

Scottish & Northern Ireland Banknote Issuance Annual Report 2023

Report on the Bank of England's work under the Scottish & Northern Ireland Banknote Regulations 2009



Executive Summary

- Six commercial banks in the United Kingdom are authorised to issue their own banknotes, three in Northern Ireland and three in Scotland (the “authorised banks”). The six banks are required to hold ring-fenced assets that back their note issuance at all times. The aggregate backing requirement of the authorised banks at end-February 2023 was £7.83 billion, a decrease of 3.9% from £8.15 billion in 2022¹.
- At end-February 2023, the authorised banks in Scotland had an aggregate backing requirement of £5.33 billion, comprising £5.21 billion of Notes in Circulation and £0.12 billion of Notes with the Potential to Enter Circulation (as defined in paragraph 11). The authorised banks in Northern Ireland had an aggregate backing requirement of £2.5 billion, comprising £2.31 billion of Notes in Circulation and £0.19 billion of Notes with the Potential to Enter Circulation.
- The Bank of England (“the Bank”) is responsible for the regulation of note issue by the six authorised banks. The Bank undertakes a range of supervisory and compliance activity throughout the year and analysis of daily regulatory reporting provided by all authorised banks. Where regulatory requirements were not met during the period, the Bank conducted an investigation and remedial actions were agreed with the authorised banks.
- There was a satisfactory level of compliance with the regime during the year to end-February 2023. During the twelve month period, the Bank assessed two ‘Notable’ compliance failures, however there were no ‘Serious’, or ‘Underbacking’ compliance failures (the categories of failures are defined in the Statement of Penalty Policy (“SPP”)).²

¹ A seventh bank “AIB Group (UK) plc” was an authorised bank in Northern Ireland until 30 June 2022 and is included in the figures for 2022, see paragraph 5.

² <https://www.bankofengland.co.uk/-/media/boe/files/banknotes/scottish-northern-ireland/scottish-and-northern-ireland-statement-of-penalty-policy-2018.pdf>

Introduction

1. The Bank assumed responsibility for the regulation of note issue by the six authorised banks on 23 November 2009.
2. Regulation 18 of the Scottish and Northern Ireland Banknote Regulations 2009 (“the Regulations”) requires the Bank to publish an annual report on the discharge of its functions under the Regulations. This is the fourteenth such report and covers the Bank’s activities from 1 March 2022 to 28 February 2023 (the Bank’s 2022/23 financial year).

Historical background

3. The six authorised banks (or their predecessors) have been regulated with regard to the backing of their banknotes since 1845. Part 6 of the Banking Act 2009 (“the Act”), which came into effect on 23 November 2009, repealed the legislation under which banknote issuance in Scotland and Northern Ireland was previously regulated and passed the responsibility for regulation to the Bank. Part 6 of the Act updated and modernised the framework for commercial note issuance to provide enhanced noteholder protection.

4. The authorised banks are:

- Bank of Ireland (UK) plc;
- Bank of Scotland plc;
- Clydesdale Bank plc;
- Northern Bank Limited (trades as Danske Bank in Northern Ireland);
- The Royal Bank of Scotland plc; and
- National Westminster Bank plc (trades as Ulster Bank in Northern Ireland).

5. In addition to the above, AIB Group (UK) plc (previously trading as First Trust Bank in Northern Ireland) (“AIB”) was an authorised bank until they voluntarily ceased issuance on 30 June 2020. AIB were required to continue holding Backing Assets (as defined in paragraph 11) for two years. From 1 July 2022, the S&NI Regulations and Rules ceased to apply to AIB. Holders of First Trust banknotes can still exchange them with AIB³.

Legislative framework

6. The Act and the Regulations set out the framework for the Bank’s responsibilities for regulating the authorised banks’ note issuance. The primary objective of the legislation is noteholder protection. The provisions in the legislation are designed to ensure that holders of genuine banknotes issued by the authorised banks receive a level of protection similar to that provided to holders of Bank of England notes, through the full backing of notes at all times (see Noteholder Protection section below for more detail). The

³ See AIB Group (UK) plc’s website (aibni.co.uk/banknotes) for further details on exchanging their banknotes.

Bank is not responsible for the design of the authorised banks' banknotes or their robustness against counterfeiting.

7. The authorised banks' note issuance is governed by the Act, the Regulations and the related Scottish and Northern Ireland Banknotes Rules ("the Rules"). These came into force in November 2009 together with a Statement of Penalty Policy ("the SPP"). Both the Rules and SPP are revised periodically; the current Rules have been in effect since April 2017 and the current SPP has been in effect since August 2018.

8. In addition, the authorised banks must comply with conditions, known as General Conditions and Specific Conditions that set out the requirements for the holding of backing assets and Excluded Notes (see Noteholder Protection section below for more detail). As the General Conditions and Specific Conditions include sensitive material, such as the security standards that sites holding backing assets must meet, they are not published.

9. The Bank has the authority to impose financial penalties on the authorised banks for non-compliance with the Regulations and the Rules.

