Neutral Citation: [2024] UKFTT 246 (TC)

Case Number: TC09115

FIRST-TIER TRIBUNAL
TAX CHAMBER

Heard in person in London on 2-11 October 2023

Appeal reference: TC/2017/06719

Loan relationships - RCIs and warrants issued by subsidiary and parent companies in the context of the 2008 financial crisis – attribution of funds received where stated consideration for the warrants was effectively nil causing the RCIs to be shown in accounts as issued at a discount – was the attribution of funds GAAP compliant – if so did the resulting debits fairly represent losses on the RCIs under the loan relationship rules.

Heard on: 2-11 October 2023
Judgment date: 26 April 2024

Before

TRIBUNAL JUDGE BOWLER
MR JOHN WOODMAN

Between

BARCLAYS BANK PLC

Appellants

and

THE COMMISSIONERS FOR HIS MAJESTY'S REVENUE AND CUSTOMS

Respondents

Representation:

For the Appellant: Mr Kevin Prosser KC and Mr James Henderson of Counsel, instructed by Freshfields Bruckhaus Deringer LLP

For the Respondents: Mr David Milne KC, Ms Elizabeth Wilson KC, Mr Emile Simpson and Ms Elizabeth Atkinson of Counsel instructed by the General Counsel and Solicitor to HM Revenue and Customs

DECISION

This decision is reissued under Rule 37 of The Tribunal Procedure (First-tier Tribunal) (Tax Chamber) Rules.

INTRODUCTION

1. The appeal concerns the corporation tax treatment of debt instruments called Reserve Capital Instruments ("RCIs") issued by the Appellant ("BBPLC") and more particularly whether BBPLC can claim losses under the loan relationship rules in relation to an accruing discount shown its accounts for those instruments.

2. In essence, BBPLC issued interest bearing RCIs with a face value of £3bn at the height of the financial crisis and at the same time its parent company Barclays PLC ("Barclays") issued warrants over its own shares ("the Warrants"). £3bn was received by BBPLC but BBPLC accounted for the transactions on the basis that £800m of the £3bn received by it was in fact value paid by the investors for the Warrants, such that the cash receipt of £3bn in BBPLC's books reflected £2.2bn paid for the RCIs and £800m capital contribution from Barclays. The difference between £2.2bn and £3bn was treated as an accruing discount and deductible for corporation tax purposes as a debit arising in relation to a loan relationship.

3. The Respondents ("HMRC") argue, in essence, that the £3bn was paid for the RCIs such that the accounts were not GAAP compliant and/or did not fairly represent losses arising in relation to the RCIs; or the credit to equity reflecting the £800m fairly represented a profit to the Appellant.

BACKGROUND AND PROCEDURE

The matter appealed

4. BBPLC appeals the conclusion and amendments contained in a Closure Notice issued on 3 October 2016 under paragraph 32 Schedule 18 Finance Act 1998 in relation to BBPLC's tax return for the accounting period ended 31st December 2008 ("the Relevant Period") in respect of deductions claimed in respect of the RCIs.

BURDEN OF PROOF

5. The burden of proof rests with BBPLC to show that the Closure Notice conclusions are wrong and it is entitled to claim the losses said to arise from an accreting discount on the RCIs. The ordinary civil standard of the balance of probabilities applies.

EVIDENCE

6. The written evidence before us consisted of a main hearing bundle running to 6608 pages and a supplementary bundle running to 475 pages.

7. Included in the bundle is a Witness Statement from Lorraine Connell and a Witness Statement provided by Mr Roger Jenkins in the case of *PCP Capital Partners LLP & Anor v Barclays Bank PLC* [2021] EWHC 307 (Comm).

8. Mr Prosser confirmed that the Appellant would not in fact be relying upon the Witness Statement of Mr Jenkins.

9. However, at times Mr Prosser has relied upon evidence of Mr Jenkins described in the *PCP* case. We have declined to rely upon that evidence save to the extent reflected in the findings made by Mr Justice Waksman in his judgment or otherwise reflected in the documentary evidence before us. This is because Mr Jenkins did not attend the hearing to be cross examined on any evidence. In addition, we take into account that Mr Justice Waksman said (at [516-522] of *PCP*) that Mr Jenkins was prepared to be dishonest and was dishonest at the time of the capital raising.

10. Lorraine Connell was unwell and therefore unable to attend the hearing. There was no request made to postpone the hearing and we were satisfied that we should not do so of our own volition given the extent of Lorraine Connell's evidence, the length of the hearing and the time already taken to bring the appeal to court.

11. Ms Connell is an employee of the Appellant. She was a Director in the Financial Institutions Group in BBPLC's investment banking division, working on the Debt Capital Markets desk, at the time of the transactions with which this appeal is concerned. She supported one of the senior personnel involved in the capital raising, Mr Boath, by providing an understanding of what kind of transaction the markets would support, in order to help with putting the deal together and getting it done. Primarily, that involved acting as an internal "go-between" amongst the triangle of the Debt Capital Markets desk, the Debt Syndicate desk and the sales team. She describes events as unfolding very quickly and explains she was not directly involved as that happened. Instead, the information shared with her was limited to what she needed to carry out the "go-between" role.

12. Ms Connell's Witness Statement was dated 2 September 2021. Much of it states what she could recollect about the events some 13 years previously. The core part of her evidence of relevance is that she recollects that there was simply "no bid" in the secondary market for debt instruments like the RCIs. As a result, she concludes that it would have been extremely difficult to value newly issued debt instruments by reference to the secondary debt markets.

13. However, her evidence was not tested in cross examination. At most we consider that it does no more than provide some support to the expert evidence of Mr Millar regarding the state of the RCIs market when they were issued.

14. Otherwise, as Mr Milne submitted, there was a notable lack of witness evidence adduced by BBPLC. None of those involved with the transactions themselves attended or provided Witness Statements. While there are well recorded issues regarding the relationship between various individuals who were senior executives at the time, one of them, Richard Broadbent, gave evidence in the *PCP* case. We have not been told why no one of those involved could provide evidence in this appeal. Similarly, no one from the auditors, PricewaterhouseCoopers ("PWC), attended which was particularly notable given the extent to which the hearing focused on the basis of the treatment in the accounts and the Appellant's accounting policies. There was no explanation given for this obvious lacuna. Mr Prosser submitted that as PWC were not involved in the capital raising negotiations they could have added little. However, they were the auditors who approved the accounting at the heart of this case. Indeed, evidence before us commented on discussions with PWC and indicated that PWC, at least initially, took a different view about valuing the RCIs to that relied upon by BBPLC. Furthermore, while we have been given voluminous bundles of evidence, the amount of contemporaneous evidence such as meeting notes and emails is relatively small. Altogether this has meant that on occasions there are notable gaps in the evidence before us.

15. However, we have had the benefit of the decision of Mr Justice Waksman in the case of *PCP*. This judgment has been provided to us in the evidence bundle and is relied upon by both parties to varying extents.

16. The findings of fact made by Mr Justice Waksman in that decision are treated by us as no more than a starting point. We are not bound by them and to the extent that evidence before us shows departure therefrom is correct we have reached our own conclusions based on that evidence. We are bound to reach our findings based on the evidence before us, but the findings made by Mr Justice Waksman were made on the basis of evidence provided by some of those directly involved in the transactions. That is of some significance, particularly where the Appellant has not produced any such witnesses in this appeal.

Expert evidence

17. We heard expert evidence from Mr Spooner and Mr Millar for BBPLC and Mr Kusi-Yeboah and Mr Larrieu for HMRC. The first of those experts in each case has provided expert accounting evidence and the second has provided expert valuation evidence.

18. While there were submissions made by Mr Prosser to the effect that the Appellant's experts were better qualified than HMRC's, we are satisfied that all four experts were well qualified to provide evidence in this appeal.

19. We address their evidence in more detail later in this decision.

20. However, we emphasise that the finding of facts is a function to be carried out by this tribunal. At times we identified a tendency for the experts to stray into this function. We are clear that we must find the facts and the expert evidence should then be applied to those facts.

21. The experts were specifically (and correctly) asked to address different factual scenarios in their reports. A large proportion of their evidence is therefore not set out, or referred to, in this decision as the evidence relates to differing facts from those which we have found.

GENERAL APPROACH

22. We do not claim to have dealt in this decision with every single point made by either side in more than 100 pages of submissions and comprehensive oral submissions. It is not necessary for us to do so. We are satisfied that we have considered all of the key issues and have taken into account all the materials which have been provided to us.

FINDINGS OF FACT

23. The parties have agreed a statement of facts and issues which we set out initially below.

The Transactions

24. At the height of the financial crisis, the Financial Services Authority ("FSA") instructed all of the major UK banks to increase materially their Tier 1 capital ratios. Part of Barclays' response was to raise additional capital from existing and new strategic and institutional investors, including those referred to as the "Subscribers" which were the vehicles representing the state of Qatar and Sheikh Mansour of Abu Dhabi. Those vehicles were Qatar Holding LLC ("Qatar Holding") representing Qatar; and PCP Gulf Invest 2 Limited ("PCP 2") and PCP Gulf Invest 3 Limited ("PCP 3") representing Sheikh Mansour. (The capital raising also involved the issue by BBPLC of mandatorily convertible notes ("MCNs") which are not the subject of this appeal.)

