

**Statement of Marty Malloy
Barclays Managing Director**

**U.S. Senate
Permanent Subcommittee on Investigations
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Good Morning. I am Marty Malloy, and I currently serve as Managing Director and Head of Barclays' European Prime Services unit. From 1998 to 2008, I headed the equity finance team of Barclays' Prime Brokerage group. In this capacity, I oversaw the execution of the Colt transaction with Renaissance Technologies. In the last eighteen months, I have met with the Subcommittee staff on several occasions in an effort to assist your review and analysis of the Colt transactions, and I am here today as a further continuation of my and Barclays' cooperation.

Barclays and Renaissance first entered into the Colt transaction in the fall of 2002. Renaissance, a highly sophisticated, well-regarded, and extremely successful hedge fund, was already a customer of the Bank at that time. Renaissance proposed aspects of a structure that ultimately became Colt in connection with ongoing discussions regarding potentially expanding its business relationship with Barclays. Over the past twelve years, Barclays and Renaissance have entered into a number of Colt options.

The mechanics of the options can be summarized as follows:

- Barclays sells to a Renaissance subsidiary (Badger) a series of cash-settled options, which reference a basket of securities held by a wholly-owned subsidiary of Barclays (Palomino).
- The basket (also known as the reference portfolio) was funded by Barclays from the funds received from Renaissance as the premium for the options, plus the leverage financing provided to Palomino by Barclays.
- Renaissance determines the composition of the basket and the overall investment strategy, pursuant to an Investment Management Agreement, and subject to numerous limitations in that document.

- Renaissance employs a “statistical arbitrage” investment strategy, and utilizes the buying and selling of both long and short positions.
- Any income derived from the investment activity in the reference portfolio accrued to Palomino.
- Each time Renaissance elected to exercise an option, the value was determined by reference to the value of the Palomino portfolio.
- Originally, these options had a maximum period of three years and more recently they have had a maximum period of eleven months.

This was a commercial transaction from which Barclays earned fees in a number of ways. On options trades like this one, the Bank realizes income from the spread on our execution of our principal trades. Additionally, Barclays benefited from being able to both pledge as collateral and lend out the securities held by Palomino.

Before putting on the first Colt option, Barclays subjected the transaction to an extensive internal review process and consulted with both internal and external regulatory and tax experts. The extensive governance and approval process employed both at the early stage of this transaction, as well as when subsequent options were considered and approved, will be discussed further by my colleague, Gerard LaRocca, in his testimony.

While Renaissance has a stellar track record and reputation as an investment manager, the Colt transaction, like any transaction, poses certain risks to the Bank. In particular, Barclays bears gap risk associated with being the holder of the basket of securities. These risks are mitigated by particular features of the transaction, including Barclays’ right to unilaterally unwind the transaction if losses exceed the amount of the premium paid by Renaissance on any existing option. There is also a monitoring system to oversee performance of the reference portfolio, and certain limitations such as concentration and skew limits. For example, over a period of several days in August 2007, this portfolio, like others using a statistical arbitrage strategy, suffered higher than expected losses. While the portfolio eventually rebounded, and the losses did not exceed the limit levels that would have triggered an automatic unwind of the

transaction, Barclays' resulting concern led us to impose several additional risk mitigating limitations on the transaction.

While Barclays had the risks and protections I just described, the Colt transaction was unique in at least one important way in that it was non-recourse. In other words, unlike other transactions in which the Bank provides financing, with the Colt transaction we cannot pursue legal remedies from Renaissance in the event the portfolio suffers losses in excess of the amount of premium paid. So the risk of loss on the portfolio once the option premium is exhausted remains entirely with Barclays.

It is my understanding that the fundamental question raised by this Subcommittee is whether, historically, Renaissance has applied the correct tax rate to its earnings from the Colt options. It is also my understanding that this question has not yet been decided by the IRS. Although the IRS issued generic legal advice in 2010, it is my understanding that this type of legal advice does not set out official rulings or positions of the IRS and may not be referenced in other documents as precedent. Since the issuance of the advice, the IRS has issued no further guidance or decision on these transactions. Although Barclays feels strongly that this transaction was subject to sufficient and significant internal and external review to ensure it complied with applicable tax laws and regulations, ultimately the question of, "what tax rate should Renaissance pay?," is a matter to be resolved between Renaissance, as the taxpayer, and the IRS. It is not uncommon for taxpayers, large and small, to have occasional disputes regarding the amount of tax that they owe, and a fulsome process exists, both at the IRS and in the courts, to resolve such disputes.

I hope my testimony has been helpful, and I will do my best to answer the Subcommittee's questions. I should note, however, that although I have been involved with many aspects of this transaction over the course of its execution at Barclays, I have not been responsible for the deal's day-to-day operations since May 2008, more than six years ago. Nonetheless, to assist the Subcommittee, the Bank has done its best to collect as much information related to this transaction as possible and therefore, at times, my testimony and answers will reflect not my personal knowledge, but what I have been informed of by others working for the Bank.