Noteholder protection

10. Under the Regulations, the authorised banks are required to hold backing assets for their notes at all times. In the event of an authorised bank entering an insolvency process as defined in the Regulations, those assets will be ring-fenced for one year or any longer period that HM Treasury may determine after consulting the Bank, for the sole purpose of reimbursing noteholders through a note exchange programme.

11. To back their note issue, authorised banks may use a combination of Bank of England notes, UK coin and funds placed on deposit in sterling in an interest bearing bank account at the Bank. Bank of England notes held as backing assets may be held at locations approved by the Bank or at the Bank. Notes held as backing assets at the Bank may include £1 million notes (Giants) and £100 million notes (Titans), which in physical terms are permanently held at the Bank.

12. For the purpose of backing requirements, notes issued by an authorised bank are always considered to be one of three mutually exclusive classes, as set out below.

- **Notes In Circulation ("NIC"):** notes that have been issued by the authorised bank and are now in general circulation, e.g. notes in wallets and purses.
- **Notes With the Potential to Enter Circulation ("NWPEC"):** notes that are held by or on behalf of the authorised banks but which are available to be issued, e.g. notes held in ATMs or in bank branches.
- **Excluded Notes:** notes which do not need to be backed. These notes are held by or on behalf of the authorised banks, which fulfil specific requirements and conditions (the General Conditions and Specific Conditions) imposed by the Bank, e.g. are stored in a banknote cage in a secure vault.

This includes notes which have been printed but which have not yet been collected from the printer.

13. NIC and NWPEC must be fully backed with backing assets. At least 60% of NIC must be backed by backing assets in the form of Bank of England notes or UK coin. The remaining 40% of NIC and 100% of NWPEC must be backed by backing assets in the form of Bank of England notes, UK coin, or funds placed on deposit in sterling in an interest-bearing account at the Bank. Excluded Notes are not required to be backed.

14. At end-February 2023, the aggregate NIC and NWPEC of all six banks was £7.52 billion and £0.31 billion respectively. As a consequence, the total backing requirement of all six banks was £7.83 billion, the breakdown of which is shown in Table 1, a decrease of 3.9% from £8.15 billion in 2022. In comparison, Bank of England NIC decreased from £81.63 billion to £81.26 billion in the same period, a decrease of 0.5%.

15. **Table 1** Breakdown of backing requirement and comparison with previous year

	28 February 2023	28 February 2022
Scotland authorised banks	£5.33 billion	£5.48 billion
<i>NIC</i>	<i>£5.21 billion</i>	<i>£5.33 billion</i>
<i>NWPEC</i>	<i>£0.12 billion</i>	<i>£0.15 billion</i>
Northern Ireland authorised banks	£2.50 billion	£2.67 billion
<i>NIC</i>	<i>£2.31 billion</i>	<i>£2.48 billion</i>
<i>NWPEC</i>	<i>£0.19 billion</i>	<i>£0.19 billion</i>
Aggregate backing requirement	£7.83 billion	£8.15 billion

16. Over the twelve-month reporting period the average NIC of the authorised banks decreased from £8.02 billion to £7.64 billion⁴. In comparison, the average NIC of Bank of England notes decreased from £82.56 billion to £82.47 billion in the same period.⁵

Compliance framework

17. The Bank has a small team of staff within its Notes Directorate to monitor compliance with the regime. The team analyses the daily and weekly data reported by the authorised banks to ensure that both the total value and the composition of backing assets held are at all times in accordance with the legislation. The Bank undertakes a range of other supervisory and compliance activity throughout the year, including checks to verify the value of backing assets and Excluded Notes held, and to confirm that the necessary conditions (e.g. security standards of sites storing backing assets and/or Excluded Notes) are met. The Bank regularly re-evaluates its supervisory activity to ensure that risks to noteholders are adequately mitigated.

⁴ Includes NIC of AIB Group (UK) plc between 1 March and 30 June 2022

⁵ Bank of England figures do not include Giants and Titans, see paragraph 11.

Compliance failures and penalties

18. During the year to end-February 2023 the Bank did not impose any financial penalties. Two Notable compliance failures were assessed. Neither of these failures were considered serious enough to justify referral to the Bank's internal decision-making committees and both were laid on file for future reference. The Bank can also issue a Private Warning for a Minor or, in exceptional circumstances, a Notable compliance failure; however these are not included in the Annual Report.

