HM Treasury

Consultation: Amendments to the Building Societies Act 1986

Call for Evidence - Response

December 2022

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Chapter 1

Introduction

Background

1.1 As part of the wider growth objective for the UK economy, the government wants to unleash the potential of the UK financial services industry as the most competitive and innovative in the world, delivering greater choice and value for consumers and businesses. The mutuals sector, with its focus on serving members and local communities, can play an important role in promoting this and provide valuable diversity within the UK financial services sector.

1.2 Specifically, building societies make a valuable contribution to the UK financial services industry. According to the latest Building Societies Association (BSA) data, collectively, building societies serve over 25.8 million members and hold over £352 billion of mortgage assets and £313 billion of savings from individuals[1].

1.3 In 2012, the coalition government published a discussion paper titled "The Future of Building Societies"[2]. This paper set out that the legislative framework for building societies should ensure they can compete effectively with other financial services firms whilst maintaining their distinctive approach as mutually owned mortgage providers.

1.4 The coalition government also requested views in the 2012 discussion paper on updates to the Building Societies Act 1986 ("the 1986 Act"), the legislation which governs building societies. The coalition government received responses and subsequently made a number of updates to the 1986 Act through the Financial Services (Banking Reform) Act 2013.

1.5 These changes amended the 1986 Act to allow building societies to take deposits from Small to Medium-sized Enterprises (SME's) with turnover of up to £1 million, without these deposits counting as wholesale funding, up to a 10% overall funding limit[3]. The changes also removed restrictions on the creation of floating charges and updated some corporate governance requirements.

1.6 Whilst this government believes the 1986 Act broadly remains fit for purpose, it recognises that there is interest and rationale in making further updates to the 1986 Act to allow building societies to compete on a more

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1 Building Societies Association (BSA) 2021-2022 sector performance data

2 HM Treasury July 2012 "The future of building societies"

3 Building societies are governed by the Building Societies Act 1986 ("the 1986 Act"). One requirement of this legislation is that building societies must obtain at least 50% of their funding from individual retail deposits ("the funding limit").

level playing field with banks and to promote competition within the financial services sector.

Government consultation and its response

1.7 Following on from engagement with the building society sector, the Prudential Regulatory Authority (PRA) and the Financial Conduct Authority (FCA), on 6 December 2021, the government launched a consultation on several amendments to the Building Societies Act 1986[4]. The consultation proposed excluding some sources of funding from the funding limit calculation and updating building society corporate governance requirements in line with modernisations made to the Companies Act 2006.

1.8 The consultation proposed to exclude four different sources of funding from the funding limit calculation. These were funding from specific Bank of England Liquidity Insurance Facilities which exist to allow banks and building societies to access liquidity in stress scenarios[5]; funding from senior non-preferred debt instruments raised to meet Minimum Required Eligible Own Funds and Liabilities (MREL) requirements, given that funding to meet capital requirements is already excluded from the funding limit; funding from repurchase agreements of high-quality liquid assets where funding essentially counts twice for the purposes of the funding limit; and deposits from Small and Medium-sized Enterprises (SMEs) with a turnover of up to £6.5 million to bring building societies in line with ring-fenced banks.

1.9 The consultation further asked whether there are future trends that respondents see as having the potential to cause future funding difficulties for building societies in the next 4-5 years.

1.10 The consultation also proposed to update the corporate governance requirements for building societies and bring them into line with the Companies Act 2006. Specifically, it proposed to explicitly allow for real-time virtual member participation in general meetings, remove the requirement for building societies to affix a seal when executing a deed, and require only one director to sign the balance sheet of a building society, instead of two directors and the CEO.

1.11 The consultation closed on 28 February 2022. The government received 5 individual responses, with most building societies responded through the BSA. The government is using these responses to the consultation to inform considerations about the proposed amendments to the Building Societies Act 1986. This document provides a summary of those responses and the government's proposed next steps.

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4 Consultation_-_Amendments_to_the_Building_Societies_Act_1986_.pdf (publishing.service.gov.uk)

5 Subject to certain eligibility criteria: see Bank of England Market Operations: Our tools

Chapter 2

Responses on the funding limit

Excluding sources of funding from the funding limit

Question 1: Should the Bank of England liquidity insurance facilities under the Sterling Monetary Framework (SMF) be excluded from the funding limit calculation?

Question 2: Should funding from level 1 HQLA repurchase agreements be excluded from the funding limit calculation?

Question 3: Should senior non preferred debt instruments held for MREL purposes be excluded from the funding limit calculation?

Question 4: Should deposits from businesses with a turnover of up to £6.5 million be excluded from the funding limit calculation, up to 10% of a building society's overall funding?

Question 5: Will the outlined changes continue to support the mutual model of building societies? If not, please provide reasoning.