Agreements with the Subscribers

25. On 31 October 2008 the following agreements were entered into:

(1) an RCI subscription agreement between BBPLC and Qatar Holding under which BBPLC agreed to issue, and Qatar Holding agreed to subscribe £1.5 billion for, RCIs with a par value of £1.5 billion;

(2) a warrant subscription agreement between BPLC and Qatar Holding under which Barclays agreed to issue, and Qatar Holding agreed to subscribe £0.76 for, 758,437,618 of warrants to subscribe for 758,437,618 ordinary shares in Barclays;

(3) an RCI subscription agreement between BBPLC and PCP 2 under which BBPLC agreed to issue, and PCP 2 agreed to subscribe £1.5 billion for, RCIs with a par value of £1.5 billion; and

(4) a warrant subscription agreement between Barclays and PCP 3 under which Barclays agreed to issue and PCP 3 agreed to subscribe £0.76 for, 758,437,618 of

warrants to subscribe for 758,437,618 ordinary shares in Barclays (together with the warrants referred to in paragraph (b) above, "the Warrants").

26. The agreements referred to in subparagraphs 24(1) and (3) above are together the "RCI Subscription Agreements"; the agreements referred to in subparagraphs 24(2) and (4) above are together the "Warrant Subscription Agreements".

27. Pursuant to the terms of the RCI Subscription Agreements:

(1) The RCIs carried an interest coupon of 14% payable annually in arrears to (but excluding) 15 June 2019 and from 15 June 2019 at a rate which was the aggregate of 13.4% plus LIBOR for three-month Sterling deposits;

(2) The RCIs had no fixed redemption date, but (subject to the satisfaction of certain solvency and regulatory capital conditions) BBPLC could elect to redeem all and not some only of the RCIs from 15 June 2019;

(3) Each relevant Subscriber's obligation to subscribe for the RCIs was conditional on the obtaining of certain approvals from the shareholders of Barclays including approval to increase its authorised share capital sufficiently to enable the Warrants to be exercisable in full and to facilitate the application of the Alternative Coupon Satisfaction Mechanism on the RCIs (the Requisite Shareholder Approvals). (The Alternative Coupon Satisfaction Mechanism was the ability of BBPLC to elect in certain circumstances to satisfy any payment on the RCIs through the issue of shares, which is (broadly) effected via an issue of BBPLC shares to Barclays and an issue of Barclays ordinary shares to the holders of the RCI.) Each relevant Subscriber agreed to subscribe for the RCIs on the date falling three business days after the date such approvals were obtained; and

(4) In consideration for each relevant Subscriber's agreement to subscribe for the RCIs, BBPLC undertook to pay commission of 2% of the aggregate principal amount of RCIs to each of the relevant Subscribers on 27 November 2008. (For the avoidance of doubt, no commission or other amounts were paid by BBPLC to the Subscribers in respect of the RCI Subscription Agreements or the Warrant Subscription Agreements on 31 October 2008.)

28. Pursuant to the terms of the Warrant Subscription Agreements:

(1) Each relevant Subscriber's right to exercise the Warrants issued to it by Barclays was conditional on (amongst other things):

(a) obtaining the Requisite Shareholder Approvals; and

(b) BBPLC issuing the RCIs and receiving full payment in respect thereof in accordance with the relevant RCI Subscription Agreement.

(2) The Warrants were exercisable at any time during the period beginning when both (i) Barclays obtained the Requisite Shareholder Approvals and (ii) BBPLC issued the RCIs and received full payment in respect of them, and ending on 31 October 2013.

29. As between the Subscribers on the one hand, and BBPLC and Barclays on the other, the RCI Subscription Agreements and the Warrant Subscription Agreements were negotiated on arm's length terms.

30. On 31 October 2008 Barclays issued 1,516,875,236 Warrants for 1,516,875,236 ordinary shares in Barclays.

31. Barclays received the sum of £0.76 in respect of each of the Warrant Subscription Agreements (in total £1.52).

32. The exercise price for each of the Warrants was 197.775p which was equal to the average closing price of an ordinary share in Barclays as derived from the Daily Official List on 29 and 30 October 2008.

33. The total amount which would be payable by each relevant Subscriber upon exercise in full of their 758,437,618 Warrants was £1.5 billion.

Agreements with institutional investors

34. On 18 November 2008 Barclays announced that, following discussions with its institutional investors, each of the relevant Subscribers had agreed to make available to those institutional investors, in aggregate, £500 million of RCIs (without Warrants).

35. Consequently, on 18 November 2008:

(1) Qatar Holding, Barclays and BBPLC entered into a concession letter under which Qatar Holding agreed to make available up to £250 million in aggregate principal amount of the RCIs for which Qatar Holding had otherwise agreed to subscribe; and

(2) PCP 2, PCP 1, Barclays and BBPLC entered into a concession letter under which PCP 2 agreed to make available up to £250 million in aggregate principal amount of RCIs for which PCP 2 had otherwise agreed to subscribe.

36. Each of the relevant Subscribers retained an obligation to subscribe and pay for the RCIs made available to the institutional investors in the event that the institutional investors did not pay for those RCIs.

37. The full take-up of £500 million RCIs by institutional investors was confirmed on 19 November 2008.

Closing

38. The Requisite Shareholder Approvals for the capital raising were obtained on 24 November 2008.

39. On 25 November 2008, an application was made for each of the Warrants and the RCIs to be listed on the Official List of the London Stock Exchange.

40. BBPLC issued the RCIs on 27 November 2008.

41. On that date, BBPLC received a total of £3 billion (net of certain commissions) ("the Proceeds") as follows:

	£million
Qatar Holding	1,250
PCP 2 (funded by IPIC)	1,250
Institutional investors	500
Total Proceeds	3,000

42. Under the terms of the RCI Subscription Agreements BBPLC was beneficially entitled to the Proceeds. There was no agreement under which any part of it was to be held on behalf of Barclays, nor was any part of the proceeds paid up to Barclays.

43. By 13 February 2013 all of the Warrants had been exercised.

44. The RCIs were redeemed in full on 15 June 2019 at a price equal to 100 per cent. of their principal amount plus accrued but unpaid interest.

Accounting and valuation aspects

45. Barclays group accounts and the solus entity accounts for Barclays and BBPLC for their respective accounting periods ended 31 December 2008 were prepared using IFRS and audited by PWC.

46. For the purposes of those accounts, Barclays apportioned the Proceeds between the RCIs and the Warrants on the basis of their estimated fair values at the point of commitment, when the RCI Subscription Agreements and the Warrant Subscription Agreements were entered into, as derived by Barclays. (For the avoidance of doubt, HMRC does not agree with the fair values attributed by Barclays to either the Warrants or the RCIs in the relevant accounts.) Barclays assessed the fair value of the Warrants to be £800 million and the remaining £2.2 billion was taken as the fair value of the RCIs at the point of commitment.

47. The double entries in BBPLC's solus accounts for the accounting period ended 31 December 2008 in respect of the transactions relevant to this appeal were:

	£ million
Dr Cash	3,000
Cr RCIs	2,200
Cr Equity (capital contribution from Barclays)	800

48. Barclays recognised a capital contribution to BBPLC of £800 million in its accounts.

49. The double entries in Barclays solus accounts for the accounting period ended 31 December 2008 in respect of the transactions relevant to this appeal were:

	£ million
Dr Investment in subsidiary (BBPLC)	800
Cr Equity (Warrants)	800

50. For subsequent accounting periods BBPLC recognised the annual coupon on the RCIs of 14% (being £420 million per annum) as an expense in its Income Statement.

51. In addition, the £2.2 billion recognised by BBPLC in respect of the RCIs was accreted up to its par value and redemption amount of £3 billion over 10.5 years (the fixed interest rate period, as BBPLC expected that it would exercise its option to redeem the RCIs in full at par on 15 June 2019) via cumulative expenses in its Income Statement of £800 million, £7,253,036 of which ("the Accreted Debit") arose in the Relevant Period.

BBPLC's corporation tax return

52. In its corporation tax return for the Relevant Period, BBPLC brought the Accreted Debit into account as a loss arising to BBPLC from the RCIs. BBPLC did not bring into account any part of the £800 million credit to equity in respect of the capital contribution from Barclays mentioned at paragraph 47 above.

Further findings

53. We now turn to the findings of fact made by us. We first briefly note the context of the *PCP* case as described by Mr Justice Waksman.