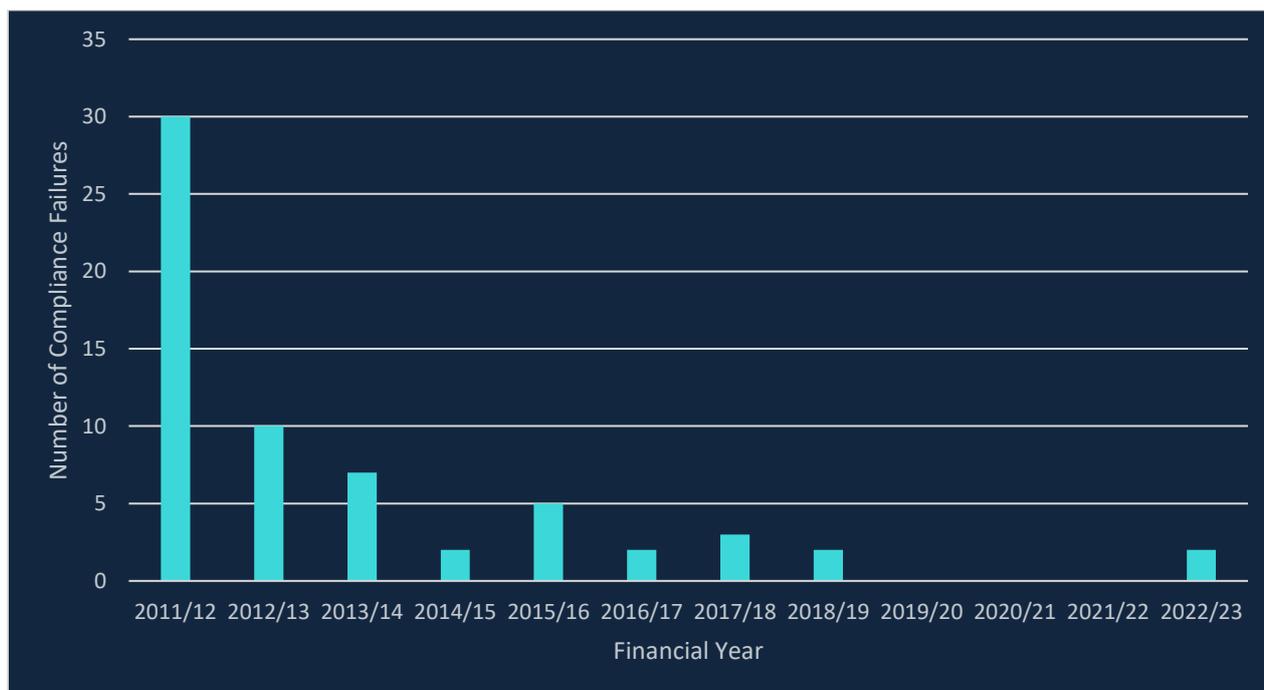
19. As shown in **Table 2** and **Chart 1**, the number of assessed compliance failures has decreased significantly since the start of the regime.

20. Between the commencement of the regime and end-February 2023, 28 compliance failures have been penalised, and penalties amounting to £119,700 have been issued and paid.⁶ No penalties were issued in the year to end-February 2023. Once received, penalties are passed to HM Treasury.

Table 2 Number of compliance failures assessed

Number of compliance failures	2011 /12	2012 /13	2013 /14	2014 /15	2015 /16	2016 /17	2017 /18	2018 /19	2019 /20	2020 /21	2021 /22	2022 /23
Investigated by the Bank's Committees (of which penalised)	4 (2)	3 (1)	2 (2)	0 (0)	1 (1)	0 (0)	1 (1)	1 (1)	0 (0)	0 (0)	0 (0)	0 (0)
Laid on file	26	7	5	2	4	2	2	1	0	0	0	2
Total	30	10	7	2	5	2	3	2	0	0	0	2

Chart 1 Assessed compliance failures by date: March 2009 – February 2023



⁶ Penalties are published in this Annual Report in accordance with Regulation 16 of the Scottish and Northern Ireland Banknote Regulations 2009.

Note: Reporting periods align with the Bank's financial year, which runs from 1 March. Any compliance failures in the process of being assessed at the end of the reporting period are shown as occurring in the subsequent financial year.

Other developments

21. On 30 June 2020, AIB ceased issuing its own banknotes in Northern Ireland, and now dispenses Bank of England banknotes through its branch and ATM network. From 1 July 2022, the S&NI Regulations and Rules ceased to apply to AIB.

22. As part of wider contingency preparations in 2022/23, the Bank participated in a business continuity exercise with the authorised banks, which was focussed on a scenario involving a cyber-attack.

Appendix 1: Legislative Documents

- The Banking Act 2009, Part 6 (“the Act”), which received Royal Assent in February 2009 and came into force on 23 November 2009.
(http://www.opsi.gov.uk/RevisedStatutes/Acts/ukpga/2009/cukpga_20090001_en_1).
- The Scottish and Northern Ireland Banknote Regulations 2009 (“the Regulations”), which were made by Parliament on 18 November 2009 and came into force on 23 November 2009.
(http://www.opsi.gov.uk/si/si2009/pdf/uksi_20093056_en.pdf).
- The Scottish and Northern Ireland Banknote Rules (“the Rules”) 3 April 2017
(<https://www.bankofengland.co.uk/-/media/boe/files/banknotes/scottish-northern-ireland/scottish-and-northern-ireland-banknote-rules-2017.pdf>).
- The Scottish and Northern Ireland Banknote SPP 28 August 2018
(<https://www.bankofengland.co.uk/-/media/boe/files/banknotes/scottish-northern-ireland/scottish-and-northern-ireland-statement-of-penalty-policy-2018.pdf>).
- The Scottish and Northern Ireland Banknote Approach Document March 2017
(<https://www.bankofengland.co.uk/-/media/boe/files/banknotes/scottish-northern-ireland/scottish-and-northern-ireland-regime-approach.pdf>).