1.12 Part of the 1986 Act sets out restrictions on building societies' funding activities. Subject to some exemptions, such as own funds, building societies are required to raise at least 50% of their funding from their members' deposits in savings accounts, with funding from other sources called wholesale funding. This is known as "the funding limit".

1.13 The funding limit restriction is an important feature of the building society model. It preserves the mutual status of building societies by ensuring they are at least 50% owned by their members, and it complements other financial regulation by ensuring societies are mainly funded by the longer-term savings of their members. The government believes that the minimum 50% requirement for funding from member deposits remains appropriate and it has no plans to change this level.

1.14 However, the government recognises that the funding limit may create challenges for building societies that other financial institutions like banks do not have.

1.15 The consultation therefore proposed that the government excludes four different sources of funding from the funding limit calculation[6] and asked respondents whether the outlined changes would continue to support the mutual model of building societies. These were funding from specific Bank

[6] Detailed rationale behind the four specific proposals around excluding a particular source of funding from a building society's funding limit were provided in the original consultation: https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/1038539/Consultation_-_Amendments_to_the_Building_Societies_Act_1986_.pdf

of England Liquidity Insurance Facilities[7] which exist to allow banks and building societies to access liquidity in stress scenarios; funding from senior non-preferred debt instruments raised to meet MREL requirements, given that funding to meet capital requirements is already excluded from the funding limit; funding from repurchase agreements of high-quality liquid assets where funding essentially counts twice for the purposes of the funding limit; and deposits from SME's with a turnover of up to £6.5 million to bring building societies in line with ring-fenced banks.

1.16 All consultation responses were supportive of excluding the noted sources of funding from the Bank of England Liquidity Insurance Facilities under the Sterling Monetary Framework (SMF) from the funding limit calculation. All responses noted that excluding this source from the funding limit would mean that access to the facilities was not constrained and would aid building societies during a stress scenario.

1.17 All consultation responses were supportive of excluding sources of funding from senior non-preferred debt instruments raised to meet MREL requirements from the funding limit calculation. Respondents noted that excluding this source from the funding limit would align with how other sources of funding for regulatory purposes are treated.

1.18 All consultation responses were supportive of excluding sources of funding from repurchase agreements of high-quality liquid assets from the funding limit calculation. Respondents noted that excluding this source from the funding limit would provide building societies with greater flexibility in managing liquidity and help support them during a stress period.

1.19 All consultation responses were supportive of excluding deposits from SME's with a turnover of up to £6.5 million, up to 10% of a building society's overall funding. Respondents noted that excluding this source from the funding limit would create greater parity between building societies and ring-fenced banks, helping to promote further competition within the banking sector.

1.20 **In sum, all consultation responses were supportive of the proposals around excluding these particular types of sources from the funding limit calculation and agreed that the outlined changes would continue to support the mutual model of building societies.** They noted that they would provide greater flexibility for building societies in financial stress and bring the 1986 Act more in line with companies.

Future trends

Question 6: Are there future trends that respondents see as having potential to cause future funding difficulties for building societies in the next 4-5 years? If so, please describe the trends and rationale.

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[7] Currently, these facilities include the Discount Window Facility (DWF), the Indexed Long-Term Repo (ILTR) and the Contingent Term Repo Facility (CTRF).

Question 7: How can the government best help building societies overcome these difficulties?

1.21 The consultation also welcomed views on future trends that respondents see as having potential to cause future funding difficulties for building societies in the next 4-5 years and how the government can best help building societies overcome these.

1.22 **Responses to the consultation raised the issue of funding from deposit aggregators, also known as intermediated savings platforms.** These platforms partner with financial institutions such as banks and building societies to advertise savings products, which individuals can choose to deposit into.

1.23 **Consultation responses requested the government either class funding from these platforms as retail funding or exclude it from the funding limit calculation**, given that the underlying depositors are retail customers.

Next steps

1.24 **The government will legislate to exclude funding from specific Bank of England Liquidity Insurance Facilities, senior non-preferred debt instruments raised to meet MREL requirements, repurchase agreements of high-quality liquid assets, and deposits from SME's with a turnover of up to £6.5 million from the funding limit for building societies**. Legislating these changes to the funding limit will provide greater flexibility for building societies in financial stress, bring the 1986 Act more in line with companies, and continue to support the mutual model of building societies.

1.25 On future trends, the government acknowledges that the savings platform market is likely to continue to grow and therefore hold a greater share of the market in the future. In recognition of this, **the government will commit to revisiting the treatment of funding obtained through the intermediated savings platforms in the medium term.** This will allow government and the regulators to develop a clearer sense of the market and its impact on building societies.

Chapter 3

Responses on the corporate framework

Virtual participation at member meetings

Question 8: Should the 1986 Act be amended to explicitly allow real-time virtual member participation in general meetings for building societies?