54. In essence, the *PCP* case concerned the extent to which representations had been made by Roger Jenkins that the deal obtained by Abu Dhabi would be the same as that obtained by Qatar. It had been discovered that there had been a payment of £42m made by Barclays to Qatar in June 2008 and a further payment to Qatar of £280m made, or commencing, at the time

of the October financing. Each payment was expressed to be in consideration of various services to be provided by Qatar, set out in short letter agreements each described as an "Advisory Services Agreement" dated 25 June and 31 October 2008 respectively ("ASA 1" and "ASA 2"). Those sums were far in excess of the disclosed contractually agreed commissions payable to the investors on their subscriptions, which amounted to £62m so far as Qatar was concerned. A further payment of £66m to Qatar, described in the October capital raising announcement as a fee "for having arranged certain of the subscriptions in the Capital Raising" was also challenged. It was further discovered that Barclays had also provided a $3bn loan to Qatar drawn down on or about 17 November 2008 ("the Loan"). PCP alleged that Mr Jenkins had made false representations about the parity of Abu Dhabi's and Qatar's deals because in truth, the £280m payment and the £66m so-called arrangement fee were no more than disguised fees paid to Qatar by Barclays in exchange for its investment. Moreover, the Loan, although not a fee as such, was yet another benefit which Qatar had obtained and in truth formed part of its overall deal with Barclays.

55. We now consider the background and chronology of the RCI transactions in more detail.

56. It is a matter of accepted knowledge that in 2008 the financial crisis caused governments, regulators and banks to consider what steps were necessary to avoid a collapse of the international banking system. In the UK, there was concern at government level that the major clearing banks did not have sufficient Tier 1 capital.

57. Barclays did not wish to go the same way as HBOS/Lloyds and RBS in receiving a capital injection from the government. It considered that to be bailed out by the government would spell the end of its autonomy and quite possibly the end of the bank itself, at least in its present and contemplated future form. On any view, it was very determined to avoid a government bailout. How desperate it was to avoid a bailout was one of the key issues in *PCP*.

58. Barclays was in a somewhat different position from the other banks. Its Tier 1 capital adequacy was much stronger and as a result, there was the real possibility that it could raise the required additional capital privately i.e. by going to the market as opposed to being bailed out. Indeed, it had already raised £4.5bn in a capital raising in June 2008 ("CR1"), £2bn of which came from the State of Qatar.

59. On 8 October 2008 HM Treasury announced that the Government was bringing forward proposals to stabilise the financial system which were intended to provide sufficient liquidity in the short-term and make new capital available to UK banks. Barclays was one of the banks which confirmed their participation in the government supported recapitalisation scheme.

60. On the same day, Mr Jenkins spoke with Qatari representatives who were interested in investing as part of what became termed Capital Raising 2 ("CR2") in the sum of around £2bn and referred to doing a "Buffett deal" i.e. one which involved the provision of warrants.

61. On 13 October 2008, Barclays announced that it intended to raise in excess of £6.5 billion of additional Tier 1 capital, and that it expected that this would be raised from investors without calling on government funding. Barclays was still eligible to call on such funding if their plans did not materialise. The FSA, acknowledging that there was no need for an immediate bailout, had in fact given Barclays until 31 March (originally 30 June) 2009 to raise the requisite additional capital.

62. The plan, as approved by the FSA, envisaged the issue of £3bn worth of preference shares by 31 December 2008, the issue of £600m worth of new shares which had previously been announced on 17 September in relation to Barclays acquisition of Lehman Bros' American business, and the issue of a further £3bn worth of new shares with the intention that this should

be done before 31 March 2009. £1bn of this new capital was to come from an existing shareholder (in fact, Qatar).

63. The announced capital raising involved the issue of £3bn of preference shares together with the issue of new ordinary shares to raise a further £3 billion. The offer of the ordinary shares would be structured to give existing shareholders full rights of participation. It was stated that Barclays had agreement in principle with an existing shareholder to contribute £1 billion in new capital to be allocated between the preference shares and the ordinary shares.

64. Emails and a presentation document show that initially it was proposed that preference shares would be issued with related detachable equity warrants. That was Barclays preferred option at the time and one which had been adopted by Goldman Sachs. On 9 October 2008 an email from the managing director of Barclays EU Financial Institutions Group, Mr Boath, to the CEO of Barclays Wealth said that "in order to get them to play it would be necessary to offer them some warrants… It was agreed for now that we would suggest the package ... to Qatar with a warrant deal that would confer an implied value for the warrants of around £50 million. The coupon on the pref we would suggest would be circa 10% plus."

65. In an email dated 11 October 2008 from Mr Boath to the Group Finance Director of Barclays, he said that "we are unlikely to be able to raise £3-4 billion without offering accompanying warrants which are attractively priced. [It was] felt that a warrant package that was valued at the equivalent of an additional 2% or so running on the Pref coupon would be supportable. Our model indicates that a five year warrant struck at today's share price over the full notional of £3 billion would result in approximately 20% value (discount). This assumes 40% volatility and is equivalent to an additional 4% or so on the running cost of the Pref coupon. This was thought to be too high a premium for a "private deal"."

66. The presentation shows that at the time the issue price for those warrants was expected to be £1.

67. Minutes of the Barclays board show that on 13 October 2008 it was considered that the mood of the money markets had stabilised. The stock market had drawn a clear distinction between those banks taking government support and those not. The reference to the existing shareholder (Qatar) had been helpful.

68. The transactions between Barclays and the Subscribers were then the result of extensive arm's length negotiations between Barclays and the Subscribers' representatives.

69. Barclays was not forced to deal with the Subscribers or any other private investors: it could instead have called on government funding, but preferred not to do so.

70. On 13 October 2008, alongside the announcement of the capital raising, internal emails show that discussions were being held with a representative for Qatar in which RCIs were discussed. The Qatar representative indicated he would take £1 billion of RCIs along with warrants struck at the money exchangeable into £1 billion of common equity. In addition, Qatar would also acquire £500 million of "common equity".

71. Minutes of a Barclays finance committee meeting on 14 October 2008 show that it was considered by this stage that the RCIs would be more attractive to investors than preference shares as the coupon was cumulative and would be tax deductible for the group, thereby enabling a higher coupon to be paid. The option of attaching a warrant to the RCI was being investigated. RCIs without warrants would be expected to pay a coupon of 13-14% whereas those with a warrant would be expected to pay approximately 10%.

72. By 17 October 2008 John Varley was able to write to the directors to say that Qatar had agreed in principle to purchasing £1.5 billion of the £3 billion RCI issue together with £500 million equity at a later stage.

73. On 20 October 2008 an email to the representative of Sheikh Mansour described the RCI structure explaining that it was expected that the instrument would carry a coupon of 10% together with detachable warrants. In addition, it was also planned that RCIs without equity warrants would be issued which would be offered to both Qatar and Sheikh Mansour as well as institutional fixed income investors. Those RCIs would carry a coupon above 10% with the additional coupon reflecting the value of the warrants. Indeed, minutes of the Barclays board and the Appellant's board show that the preference was to issue vanilla RCIs with a coupon of 13 to 14%, although it was recognised that it was possible that investors may require warrants to be attached to them.

74. At around the same time there were internal emails produced in evidence in the *PCP* case which led to Mr Justice Waksman stating that as at 21 October 2008 Barclays' position was that they were moving towards an RCI no warrant deal so far as Qatar was concerned. Mr Justice Waksman goes on to say that on the other hand shortly after 23 October 2008 a presentation referred to each of Qatar and Abu Dhabi receiving £1.5 billion of warrants, but around that point internal Barclays emails showed Mr Justice Waksman that the Qataris were now asking too much, wanting to keep the coupon on the RCI at 14% and have the warrants. Barclays did not want to give them warrants and such a coupon.

75. Meanwhile Barclays board minutes for 21 October 2008 recorded the comment in recent publicity concerning the government's influence over those banks accepting government capital injections and the board's desire to be unconstrained by government involvement. In that same board meeting there was discussion about the proposed issue of £3 billion of RCIs, noting the preference that these would be "vanilla" with a coupon of 13-14%. At the same time discussions were noted as having continued about a fully underwritten rights issue alongside both the issue of RCIs to Qatar and certain institutional investors and an issue of up to £1 billion of warrants to Qatar together with an offering of up to £2.5 billion of warrants to the institutional investors who participated in the RCI issue. It was not said that the warrants would be issued for nominal consideration. The offer of warrants to institutions did not take place. Separate notes of the meeting show that the board considered that the warrants were "very precious" so that they would be guarded jealously.

76. On the same day the board of the Appellant met and the minutes are consistent in describing the preferred form of RCI issue as well as the proposals for the warrants and share issue described in the Barclays minutes.

77. On 22 October, Mr Boath, Mr Jenkins and others met with the Qatar representative. There was a presentation on what by now had become the RCIs and there was then a further discussion. The Qatar representative had been complaining that the Qataris had lost out over their investment in CR1 because they ended up paying almost all of their commitment and the Barclays share price had significantly dropped since then. By that stage, they were seeking a 14% coupon on the RCIs (which materialised) and a further total sum of £600m; Barclays had offered £120m.

78. Minutes of a Barclays board meeting on 22 October 2008 refer again to a proposed rights issue as well as the RCIs, stating that those instruments would not carry warrants but would have a 14% coupon.

