives of Northern Rock

2.46. It has been suggested to me that some of the pension arrangements and payments to senior executives of Northern Rock, both before and after the transfer into TPO, may not have been appropriate and that there could be a potential claim for recovery of all or part of the sums involved.

2.47. Any such payments made after the transfer into TPO are not relevant for the purpose of my valuation. As far as payments made before the transfer into TPO are concerned, even if a claim to recover such payments could be brought and was successful, it would not be material in the context of the balance sheet.

Interpretation of going concern status

2.48. It has been represented to me that the Valuation Assumptions refer to Northern Rock, the corporate entity, rather than its business and that I am therefore not required to assume that the business (or part of it) could not continue and be sold as a going concern.

2.49. In circumstances where I am required to assume that Northern Rock is in administration and unable to continue as a going concern, it is unlikely that the administrator would find anyone prepared to buy the entire business of Northern Rock.

2.50. I did not identify significant parts of Northern Rock's business that would be run as a going concern with a view to selling that part at a price that would exceed the book value of relevant assets.

2.51. It is noteworthy that, prior to the transfer to TPO, Northern Rock considered the sale of its branches and operating platform. However, the offers received indicated that there would have been a discount to book value for these assets.

2.52. I believe that had an administrator tried to sell these assets, a discount would have been applicable.

The appropriateness of the net asset method

2.53. I have been asked to comment on whether the net asset method of valuation is the most appropriate valuation method to use or whether I should instead use some other valuation method.

2.54. As stated in Section 8 of the Consultation Document, the net asset method of valuation is usually used for a business that is no longer a going concern. My approach to the valuation reflects the withdrawal of financial assistance but then considers the run-off of the remaining assets over an assumed 5 year period of administration which, after allowing for

realisations from the assets and payments to the creditors, results in a net deficit position of £5.68 billion.

Whether the BoE would have acceded to a long-term run off of assets

2.55. I have been asked to comment on whether the BoE would have acceded to a long-term run-off of Northern Rock's assets in order to repay its loan.

2.56. I do not believe that this is a relevant consideration because I am required to assume the withdrawal of the financial assistance and that no financial assistance would be provided in future (apart from ordinary market assistance offered by the BoE subject to its usual terms).

2.57. To give effect to the withdrawal of financial assistance, I am required to assume that the BoE had already been repaid prior to the appointment of an administrator and therefore the issue raised by consultees does not arise.

Whether the Treasury would have become a significant unsecured creditor of Northern Rock as a result of calls upon it as deposit guarantor, resulting from an administration, and if so whether it would have acceded to a long term run-off of assets in order to repay amounts called under the deposit insurance scheme.

2.58. I have been asked to comment on whether the Treasury would have become a significant unsecured creditor of Northern Rock, as a result of calls upon it as deposit guarantor following Northern Rock being placed into

administration, and whether it would have acceded to a long-term run-off of assets in order to repay the amounts it had committed.

2.59. The withdrawal of financial assistance includes the withdrawal of any guarantees provided by the Treasury, therefore that question does not arise.

Requirement for additional information

2.60. I have been asked to confirm that I have been granted access to all information I have requested from the Treasury and other parties. In particular, I have been asked to:

- confirm whether I have met certain parties and to provide copies of the notes of such meetings;
- state whom I met from Goldman Sachs and to provide copies of the notes of such meetings;
- confirm what information I received from the BoE;
- confirm whether I was given access to the FSA's files concerning Northern Rock's obtaining of Basel II approval; and
- provide notes of interviews with FSA personnel and other documents provided by the FSA.

- 2.61. In addition, I have been asked to provide details of the actual assumptions I have used, a breakdown of how the projected losses are incurred and sensitivity analyses based on varying the assumptions.
- 2.62. I can confirm that I am not awaiting any information that I believe would have an impact on my determination of value.
- 2.63. One consultee has cited the Court of Appeal decision in *R v North and East Devon Health Authority, ex parte Coughlan [2001]* as authority for the proposition that procedural fairness requires that I provide them with all the information with which they have requested to be provided.
- 2.64. I do not agree. *Coughlan* says that in order for a consultation to be carried out properly, it “*must include sufficient reasons for particular proposals to allow those consulted to give intelligent consultation and an intelligent response*”. It does not provide that consultees must be provided with any information as they might request, nor does it entitle me not to follow the provisions in the Compensation Order which govern the disclosure of information.
- 2.65. The Compensation Order (as amended) provides that I may disclose information:
- pursuant to paragraph 9C of the Schedule to the Compensation Order, with the consent of the person from whom I obtained that information and, if different, the person to whom it relates; or
 - without consent pursuant to paragraph 9D, if and to the extent that I consider it necessary to do so for the purpose of exercising the functions of my office, providing that before disclosing any information I must have regard to the need to exclude from disclosure (so far as is practicable):
 - (a) “*commercial information, the disclosure of which might significantly harm the legitimate business interests of the person to whom it relates,*
 - (b) *information relating to the private affairs of an individual, the disclosure of which might significantly harm the individual’s interests, or*
 - (c) *any information the disclosure of which would be contrary to the public interest*”.¹
- 2.66. I have disclosed information where I consider it necessary to do so to enable the reader to understand the work I have undertaken. I do not consider it necessary, for the purpose of exercising the functions of my office as Independent Valuer under the Compensation Order, to disclose further information other than that which I disclosed in the Consultation Document.