1.26 The consultation proposed that the 1986 Act explicitly allows for real-time virtual member participation at general meetings to promote member engagement and bring building societies in line with the Companies Act[8]. **All responses to the consultation welcomed these proposals and felt that they would help modernise the 1986 Act and provide societies with equal flexibility as companies.**

Other updates

Question 9: Should the 1986 Act should be updated to allow for just one director to sign the balance sheet on behalf of the board?

Question 10: Should building societies be allowed to either affix a seal or obtain the signatures of directors to execute a deed, bringing building societies' corporate framework more in line with companies?

1.27 The consultation proposed other small but valuable changes which would be desirable to make in order to bring building societies' corporate governance structures onto a more level playing field with that of companies.

1.28 The government proposed altering the requirement for the balance sheet to be signed by two directors and the CEO to allowing one director to sign the balance sheet on behalf of the board. As companies also only require one director to sign their accounts, this would reduce a small but unnecessary burden for building societies. **All responses to the consultation welcomed this proposal and felt it would help provide societies with equal flexibility as companies.**

1.29 The government also proposed that the requirement to affix a seal to execute deeds is updated in line with companies. The Companies Act 2006 states that to execute a deed, companies may either affix a seal or obtain the signatures of directors. However, building societies are not afforded the same flexibility and must affix a seal. **All responses to the consultation**

8 See s.360A of CA 2006; *"nothing in this Part [13] is to be taken to preclude the holding and conducting of a meeting in such a way that persons who are not present together at the same place may by electronic means attend and speak and vote at it"*.

welcomed this proposal and felt it would provide societies with equal flexibility as companies.

Next steps

1.30 The government will legislate to explicitly allow real-time virtual member participation at general meetings; to alter the requirement for the balance sheet to be signed by two directors and the CEO to allow one director to sign the balance sheet on behalf of the board; and to allow building societies to execute a deed either by affixing a seal or obtaining the signatures of directors. These amendments will help modernise the 1986 Act and provide societies with equal flexibility as companies.

Chapter 4

Responses on out-of-scope issues

Out-of-scope issues

1.31 There were other issues raised by respondents, but these were out of scope of the consultation. These included removal of criminal offences, fiduciary duties, raising the probate limit for deceased investors, and gender-neutral terminology.

1.32 **Two respondents proposed removing the 'normal retirement age' (as stated in the 1986 Act) for directors, raising the issue of age discrimination and how this potentially contravenes the Equality Act 2010.** The 1986 Act currently requires directors above the age of 70 who wish to be re-elected to have their age notified to each person entitled to vote in the election and for the board to approve by resolution that the individual is eligible for re-election. There were equivalent provisions set out in the Companies Act 2006 for PLCs, but following the Equality Act 2010 - which includes age as a protected characteristic - those provisions were deleted from the Companies Act.

Next steps

1.33 Given that the majority of the other issues raised were out of scope of the main consultation questions, were not raised by all respondents, and need further evidence gathering on, **the government will look to review the out-of-scope issues raised by respondents at a later date.** This will allow more appropriate time for the government to engage properly with the sector and come to a well-evidenced policy view.

1.34 **The government will legislate to remove the normal retirement age for directors**. This will bring the 1986 Act in line with the Equality Act 2010 and the Companies Act 2006.

Annex A

Individual responses

Summary of views requested

A.1 The consultation sought views on the questions listed below:

1. Should the Bank of England liquidity insurance facilities under the Sterling Monetary Framework (SMF) be excluded from the funding limit calculation?
2. Should funding from level 1 HQLA repurchase agreements be excluded from the funding limit calculation?
3. Should senior non preferred debt instruments held for MREL purposes be excluded from the funding limit calculation?
4. Should deposits from businesses with a turnover of up to £6.5 million be excluded from the funding limit calculation, up to 10% of a building society's overall funding?
5. Will the outlined changes continue to support the mutual model of building societies? If not, please provide reasoning.
6. Are there future trends that respondents see as having potential to cause future funding difficulties for building societies in the next 4-5 years? If so, please describe the trends and rationale.
7. How can the government best help building societies overcome these difficulties?
8. Should the 1986 Act be amended to explicitly allow real-time virtual member participation in general meetings for building societies?
9. Should the 1986 Act should be updated to allow for just one director to sign the balance sheet on behalf of the board?
10. Should building societies be allowed to either affix a seal or obtain the signatures of directors to execute a deed, bringing building societies' corporate framework more in line with companies?

Summary of individual responses

A.2 The government received 5 responses. Responses received came from:

- Building Societies Association[1],
- Nationwide Building Society,
- Coventry Building Society,
- Leeds Building Society, and
- Hargreaves Lansdowne.

[1] The Building Societies Association (BSA) is the main Trade Body for the sector. The BSA represents all 43 building societies in the UK as well as 7 credit unions.

HM Treasury contacts

This document can be downloaded from www.gov.uk

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