79. On 23 October Mr Jenkins was told that PCP would require £3bn worth of warrants if it was to subscribe on behalf of Sheikh Mansour. In dealing with that, Mr Jenkins was said to have responded that if so, the warrants would have to be "split" between PCP and Qatar as that

would be the "rule". Later that day after meetings Mr Jenkins emailed other Barclays executives to say that the Qataris wanted to keep the RCI coupon at 14% and have warrants as well, which he said was too much of a premium over government yield and would be at a 17/18% cost.

80. On 24 October term sheets were sent out for the RCIs and warrants together with a further element – mandatorily convertible notes. The warrants at this point were three year warrants and the coupon on the RCIs was 14%. There were discussions about a possible fee being paid to Qatar described as not connected to the capital raising and the Qataris indicated they were walking away from the deal. However, negotiations continued with considerable discussion about the $3bn loan by Barclays to Qatar. For a while there was the potential of the Libyan Investment Authority subscribing, although by 31 October that body was out of the picture.

81. On 26 October 2008 an internal Barclays email shows that Qatar wanted five year warrants and in fact this had been sought by the Abu Dhabi representative a few days previously.

82. A Barclays board meeting on the same day describes Qatar and Abu Dhabi wanting to invest £6 billion in total with £3 billion of RCIs being issued with warrants attached. Separate notes from that meeting describe a good dialogue with institutions. The main reason for adding warrants to the RCIs was that it was felt that the addition had to be done; a "plain vanilla" RCI would not allow Barclays to achieve £3bn together with the mandatory convertible notes.

83. On 30 October 2008 Qatar raised the need to get a blended share price of 130p combining CR1 and CR2.

84. On the same day after much negotiation the $3bn unsecured Loan to Qatar was agreed by Barclays.

85. The RCI/MCN/Warrants deal was announced on 31 October 2008.

86. The Barclays announcement of 31 October 2008 described the capital raising as being effected through an issue of £3 billion of RCIs with an associated issue of warrants. This was then interpreted in a Merrill Lynch paper of 3 November 2008 as being an issue of the RCIs which came with warrants attached.

87. On 10 November Barclays institutional investors were expressing some discontent with the proposed deal as set out in the announcement, which meant that some adjustment to what Qatar and the PCPs were to receive had to be made to appease those investors. The eventual result was that Qatar and the PCPs agreed to release £250m worth of the £1.5bn worth of RCIs which they were each going to take. This would allow £500m worth of RCIs to be offered to institutional investors.

88. The institutional investors took up the offer. RCIs with a par value of £500 million were issued to them for £500 million.

89. Between 31 October and 20 November 2008 the Barclays share price dropped from 205p on 31 October 2008 at opening to 130p on 19 November 2008. On 31 October 2008 at close the share price had dropped from 205p to 179p.

90. Having regard to the chronology, the evidence of negotiations and expert valuation evidence, Mr Justice Waksman specifically found that:

(1) Barclays was desperate, in the sense that it would go to extraordinary and unusual lengths to bring about CR2, although he accepted that this did not mean at any cost whatsoever. He also accepted that there was the necessary hurdle of 75% of shareholder approval at the required EGM which had to be surmounted. There was a strong view that

taking government money would be very damaging to the bank and to the country in circumstances where, unlike other banks, a bailout was far from inevitable. In addition, key players at Barclays had justifiable concerns about their own futures - and bonuses - in the event of a bailout. There was also an element of personal ego so far as Mr Jenkins was concerned. This was important because while he could not himself sanction any particular deal with, for example, the Qataris, he was clearly highly influential at Barclays and was intent on doing whatever he thought should be done. He was also a risk-taker;

(2) Mr Jenkins himself said that no bank had any bargaining position of strength in October 2008 and the pool of investors was very very small. Moreover, while Barclays was given a six-month breathing space in order to raise the necessary capital, the fact was that Barclays had just done CR1 in June 2008 which had resulted in the Qataris subscribing for many more shares than they had anticipated because of a lack of interest in the "clawback" part of the deal by other shareholders. Moreover, the Qatari shareholders were now being challenged by the falling share price in October 2008. That explains the change in the Qataris' asked-for blended share price under CR1 and CR2 from 150p to 130p. They therefore had the motive and the bargaining power to demand a high price;

(3) effectively, whatever the Qataris demanded in terms of benefit to them (including ultimately £346m and a $3bn unsecured loan) they got;

(4) despite Barclays apparent protestations to the contrary, in the course of one meeting (23 October), those acting for PCP had been able to secure the issue of £3bn worth of Warrants with £1.5bn worth for the SPVs which had not been on the negotiating table up to that point. Despite pressure from Barclays, and an apparent agreement by the Qataris to make available some of the RCIs together with Warrants as a compensatory clawback to other shareholders, PCP held out against giving up the Warrants. In the end the bank agreed and the shareholder votes still went through;

(5) ASA2 under which Barclays agreed to pay Qatar 20 quarterly instalments of £14m was part of the mechanism to deliver to Qatar the blended price of 130p per share which it required before entering into the subscription. Any realistic appraisal of the events leading up to 31 October must conclude that the entering into the advisory services agreement was a real and absolute condition of Qatar entering into the subscription agreements for CR2;

(6) the Loan formed part of the price or consideration for the subscription which the Qataris sought and obtained;

(7) it was common ground that in practice there was no liquid market in which to trade the RCIs. That said, they proved popular with existing shareholders in CR2 who took up all of the £500m worth offered; this was no doubt at least in part because of the very attractive coupon;

(8) part of the reason why this was such an attractive deal was because of the five year Warrants and the prospect of large gains as a result of a significant increase in the share price over that period. That value was specifically recognised by Sheikh Mansour; and

(9) while the Warrants were in effect provided to the Subscribers free of charge, they were extremely valuable because of the fixed exercise price, at least if one took the view that Barclays share price would rise significantly above the current average closing price in the 5 years from issue.

Terms of the RCIs and Warrants

91. In addition to the agreed facts regarding the terms of the documents we find that the RCI Subscription Agreements ("RSAs") stated that:

(1) the issue price of the RCI's was 100%; and

(2) the RCIs were defined as £3bn 14 per cent Step up Callable Perpetual Reserve Capital Instruments of the Issuer. That same definition was included in the terms of the RCIs themselves and the Warrants.

The RCI Prospectus

92. The Prospectus states that the issue price was 100 per cent.

93. The Prospectus states that if the RCIs ceased to be eligible to qualify as Tier 1 Capital they may be substituted with qualifying Tier 1 instruments. There is no suggestion that only part of the amount paid for the RCIs would be eligible to qualify as Tier 1 Capital. (We address this further below in the context of correspondence with the Financial Services Authority.)

The Warrant Subscription Agreements

94. Each Warrant Subscription Agreement states that the consideration for the issue of the 758,437,618 Warrants is 76 pence.

The Warrant Prospectus

95. The Warrant issue price was stated to be 0.01 pence per 100,000 Warrants.

Reason for the structure and internal Barclays analysis

96. Although we did not have any witnesses attending to explain the structure we have been provided with the following description in a paper setting out the expected accounting treatment of the RCIs.

97. The paper describes the impact of an issue of warrants as being to reduce the nominal financing costs of the group of raising RCI funding. (As we explain below it was not considering the actual issue of the Warrants and RCIs as the assumed terms were different but the paper sheds light on why the two companies issued the two instruments.) It was noted that Barclays would not receive any immediate consideration, but BBPLC would have a reduced cost of funding. An alternative would have been for Barclays to have raised equity or to have raised the RCI funding with warrants and then contributed the funds to BBPLC. It was not practical for Barclays to raise RCI funding because of what was described as the "subordination issue" (the fact that debt in Barclays would be one step removed from BBPLC assets and costly). BBPLC's shares were not traded so the ability to issue a warrant with liquidity was not available to it.

98. The paper went on to conclude that both the warrants and the RCIs should initially be recognised at fair value, but in doing so it was considered that the coupon of the RCI was calculated such that the fair value of the RCIs together with the warrants was the same as the nominal value of the RCIs. Therefore an adjustment was necessary to allow Barclays to recognise the warrants at fair value and for BBPLC to recognise the RCIs at fair value with accretions of nominal value using effective interest. As the majority of the cash would be received by BBPLC the relative transfer of value should be treated as a capital contribution from Barclays to BBPLC.

99. There is no evidence of any consideration of the capital contribution by either the board of Barclays or BBPLC. Instead, it appears to have been a conclusion from the accounting analysis.

100. There is an internal Barclays presentation which considered the early plans for the capital raising and various options. That presentation focussed on a preference share issue or rights issue and noted that such a form of capital raising would enable "equity capital to be injected into BBPLC, benefitting solus ratios". However, that is some way from evidence that the Board of Barclays decided to make a capital contribution to BBPLC.

101. Notably, the accounting paper was produced prior to the actual transactions as it assumed that the RCI coupon would be 10% with the warrants having reduced the coupon by 2% to 3%. However, the actual transactions were significantly different in that the coupon of the RCIs was not reduced to take into account the value of the actual Warrants. As the findings earlier show, the Subscribers had been able to procure what they wanted and obtained the higher coupon on the RCIs together with the Warrants.