¹ The Northern Rock plc Compensation Scheme (Amendment) Order 2009, Article 9D(4)
http://www.opsi.gov.uk/si/si2009/uksi_20090791_en_1

2.67. One consultee has also noted that I refer in the Consultation Document to Adam Applegarth's 22 September 2007 letter to the BoE (Exhibit D to the Consultation Document) and the Insolvency Paper dated 24 September 2007 (Exhibit E) and an issue has been raised as to what extent I placed reliance on that material.

2.68. I gave careful thought to the extent to which I should rely on the above material because it was written at a time when various options were under consideration and bearing in mind that it may have been written to emphasise to the BoE and the Treasury the potential consequences if Northern Rock were to be placed into administration. In other words, it might be thought that the purpose of these documents was to persuade rather than only to inform.

2.69. I discussed those documents with relevant parties and I am satisfied that they accurately represent their views of what would have happened if Northern Rock were to have been placed into administration at that time.

2.70. In any event, I formed my own view as to the outcome of an administration of Northern Rock as at the Valuation Date, and then compared that view with the outcome envisaged in the above documents.

Information held by Robert Peston and the BBC

2.71. It has been suggested to me that I should investigate a potential claim for loss resulting from the leak of information regarding the provision of the LOLR facility and that the

amount of this potential claim should be included in the valuation.

2.72. I have not investigated whether Northern Rock would have legal grounds for such a claim against those responsible for the leak. I do not believe that an administrator would seriously consider bringing such a claim and incurring the associated legal costs unless there was a reasonable prospect of success and a material benefit to creditors.

2.73. Even if such a claim could be brought and was successful, any damages that could in practice be recovered by pursuing the person responsible for the leak are unlikely to be material in the context of Northern Rock's balance sheet.

Statements made by the Treasury and the FSA

2.74. It has been represented to me that I should investigate any change in the circumstances of Northern Rock between the time that the Treasury or the FSA first issued statements on Northern Rock in 2007 and the Valuation Date (in particular the Chancellor of the Exchequer's statement of 17 February 2008) and that I should provide access to all papers relevant to this investigation.

2.75. Any statements issued by the Treasury and the FSA, prior to the Valuation Date, were made in the context of the provision of financial assistance to Northern Rock. The opinions expressed in these statements therefore have no bearing upon my valuation of Northern Rock, which I have undertaken applying the Valuation Assumptions.

Private sector bidders

- 2.76. It has been represented to me that I should use information provided by bidders for Northern Rock to give evidence of value of Northern Rock. I can confirm that I have considered such information.
- 2.77. As noted in the Consultation Document, I obtained transactional information, including information in relation to potential and actual bids for Northern Rock and its assets, and analyses of these bids carried out by advisors of Northern Rock and the Tripartite Authorities. I also met with potential bidders for Northern Rock.
- 2.78. It should be remembered that any bids made for Northern Rock in the period leading up to the Valuation Date were made on the basis of continuing financial assistance and therefore they are not indicative benchmarks for the assessment of value of Northern Rock when the Valuation Assumptions are applied.

Financial support provided to a purchaser of Northern Rock

- 2.79. One consultee has suggested to me that I should consider the possibility of the sale of the whole business and/or the deposit base in the situation where financial support is provided to a purchaser of Northern Rock and not to Northern Rock itself.
- 2.80. This would involve attributing to Northern Rock a value which is dependent on public support, albeit that such support would be provided via the purchaser. I am required

to assume that no financial assistance would be provided to Northern Rock from the Valuation Date onwards. The provision of support to a purchaser of Northern Rock would constitute providing “*financial assistance*” to Northern Rock as that expression defined in Section 15(1). I must therefore assume that no such assistance would be provided. In any event, taking the possibility of such support into account would be to proceed in a manner which is contrary to the purpose of the legislation, namely to ensure that any value which is dependent on public support is disregarded.

