



HM Treasury

Financial Services (Banking Reform) Bill

Government Amendments: Building Society Changes

Briefing for Peers

October 2013

The Government published '*The future of building societies*' consultation in July 2012 which asked the building society sector whether there were any legislative changes to the Building Societies Act 1986 that would remove limitations or barriers to growth, while preserving the distinctive and traditional building society model.

Building societies are not subject to company law, and therefore can be left behind when modernisations are made for companies. The amendment will make modernising changes to the Building Societies Act 1986, to bring it more in line with company law, assist societies in raising funding, and make minor technical changes, in order to allow the sector to compete on a more level playing-field with banks.

Specifically, the amendment will:

- Make it easier for building societies to communicate with members electronically, rather than using paper, by stating that a person is deemed to have consented to access a document on a website if that person has been asked by the society, or, if that person has been asked and has not replied within 28 days.
- Allow societies to issue floating charges, a common type of security used when borrowing. A floating charge is a security over a changing group of assets e.g. over a group or class of present and future mortgages, rather than one particular mortgage. Banks are able to issue floating charges, and removing this restriction will give building societies similar flexibility to raise wholesale funding. The original reason for the ban on floating charges was to protect societies from excessive control by charge holders able to appoint an administrative receiver. However, due to changes in insolvency law, this threat no longer exists.
- The Building Societies Act requires societies to be funded by a maximum of 50% of wholesale funding. Currently, small business deposits count as wholesale funding. This change will change the classification of small business deposits so that they do not count as wholesale funding, and can therefore be disregarded from the funding limit calculation. The maximum amount that can be disregarded is capped at 10% of the value of the society's group funds. It is appropriate to make this change because deposits made by small businesses are far more akin to retail deposits than wholesale funding. This will give societies more leeway in meeting the funding limit, and therefore greater freedom to source wholesale funding. It will also allow societies more freedom to provide services to small businesses.
- Allow holders of deferred shares (a type of mutual capital instrument) of less than 2 years standing to be eligible to receive shares or cash when a society demutualises. Holdings in deferred shares change

regularly as a secondary market develops and therefore only some holders (those of over 2 years) could receive ordinary shares in the successor bank upon demutualisation but most (those of under 2 years) could not. Making this amendment addresses this issue. It also removes the risk that Tier 1 capital (high quality, e.g. shares) would be downgraded to Tier 2 capital (lower quality, e.g. subordinated debt) in the event of such a demutualisation. There will be no change to the position that other society members must have been a member of the building society for at least 2 years to be eligible to receive shares or cash on a demutualisation.

- Allow building societies to change their financial year end date to any date in the year (rather than just 31 December), which banks can currently do.
- Remove the requirement for building societies to provide each new shareholding member with a copy of the Summary Financial Statement. Instead it will be made available online. There is no equivalent requirement for banks.
- Remove the requirement for officers (who are not directors) to make disclosures for the purposes of the society's annual business statement. Such disclosure is excessive, time-consuming and costly, and there is no equivalent requirement for banks.
- Remove the words "in priority" in s100(8) of the Building Societies Act, relating to the distribution of shares on a transfer of a society's business. Section 100(8) was intended to ensure that the right of a shareholder to acquire shares on a transfer of business was limited to long-term shareholders (those who had held shares in the society for at least 2 years before the transfer), but the inclusion of the words "in priority" created an anomalous outcome. The effect is that, if the only preference or priority is restricted to two-year shareholders, other members, including borrowers, could also be given the right to acquire shares. The provision has been considered by the courts and was noted by the Treasury Committee – H.C. Treasury Committee, Ninth Report, Session 1998-99, July 22, 1999. The amendment closes the loophole. The Treasury Committee Report is available online at <http://www.publications.parliament.uk/pa/cm199899/cmselect/cmtreasy/605/60506.html>. The relevant bullet points are 44-48.

Further Enquiries

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2. For access to publications please go to <http://www.gov.uk/government/policies/creating-stronger-and-safer-banks>