Comment at the time

102. On 3 November 2008 one journalist commented that the decision to raise £5.8 billion super expensively from the Middle East had inflicted a £2 billion cost on other shareholders. Part of that cost came from the "huge pile of warrants Barclays has given the Abu Dhabi and Qatari sheikhs... Using a standard Black-Scholes option model … each warrant is worth 50p. Given that there are 1.52 billion warrants, that's a £760 million hit."

103. In that same article it was commented that the next "hit" came from the "nosebleed price" that Barclays was paying on £3 billion of RCIs. The 14% coupon set for 10 ½ years was compared to the bailout offered by the UK government under which Barclays would have had to issue preference shares with a 12% coupon. While that coupon would not be tax deductible it was noted that the bank would have been able to pay those shares off as soon as it could raise the cash.

104. These costs (together with others such as the fees) were described as a "thwack" to other shareholders.

105. Similarly, a Merrill Lynch comment on 3 November 2008 described the Barclays transaction as a £3.2 billion opportunity cost for existing shareholders when compared with the UK government offer to underwrite a capital raising. That amount was calculated taking into account the cost of the Warrants issued as well as the longer term of the RCIs versus UK government preference shares. It was noted that the market capitalisation of Barclays fell by £2.2 billion after the deal was announced which Merrill Lynch thought suggested a discounting of this value transfer from existing to new shareholders.

106. RBS also commented on 4 November 2008 that the new capital transactions appeared to be expensive and the Warrants were seen as a one-way bet against existing shareholders.

107. Further market sentiment can be seen by the price of Barclays shares falling after the announcement (as we describe earlier).

Accounting treatment

108. We set out in some detail the record of a telephone conversation on 21 November 2008 (prior to the Requisite Shareholder Approvals and the issue of the RCIs) between Mr Boath and Jonathan Stone (Group Treasurer, Barclays Treasury):

> "JS: Sold a load of bonds. 500 million at 14 coupon. Quite an impressive performance when you couldn't sell them before at the same price […] The world's moved on. They see a different organisation…
>
> […] As this is an accounting geeky thing you'll say, "it's illogical John. It's all complete hogwash and bollocks" but it's reality for accountants […] we're disclosing the warrants at, say, an […] 800 value, RCIs at 220. Now you can

argue over the warrant value but, […] they're turning round and saying "Well how did you value the RCIs at the issue date on 31 October?" I said, "Well simply you took the warrant value and deducted it from the total proceeds". Oh you can't do that. That's not the right way to look at it. The question should be what would you have issued the warrants, the RCI at, on a stand-alone basis for the disclosure? They say, "[…] we need to get some support for what is the implied yield on the RCI when you issued it on 31 October" […] and my comment […] was "[…] there's no way to be able to use a market indication because […] there were no trades really in reality." The reality is that we know we went to the market with an RCI that had a coupon on it of 14%. When we first went to the market we went with a muted or soft sounding. We went with that with a 14% coupon […]

[…]

[…] were we talking warrants at the time of those to the investors

RB: No

[…]

JS: So we were talking without warrants […] we were talking to the market about doing an RCI at a coupon north of where the issue was being traded by the Government.

RB: And people were telling us that that would have to be around the 14%/15% coupon

[…]

JS: what will be the fair value of a stand-alone RCI without any knowledge of […] [what's] going on in the equity and the other components of the instrument.

RB: I don't know, there was no bid.

[…]

RB: The reality was that we couldn't issue RCI s at the time […] And what they were telling us was if you had all the other uncertainty around your capital plan resolved then the kind of […] coupon that we would expect for an issue that we would buy, or at least look at, would be 14% to 15%.

JS: Plus the fact you gave me some warrants as well, which have value too.

RB: No, because we never offered them any warrants

[…]

JS: Well this is where […] you have to suspend reality. On the one hand we're looking at where we're at 31 October and were saying we had warrants issued a below par. The problem is we also now have evidence that once all the equity's in place investors bought the RCIs 14% coupon at par. The reality is our [strategic investors] did not buy RCIs at par[…] they bought them 14% coupon plus warrants

JS: therefore if you take the warrant away what's the real value of the RCI?[..] You just take away the value of the warrant against it. That's what we've done.

[…]

JS: PWC are saying, "Oh well terribly sorry, […] but you can't do that. You've got to look at the stand-alone value of the RCI" […] I said, "Listen. I know it's going to be north of 14%. That's a certainty. Therefore while they

were issued with a 14 coupon they were not, probably, issued at par because fundamentally there was no bid"[...] It is bizarre the conversation we're having."

Financial Services Authority ("FSA") treatment of the RCIs

109. The RCI Prospectus, dated 25 November 2008, states at page 4 that:

> "On issue, the RCIs will qualify as Tier 1 Capital for the purposes of the Financial Regulator's capital adequacy regulations".

110. The Prospectus shows that it was approved by the FSA UK listing authority on 25 November 2008.

111. To qualify as Tier 1 Capital, there was a regulatory requirement that the RCIs were fully paid up. This requirement was stated in the version of the Financial Services Authority Handbook in force on that date, GENPRU 2.2.64, entitled "General Conditions for Eligibility as Tier 1 Capital". Rule 2 stated that:

> "The conditions that an item of capital of a firm must comply with under GENPRU 2.2.62R(2) are as follows: […] (2) it is fully paid and the proceeds of issue are immediately and fully available to the firm"

112. The Issue Price in the Circular of 7 November 2008, was stated to be 100 per cent. That was consistent with the FSA requirement as was the fact that the RCIs were clearly drafted to be issued at par. LR 13.2.1 of the FSA Handbook in force at the time stated that:

> "A listed company must not circulate or publish a circular unless it has been approved by the FSA".

113. Therefore we find that the Circular would have been approved by the FSA.

114. However, later correspondence with the FSA did not address the fully paid up requirement and put forward the description of the RCIs being shown in its accounts as having been issued for £2.2bn.

115. In November 2008 Barclays started correspondence with the FSA about the capital treatment of the RCIs and Warrants, explaining that in the accounts the RCIs would be shown as issued for £2.2 billion and the Warrants for £800 million on the basis that it was necessary to establish fair values of the instruments within the overall transaction price of £3 billion.

116. On 1 December 2008 the FSA challenged Barclays analysis of the transactions. The FSA queried in particular:

(1) the spreadsheet showing the value attributed to equity amortising down from £800 million to 0 after 10 years. The FSA asked why if the £800 million was a capital contribution it amortised; and if it was not permanently available it should not be treated as core Tier 1 capital;

(2) the FSA would expect the capital contribution from Barclays to be shown in its accounts as a reduction in its cash;

(3) the FSA's interpretation of IAS 32 was that the debt element should be valued first when apportioning the £3 billion and noted that a significant portion of the RCIs were sold to investors without warrants at the same coupon as those with warrants.

117. On 5 December 2008 the director of Barclays capital division replied to the FSA stating that:

(1) the RCIs were issued at a discount and £2.2 billion proceeds were received for them;

(2) while the RCIs were issued by the Appellant and the Warrants by Barclays "for convenience" the Appellant received all the proceeds. It was management's firm intention for Barclays to contribute the £800m payable for the Warrants to the Appellant as increased investment;

(3) only £2.2 billion, the fair value of the debt component at the issue date, would be included in capital initially. The accounting valuation, and therefore the regulatory capital valuation, of the RCI would increase to par over the period to redemption, recognising that it was issued at a discount;

(4) no RCIs were issued by Barclays without warrants as at the issue date. A number of them were sold subsequently by the holders in the secondary market a number of weeks later in different market conditions;

(5) the FSA interpretation of IAS 32 would only apply if a compound instrument had been issued but that was not the case here.

118. There are no board minutes or other internal papers to support the statement that it was management's intention for Barclays to contribute the £800 million as a capital contribution to the Appellant. There is no other witness evidence to that effect. Having considered the evidence of the phone call about the accounting treatment and the paper addressing the reasons for the structure we conclude that the capital contribution shown in the accounts arose from an accounting analysis rather than an active decision of Barclays to make it.

119. The statement made that no RCIs were issued by Barclays without Warrants is somewhat difficult to square with the fact that £500m of the RCIs were issued to the institutional investors. Mr Prosser submitted the statement made on 5 December 2008, when referring to the position on the issue date, meant the commitment date of 31 October 2008, but we find that such a reference back to 31 October 2008 is not apparent.

120. We have not been provided with the conclusion of the discussions between Barclays and the FSA. There appears to have been a meeting with the FSA but no note of it has been provided. Ultimately it appears that the FSA agreed to follow the accounting treatment but we do not have any witness or documentary evidence to explain how the regulatory requirements were navigated.

121. However, what is clear from the correspondence is that any agreement by the FSA to the capital treatment proposed by Barclays was on the basis of the accounting treatment described by Barclays and Barclays' interpretation of the apportionment of the £3 billion. It therefore adds little weight to BBPLC's claim that its accounting treatment shown in its audited accounts was correct.