Damages resulting from a claim against the Tripartite Authorities

- 2.81. It has been represented to me that an administrator of Northern Rock might have had to consider whether any legal action could or should be taken against the Tripartite Authorities in respect of alleged regulatory failures. I have been asked to assess the likelihood of a successful outcome of such claim and, if appropriate, the amount of any potential damages.
- 2.82. Under the Memorandum of Understanding, which sets out the division of responsibilities between the Tripartite Authorities, the BoE is responsible for contributing to the stability of the financial system as a whole; the Treasury is responsible for the institutional structure of the financial regulatory system and the FSA is the regulator responsible for authorising and supervising individual banks. Therefore, I would expect any claim in respect of alleged regulatory failure to be brought against the FSA.

- 2.83. The FSA is protected from liability in damages in respect of acts carried out in good faith in the discharge of its statutory functions. This statutory immunity is set out in the Financial Services and Markets Act 2000. A claim could however be brought provided that it is based on an act or omission by the FSA which the administrator can show to have been in bad faith (or unlawful under the Human Rights Act). I am not aware of any evidence that would enable such a claim to succeed. Accordingly, such a claim is merely speculative.
- 2.84. I do not believe that an administrator would seriously consider bringing a claim against the FSA and incurring the associated legal costs, unless there was a reasonable prospect of success and a material benefit to creditors. I believe that the chance of success of such claim to be too remote to incorporate in my valuation. I have not considered this point further.

Repurchase of Northern Rock debt by Northern Rock

- 2.85. It has been suggested to me that the administrators of Northern Rock may have been able to repurchase Northern Rock's own debt if the market price of the debt was lower than the amount that would be payable to the debt-holder at the end of the administration, resulting in additional funds being available to the administrator.
- 2.86. It is questionable whether an administrator has the power to buy back debt. In any event, I do not consider this to be an avenue that an administrator would seek to pursue.

- 2.87. First, it would expose him to potential claims from the other creditors if the debt purchased is worth less at the end of the administration than the amount he paid for it. The volatile nature of debt markets would make it impossible to predict this with any certainty during the administration. The risk of such claims would be reduced if an administrator could obtain the support of all the creditors of the company to any proposed transaction. However, the number of Northern Rock creditors would have made that impractical.
- 2.88. Secondly, an administrator would have to disclose to the creditor in question his assessment of the value of the debt at the end of the administration, such that the creditor would know that the administrator would be buying the debt at a discount. Any creditor in this position would be unlikely to trade with the administrator on this basis.

3. The effect of these representations on my provisional views set out in the Consultation Document

- 3.1. The purpose of this section is to explain whether or not my provisional views, set out in the Consultation Document, have changed as a result of the representations.
- 3.2. I have reviewed and considered all representations received since the publication of the Consultation Document. None of the representations I have received caused me to change my provisional views expressed in the Consultation Document. I have therefore determined that my provisional views on the amount of any compensation payable to former shareholders and those whose rights to receive shares have been extinguished by Article 4 of the Transfer Order are still appropriate.

4. My final determination as to the amount of any compensation payable by the Treasury

4.1. My method of determining the amount of any compensation payable to Affected Parties is as follows:

- (a) determine the assets that would need to be realised immediately prior to the Valuation Date to raise sufficient funds to repay the BoE funding;
- (b) on the basis that Northern Rock is unable to continue as a going concern and is in administration as at the Valuation Date, ascertain the amount of any surplus that would have been available for distribution to shareholders; and
- (c) determine the amount of any compensation payable to Affected Parties.

4.2. Having applied the Valuation Assumptions, I have determined that at the end of the assumed administration there would be a net deficit of approximately £5.68 billion. There would therefore be no surplus at the end of the assumed administration for distribution to shareholders.

4.3. As I explained in the Consultation Document, it would be appropriate to discount any surplus or deficit at the end of the assumed administration period to reflect the value of Northern Rock as at the Valuation Date. Since I have determined that there would be no surplus available for distribution to shareholders, I have not discounted the deficit.

4.4. It follows from the deficit to which I refer above, that there is no value in the shares as at the Valuation Date and therefore that no compensation is payable to former shareholders.

4.5. It further follows that as at the Valuation Date there is no value in the right to receive shares and therefore that no compensation is payable to those whose rights to receive shares were extinguished by Article 4 of the Transfer Order.

4.6. No-one has submitted a claim for compensation based on their “consequential rights” being extinguished pursuant to Article 12 of the Transfer Order.

4.7. In summary, therefore, I determine that the amount of compensation payable by the Treasury to former shareholders or to those whose rights to receive shares have been extinguished is nil.