Expert evidence

122. We have been provided with extensive expert accounting evidence which was explored in detail at the hearing. The experts have provided a joint report setting out those matters about which they are in agreement.

123. It is agreed that:

(1) The RCIs and RSAs should have been accounted for separately;

(2) The RSAs were loan commitments, but the parties' accounting experts disagree as to the date on which they became loan commitments. Mr Spooner's evidence is that they were loan commitments when they were entered into on 31 October 2008 whereas Mr Kusi-Yeboah says that the RSAs only became binding contracts when shareholder approval was obtained on 24 November 2008. However, BBPLC was not required to recognise the RSAs on 31 October 2008 or any other date thereafter;

(3) BBPLC was required to recognise the RCIs on balance sheet on 27 November 2008 and the RCIs should initially be recognised at fair value. However, the parties' accounting experts disagree about what that value is and when it should be assessed. Mr Spooner says that they should be assessed on the basis of their value as at commitment date i.e. 31 October 2008; whereas Mr Kusi-Yeboah says that a commitment date fair value policy is not compliant with IFRS and that an issue date fair value policy is required;

(4) the transaction price of £3 billion is an "entry price" as it is the price that was set when the agreement between the parties was entered into;

(5) the market for the RCIs was inactive on 31 October 2008 and 24 November 2008.

124. The experts do not agree as to whether in substance the £3bn was paid for the RCIs only or for the RCIs and the Warrants. Mr Spooner's view is that £3bn was paid for both the RCIs and the Warrants such that £800m should be treated as the value of the Warrants which means that the transaction price for the RCIs was in fact £2.2bn. He maintains that the transaction price is the best evidence of fair value unless there is evidence to the contrary and that there was no such evidence in this case. The transaction price was £3bn for the two instruments. Mr Kusi-Yeboah says that the correct initial measurement date for the RCIs is 27 November 2008 using fair value on that day and the best evidence of fair value was then the quoted prices.

125. The accounting experts do not agree whether it was in any event IFRS compliant to allocate the £3bn proceeds between the RCIs and the Warrants.

126. We have also been provided with extensive expert valuation evidence which was explored in detail at the hearing. That evidence is predicated on performing a valuation analysis of the RCIs and the Warrants for the purposes of ascertaining the fair values of those instruments as at 31 October 2008 and 27 November 2008. In particular, Mr Millar was instructed to proceed on the basis that the £3 billion was paid to BBPLC for both the RCIs and the Warrants from an accounting perspective. Mr Larrieu's instructions were different, but he was asked to assess the fair value of both the RCIs and the Warrants. We would only need to engage with their valuation conclusions if we decide that in fact the £3 billion was paid for both of the instruments although even then their ranges of valuations overlap significantly and indeed Barclays' own valuation of £800m falls within those ranges.

127. We have considered the expert evidence carefully. We take into account the opinions stated by the experts about whether the £3bn should in substance be treated as having been paid for the RCIs only or the RCIs and the Warrants. Mr Spooner sets out detailed arguments, but in summary the core of his view is that it is apparent from the terms of the instruments that both were related and that the Warrants had a value materially in excess of the contractual consideration of £1.52 such that the £3 billion should be treated as having been paid for both of them. We recognise these arguments in favour of an apportionment of the £3 billion, but ultimately it is a matter for us as the fact-finding tribunal to decide the facts in this case.

Secondary findings

128. The chronology set out above shows that the transactions were the result of extensive and, at times, fraught negotiations between Barclays and the Subscribers' representatives.

129. The RCIs and Warrants were negotiated as a "package deal". That "package deal" also included the mandatorily convertible notes, commissions/fees, ASAs and the unsecured Loan. Mr Prosser submitted that the other elements were irrelevant; neither side's experts had mentioned them and neither side argued that they were relevant to how the RCIs should be valued. In fact, Mr Milne and Ms Wilson's skeleton argument did refer to the whole package

in response to a submission made by Mr Prosser that the RCIs and Warrants were part of a "package deal". We are clear that it would be remiss of us to fail to take into account the overall deal negotiated.

130. Mr Prosser submitted that BBPLC was not seeking to argue that the value received for the RCIs should be reduced further from £2.2 billion to reflect the other value passed to Qatar. We agree that concluding simply that value was passed from Barclays to the Subscribers does not by itself mean that the RCIs should be treated as having been issued at less than their face value; and we would say that similarly this conclusion applies not only to the value passing in the form of the Loan and the ASA 2 fees, but also the Warrants.

131. There is little difference in the expert opinion as to the value of the Warrants at around £800 million on 31 October 2008 and indeed Mr Skailes' evidence in the *PCP* case was broadly consistent in estimating the value at around £860m. It is clear that the parties, including not only the investors but also Barclays, viewed the Warrants as a very valuable part of the package deal. However, the question for us is whether that value was, in essence, given away by the Barclays shareholders when the Warrants were issued for a nominal consideration, or whether the amount paid for the RCIs should be apportioned such that £800 million is allocated to the Warrants.

132. Mr Prosser submits that we should find that Barclays were not willing to give away the Warrants which were seen as valuable, or to issue them as an isolated deal for a nominal consideration. We agree that they were clearly not going to be issued in isolation for a nominal consideration; they were issued in the context of the overall package agreed with the Subscribers. However, the fact that they had value does not in itself mean that Barclays would not give them away as Mr Prosser urges us to conclude. That can only be determined looking at the negotiations and evidence overall. Of course, in substance it was the shareholders giving away the Warrants if we conclude that none of the £3 billion was in substance paid for them. To determine whether that is the correct conclusion we must consider the evidence beyond the mere fact that Barclays (as well as the investors) attributed value to the Warrants.

133. On this crucial matter we are, as Mr Milne submitted, particularly lacking the attendance of witnesses who could have addressed this very point. In the absence of such evidence, we come back to the documentary evidence we have described and to the judgment of Mr Justice Waksman who had the benefit of hearing evidence from some of those involved.

134. We consider it notable that at no point in any of the presentations, internal emails, board minutes and meeting notes is there any contemplation that the RCIs were issued for anything other than the £3 billion face value. Many of the papers assumed that the Warrants are attached to the RCIs, but at the end of the day, for the reasons we have identified from the documents, the RCIs and the Warrants were issued by different companies. A composite instrument was not issued (and for the avoidance of doubt, neither party has relied upon the accounting rules for composite instruments). The closest the documents at the time came to considering the RCIs as being seen as issued for below par was the Barclays internal accounting analysis paper described earlier. However, that was considering a notably different deal from the actual issue of RCIs and Warrants.

135. The Subscribers were invited to invest £3 billion and to receive either (i) "vanilla" RCIs carrying a higher coupon, or (ii) RCIs carrying a lower coupon with warrants "attached", on the basis that the value of the warrants equated to the additional coupon under (i). But the Subscribers rejected (i) and (ii), and instead insisted on making the same investment and receiving (iii) RCIs carrying a higher (14%) coupon with the Warrants as well.

136. Mr Prosser submitted that the issue of the RCIs and Warrants was a composite transaction as a matter of substance and economic reality relying, in particular, on the following facts:

(1) the RSAs and Warrant Subscription Agreements were entered into on the same day by related parties and in contemplation of each other;

(2) the Warrants had a value significantly in excess of £1.52 and that was recognised by the parties;

(3) the issue of both the RCIs and the Warrants was conditional on the same Requisite Shareholder Approvals;

(4) the exercise of the Warrants was dependent on the RCIs being issued and fully paid;

(5) the mandatory transfer provisions enabling Barclays to transfer the Warrants to a nominated person whereupon the exercise price would be market value such that the Warrants themselves would then have no value;

(6) the negotiations themselves showing that the RCIs and Warrants were seen as a package deal. The Subscribers declined the offer to subscribe for the RCIs with the higher coupon of 14% without the Warrants; and

(7) Barclays never offered the Warrants as an isolated deal.

137. While we are clear that the issue of the RCIs and the Warrants was, in substance, a composite transaction, in the sense that the Subscribers required both to be issued in order for the capital raising to proceed, that does not in itself mean that £800 million of the £3 billion must be allocated to the Warrants as a matter of economic substance. It is perfectly possible for there to have been a deal where the £800 million was effectively given to the Subscribers as part of the overall package in order for BBPLC to receive the £3 billion for the RCIs, despite the higher coupon. Indeed, there are other elements of the deal struck which gave value to Qatar in particular, such as the fees of £280m paid to Qatar under ASA2 and the unsecured $3 billion Loan. Those were extraordinary times and, as Mr Justice Waksman stated, whatever the Qataris demanded, they got. In that context another transfer of value of £400m worth of Warrants for Qatar is understandable and, indeed, consistent. But that begs the question as to who gave that value to Qatar.

138. We conclude as matter of fact that the £3bn was paid for the RCIs and the value in the Warrants was given away by the Barclays shareholders having regard in particular to the following:

(1) the starting point is the terms of the RCIs and the Warrants themselves. The RCIs are clearly written as debt instruments issued at par. The Warrants state a consideration of 76p paid by each of the Subscribers. There is no suggestion in the documents that the consideration for the Warrants was partly received through the payment for the RCIs;

(2) the institutional investors paid £500m for the RCIs issued to them at par value for £500m. The institutional investors did not receive any Warrants. We recognise that by the time the institutional investors subscribed, the perceived value of the RCIs would have changed given the commitment of the Subscribers (as explained to us by Mr Spooner and Mr Millar), but it remains the case that the institutions paid par value for notes issued at par value;

(3) the comment at the time was that the Barclays shareholders had taken a "thwack" as a result of the deal including giving away £800m of value. That sense was reflected in professional press comment and the drop in the Barclays share price on the announcement of CR2. Indeed, the issue of the Warrants cost Barclays nothing. It was the existing shareholders who were giving up value; their earnings per share would be reduced. This sense was reflected in the comment of Mr Justice Waksman, who, having

heard from some of those involved, said that the Warrants had been given away. We recognise that, as Mr Prosser submitted, Mr Justice Waksman was not considering the economic substance of the deal in the way that we are and made the comment having summarised the terms of the RCIs, Warrants and MCNs. However, Mr Justice Waksman specifically made his comment in the context of saying at the same time that the Warrants were extremely valuable if one took the view that Barclays' share price would increase in the next 5 years. Nowhere in the long, forensic judgment is there any suggestion that anyone regarded the RCIs as having been issued other than at par and Mr Justice Waksman's comment that the Warrants had been given away is consistent with the view of external commentators at the time;

(4) what Qatar wanted it got. These were extraordinary times. The Warrants were a part of what Qatar demanded just as the Loan and fees were. All were elements of the value demanded by Qatar to enable Barclays to raise capital. There was no indication in any of the documents that Qatar was perceived to be paying part of its £1.5bn for the value of the Warrants. Quite the reverse – the Warrants were held out to Qatar as having value such that the coupon on the RCIs could be reduced, but the Subscribers required the £3bn RCIs priced at a 14% coupon and the Warrants on top. As Ms Wilson submitted, to say that the Warrants had a value of £800 million and that the Subscribers paid £800 million for them would mean they were not getting a good deal and that the Warrants were not one of the sweeteners to get them to participate in the capital raising. Yet it is clear that the very real sense at the time was that the Subscribers had obtained very real value out of the deal, obtaining the Warrants without any compensating reduction in the RCI coupon. One could say that getting the Warrants was one of the conditions for them of subscribing for the RCIs;

(5) The idea that the Warrants should have value attributed to them from the RCI proceeds looking at the substance for Barclays and BBPLC had more basis when that was based on the Warrants enabling a lower coupon to be paid, as described in the reasons for structure paper. However, that fell away with the ultimate deal.

139. The particular facts and arguments weighing against this conclusion are that:

(1) the Warrants were seen as precious such that Barclays would not have given them away. We recognise that they had value but that in itself does not answer the question as to who was giving what value to whom;

(2) Legal form should not determine the economic substance which is what the accounting is required to reflect. We agree and have only viewed the legal form as the starting point;

(3) the internal Barclays structure paper showing that in order to raise the money via RCIs the notes had to be issued by BBPLC and the Warrants had to be issued by Barclays. We consider that is a potentially strong argument in favour of concluding that an overall deal of RCIs and Warrants issued for a combined value of £3bn was what was being considered and it was simply mechanics which split the £3bn in the way it was rather than issuing a combined instrument. However, that argument is weakened by the fact that the paper assumed that warrants would enable a lower coupon when in fact that did not occur;

(4) the auditors, PWC, approved accounts showing that the RCIs were issued for £2.2bn. However, we had no evidence from the auditors to explain on what basis that conclusion was reached. The evidence shows that PWC were asking for a standalone valuation of the RCIs rather than the approach of taking a value of £800m for the Warrants and deducting that from £3bn. How PWC were persuaded to change their view

we do not know. We have expert evidence addressing the accounting and valuation, but much of that evidence is predicated on the substance being that £3bn was paid for the RCIs and the Warrants. It therefore adds little to our fact finding as to what the £3bn was paid for;

(5) The RCIs and Warrants were two parts of a package for which £3bn was paid. Therefore in reflecting economic substance that £3bn must be apportioned. However, this begs the question: the package could be one where those paying the £3bn paid £3bn for the RCIs and nothing for the Warrants, or £2.2bn for the RCIs and £800m for the Warrants. Mr Prosser submitted that the package was analogous to a customer going to a car showroom and turning down a car priced £50,000 until the showroom offered three years free servicing. Then part of the £50,000 should be attributed to the value of the servicing. However, we consider that there is a fundamental difference here. The value is not given by the equivalent of the showroom (Barclays and/or BBPLC) but by the shareholders of Barclays if the Warrants are given away for no more than the £1.52 paid in substance;

(6) The reference in the note of a call between two Barclays personnel stating: "The reality is our strategic investors did not buy RCIs at par… They bought them 14% coupon plus warrants." (That reference to "strategic investors" is to the Subscribers.) However, it is a note of a call between two people neither of whom were before us to have that evidence properly explained or tested in cross examination. Jonathan Stone was Group Treasurer but not one of those negotiating the transactions or attending the Board meetings of BBPLC or Barclays. He sees £3bn received from the Subscribers who had received RCIs and Warrants and is considering how to account for the transactions. His view that the Subscribers did not buy the RCIs at par is one view that has not been tested in any meaningful way;

(7) Mr Prosser submits that another analogy should be drawn to the facts in the case of *Marks & Spencer plc v HMRC* [2019] UKUT 182. That concerned the promotional offer run by Marks & Spencer ("M&S") allowing a customer to choose three food dishes for £10 and obtain a bottle of wine for "free". He submits that thinking of the Warrants as being issued for "free" runs into the same issues. One of those would be to rely on the fact that institutions purchased RCIs without Warrants at par. In the *Marks & Spencer* case some customers bought the food and did not take up the wine offer. The Upper Tribunal decided that the economic and commercial reality was that M&S was offering a package of four items and the word "free" was used in a promotional sense. The £10 had to be allocated across all four items. However, we consider that *Marks & Spencer* has little bearing here. As Mr Milne and Ms Wilson submit, it concerned the VAT rules and in particular the specific EU meaning of "consideration" (at [100]). The conclusion that the £10 was allocated across all four items also avoided untaxed consumption of wine on which M&S had claimed input tax (at [107]). It is also an attempted comparison which ignores certain key elements in this case: Barclays were not offering a customer an ability to choose a package; it was faced with the need to raise Tier 1 capital and the only way in which it could do so without resorting to government funding was to agree to give the Warrants to the Subscribers even though it had hoped only to do so as a way of reducing the coupon on the RCIs. Again, the comparison to *Marks & Spencer* ignores the fact that the value in the Warrants was not value moving from Barclays – it was a cost borne by the Barclays shareholders.

140. Therefore considering our findings overall and the strength of the factors leading to a conclusion that the £3bn was paid for the RCIs alone, these contrary arguments are insufficient

to conclude that BBPLC has shown that part of the £3bn should be viewed in substance as having been paid for the Warrants.

Consequent accounting

141. On the basis of the facts we have found, Mr Spooner's opinion is that the fair value (as defined in IAS 39) of the RCIs as at 31 October 2008 is the transaction price agreed by the parties i.e. £3 billion. Mr Kusi-Yeboah said that the transaction price does not represent the fair value of the RCIs and BBPLC would be required to establish that fair value by using other valuation techniques.

142. We find Mr Spooner's evidence on the way to apply IAS 39 to be preferable not least because it has the significant attraction of recognising the transaction price rather than requiring some other market valuation.

143. However, in any event Mr Kusi-Yeboah's opinion is that valuing the RCIs at fair value as at 27 November 2008 would produce a value of at least £3 billion such that there is no accruing discount. We therefore do not need to address the valuation issue further.

144. We also do not need to engage further with the detailed arguments about commitment date and issue date accounting.

AGREED ISSUES

145. The parties have agreed that the appeals raise the following issues.

146. References below to statutory provisions are to provisions of Chapter II of Part IV of the Finance Act 1996, the corporation tax loan relationships legislation in force during the Relevant Period.

147. It is common ground that:

(1) the RCIs are loan relationships of BBPLC as defined by section 81,

(2) accordingly, by section 85A BBPLC is required to bring into account for the Relevant Period the credits and debits that, in accordance with generally accepted accounting practice (including IFRS), are recognised in determining its profit or loss from the RCIs for the Relevant Period,

(3) but this is subject to section 84(1)(a) which provides that the credits and debits to be brought into account are the sums which when taken together "fairly represent", for the Relevant Period, all profits, gains and losses (disregarding interest) arising to BBPLC from the RCIs.

148. The issues in this appeal are whether:

(1) as BBPLC contends:

(a) its solus accounts (the Accounts) were compliant with IFRS in bringing the RCIs into account at their fair value as at 31 October 2008 (the Commitment Date) and also in assessing their fair value as at that date at £2.2 billion;

(b) the Accreted Debit "fairly represents" the losses (disregarding interest) of BBPLC in respect of the RCIs for the Relevant Period; and

(c) the Accounts do not recognise the credit to equity referred to in the Agreed Facts (the Credit to Equity) as a profit arising to BBPLC from the RCIs, and the Credit to Equity does not "fairly represent" a profit arising to BBPLC from the RCIs;

(2) or as HMRC contend:

(a) the Accounts did not comply with IFRS: if they had done so they would have brought the RCIs into account at their fair value as at 27 November 2008 when they were issued (the Issue Date) and assessed their fair value as at that date at least £3 billion, with the result that they would not have recognised any losses (disregarding interest) as arising to BBPLC from the RCIs for the Relevant Period;

(b) alternatively, even if the Accounts did comply with IFRS, they would also have done so if they had brought the RCIs into account as mentioned in (2)(a), and only the latter treatment would "fairly represent" the losses (disregarding interest) arising to BBPLC from the RCIs for the Relevant Period;

(c) in the further alternative, even if the only accounting treatment compliant with IFRS was the actual treatment in the Accounts, the Accreted Debit does not "fairly represent" the losses (disregarding interest) arising to BBPLC from the RCIs for the Relevant Period; and

(d) in the yet further alternative, even if the only accounting treatment compliant with IFRS was the actual treatment in the Accounts, and the Accreted Debit does "fairly represent" the losses (disregarding interest) arising to BBPLC from the RCIs for the Relevant Period, the Credit to Equity "fairly represents" a profit arising to BBPLC from the RCIs for the Relevant Period.

(3) The fair value of the RCIs as at the Commitment Date and the Issue Date is not agreed and is a matter for expert evidence.

THE PARTIES' CASES

149. We heard extensive submissions from both parties, but it would be otiose to set them out in this decision. At their heart the core dispute is whether the £3bn was paid for the RCIs alone and/or should be treated in the accounts as having been.

THE LAW

150. The applicable provisions are not in dispute.

151. Section 80(1) FA 1996 provides:

> (1) For the purposes of corporation tax all profits and gains arising to a company from its loan relationships shall be chargeable to tax as income in accordance with this Chapter."

152. Section 84(1)(a) provides:

> (1) The credits and debits to be brought into account in the case of any company in respect of its loan relationships shall be the sums which, when taken together, fairly represent, for the accounting period in question-
>
> (a) all profits, gains and losses of the company, including those of a capital nature, which (disregarding interest and any charges or expenses) arise to the company from its loan relationships and related transactions".

153. Section 85A(1) provides:

> (1) Subject to the provisions of this Chapter (including, in particular, section 84(1)), the amounts to be brought into account by a company for any period for the purposes of this Chapter are those that, in accordance with generally accepted accounting practice, are recognised in determining the company's profit or loss for the period."

154. Section 85A(2) provides:

> (2) If a company does not draw up accounts in accordance with generally accepted accounting practice ("correct accounts") –
>
> (a) the provisions of this Chapter apply as if correct accounts had been drawn up, and
>
> (b) the amounts referred to in this Chapter as being recognised for accounting purposes are those that would have been recognised if correct accounts had been drawn up.

155. Section 85B(1) provides:

> (1) Any reference in this chapter to an amount being recognised in determining a company's profit or loss for a period is to an amount being recognised for accounting purposes-
>
> (a) in the company's profit and loss account or income statement,
>
> (b) in the company's statement of recognised gains and losses or statement of changes in equity, or
>
> (c) in any other statement of items brought into account in computing the company's profits and losses for that period.

156. Amounts recognised in any of the GAAP-compliant statements mentioned in section 85B(1) are, without more, "profits" or "losses" as the case may be for the purposes of section 84(1)(a): *The Union Castle Mail Steamship Co Ltd v HMRC* [2020] EWCA Civ 547 at [38].

157. In *Union Castle* Lord Justice David Richards made clear that the question before the Court of Appeal in that case was whether Parliament had "surrendered to accountants" the determination of the taxable profits and allowable losses arising from derivative contracts. (The legislation dealing with the taxation of derivative contracts has the same "fairly represents" test and in *Union Castle* it was accepted at [41] that for the purposes of the "fairly represents" requirement there was no relevant distinction between the loan relationship code and the derivatives contracts code.)

158. The Court of Appeal focused on the equivalent wording to that contained in s80 and s84 which identifies the profits and losses arising to the company from what was in the *Union Castle* case the derivative contracts and in this case would be the loan relationships.

159. At [51] Lord Justice Richards said:

> The true and fair or fair presentation "override" forms part of GAAP. It involves a departure from a particular accounting standard but not a departure from GAAP. By contrast, where applicable, the statutory "fairly represent" requirement in paragraph 15(1) does mandate a departure from GAAP.

160. Therefore accounts may be prepared on the basis of providing a true and fair view, but the "fairly represents" requirement, where applicable, mandates a departure from the GAAP compliant accounts. Lord Justice Henderson went on to explain that the purpose of accounting standards may not always match the purpose of determining profits and losses for tax purposes. It was for this reason that the "fairly represents" requirement is included in the legislation.

DISCUSSION

161. We have found that the £3bn was paid for the RCIs and not for a package of RCIs and Warrants. We have also relied upon the expert accounting evidence to conclude that the BBPLC accounts should have recognised £3bn as the amount received for the RCIs and shown that value in their accounts. Accordingly there should have been no Accreted Debit and no loss arising in relation to that loan relationship under the loan relationship rules in Chapter II of Part IV of the Finance Act 1996.

162. However, we have also considered the position were it to be concluded that the £3bn should have (or could have) been allocated to the Warrants as well as the RCIs under GAAP.

163. We agree with Mr Prosser's submission that *Union Castle* makes clear that the amounts shown in GAAP compliant accounts are the starting point. However, given our findings, we agree with the position articulated by HMRC in their review letter that such a result could only have been because the transactions were viewed overall on some group basis looking at the money received and the value given away by the group (or, given our findings, more particularly, its shareholders).

164. At this point we move on to address the "fairly represents" requirement in s84(1)(a) as Mr Prosser agrees we should.

165. BBPLC accepts that the "fairly represents" requirement in s.84(1) is a separate and potentially overriding condition which has to be satisfied once the initial computation in accordance with GAAP has been performed: *GDF Suez Teeside Ltd v HMRC* [2018] EWCA Civ 2075 at [43]. The fairness requirement is not limited to situations involving tax avoidance, asymmetry of tax treatment, or situations of manifest absurdity. It is engaged whenever fair representation would not otherwise be achieved: *HMRC v Smith & Nephew Overseas Ltd* [2020] EWCA Civ 299 at [42].

166. In *Union Castle* Lord Justice Richards made the purpose of the "fairly represents" test clear: in short, the purpose of accounting standards may not always match the purpose of determining profits and losses for tax purposes.

167. Mr Prosser submits that BBPLC's accounts do fairly represent the economic substance of the transactions. They represent a real economic loss suffered by BBPLC in relation to the RCIs. That therefore means that the "fairly represents" test is satisfied.

168. However, we agree with HMRC's position that it is wrong to view BBPLC's profits or losses for tax purposes from the perspective of commercial substance at a group level. The tax position of BBPLC must be determined on the basis of the company alone. The loan relationship rules do not permit consideration of a wider group perspective or the overall economic effect on the group. BBPLC received £3 billion for the issue of the RCIs with no obligation to account for any of that amount to Barclays. It issued the RCIs at par, received £3bn and then repaid £3bn.

169. Therefore even if the accounts can show £2.2 billion as the value of the RCIs when issued under GAAP, the Accreted Debit in BBPLC's accounts does not "fairly represent" losses arising to BBPLC from the RCIs under s84.

170. As a result the same conclusion would be reached by us that there is no loss arising to BBPLC from the RCIs under the loan relationship rules even were we to accept that the accounts were GAAP compliant in showing that only £2.2bn was paid to BBPLC for the RCIs on issue.

171. Given these conclusions we have decided that any further consideration of the other agreed issues would be entirely academic. In particular, we note that HMRC only seek to argue that the £800m capital contribution would be taxable under the loan relationship rules should it be concluded that the Accreted Debit fairly represented losses in respect of the RCIs.

CONCLUSION

172. We therefore conclude that the Appellant's appeal of HMRC's conclusion and amendments contained in a Closure Notice issued on 3 October 2016 under paragraph 32 Schedule 18 Finance Act 1998 in relation to BBPLC's tax return for the Relevant Period in respect of deductions claimed in respect of the RCIs is dismissed.

RIGHT TO APPLY FOR PERMISSION TO APPEAL

173. This document contains full findings of fact and reasons for the decision. Any party dissatisfied with this decision has a right to apply for permission to appeal against it pursuant to Rule 39 of the Tribunal Procedure (First-tier Tribunal) (Tax Chamber) Rules 2009. The application must be received by this Tribunal not later than 56 days after this decision is sent to that party. The parties are referred to "Guidance to accompany a Decision from the First-tier Tribunal (Tax Chamber)" which accompanies and forms part of this decision notice.

JUDGE TRACEY BOWLER
TRIBUNAL JUDGE

Release date: 26th April 2024