

Financial Services (Banking Reform) Bill

Government annotated amendments: Provisions for building societies

After Clause 15

LORD DEIGHTON

Insert the following new Clause —

“Building societies

Schedule (*Building societies*) (which contains provision about building societies) has effect.”

This introduces the new schedule relating to building societies.

Clause 21

LORD DEIGHTON

Page 29, line 33, at end insert —

“() Section (*Building societies*) and Schedule (*Building societies*), apart from paragraph 4 of that Schedule, come into force at the end of the period of 2 months beginning with the day on which this Act is passed.”

Each of the building society provisions will come into force automatically two months after the Bill receives Royal Assent, except for the provision relating to floating charges in paragraph 4 which will be commenced by order.

Before Schedule 2

LORD DEIGHTON

Insert the following new Schedule —

“BUILDING SOCIETIES

Introductory

1 The Building Societies Act 1986 is amended as follows.

Exclusion of small business deposits from funding limit

2 (1) Section 7 (the funding limit) is amended as follows.

This will amend section 7 of the Building Societies Act 1986 which sets out the funding limit for building societies. The funding limit requires that the value of deposits made by individuals in the society (known as “retail funds”) is at least 50% of the value of the total funds of the society’s group (or total group funds).

(2) In subsection (3), omit the “and” at the end of paragraph (a) and after that paragraph insert —

“(aa) subject to subsection (3A), the principal of, and interest accrued on, sums deposited with the society or any subsidiary undertaking of the society by a small business (see subsection (10));”.

This will change the calculation of the funding limit so that deposits by small businesses will not count towards the value of total group funds. But the amount that can be disregarded for the purposes of the funding limit is limited by the next subsection, subsection 3(3A). This means, for the purposes of the funding limit, a limited amount of the deposits of small businesses will no longer be treated as “wholesale funds”. This makes it easier for societies to meet the funding limit, whilst encouraging the taking of small business deposits.

(3) After subsection (3) insert —

“(3A) In respect of any day by reference to which the value of X falls to be calculated for the purposes of subsection (1) in relation to the society, the total amount to be disregarded under subsection (3)(aa) may not exceed 10% of the amount that would, in the absence of subsection (3)(aa), be the value of X on that day.”

This is the limit on the amount of small business deposits that will not count for the purposes of the previous subsection, subsection 3(aa). It means that, when calculating the funding limit, no more than 10% of the value of total group funds can be disregarded in respect of small business deposits.

The 10% limit helps to ensure that building societies do not breach their principal purpose which requires them to be “substantially funded by member deposits”, as set out in section 5(1) of the Building Societies Act 1986. This is because deposits from small business (unlike deposits from individuals) are not member deposits.

The value of total group funds is the value it would be without the modification made by new subsection (3)(aa), i.e. after all the other modifications required by or under section 7 have been made.

(4) After subsection (6) insert —

“(6ZA) Where a person declares that the person is a small business, the person shall, unless the contrary is shown, be conclusively presumed for the purposes of this section to be a small business.”

A business is assumed to be a small business if it has declared itself to be a small business, unless this is shown not to be the case.

(5) After subsection (9) insert —

“(10) In this section “small business” means any person (other than an individual acting as a sole trader) carrying on a business which had a turnover in the relevant financial year of less than £1,000,000.

This is the definition of a small business: it is as any person with an annual turnover of less than £1 million, but not including individuals acting as sole traders. For example, a small business could be a company, partnership, mutual association or other unincorporated body. This definition is based on the definition used to calculate the eligibility of small businesses for the Financial Services Compensation Scheme.

(11) For the purposes of subsection (10) —

(a) the “relevant financial year”, in relation to any day by reference to which the value of X falls to be calculated for the purposes of subsection (1) in relation to a building society, means the last financial year ending before that day;

(b) “turnover”, in relation to a small business, means the amount derived from the provision of goods and services falling within the business’s ordinary activities, after deduction of trade discounts, value added tax and any other taxes based on the amounts so derived;

(c) in respect of any relevant financial year, the reference to £1,000,000 includes the equivalent amount in any other currency, calculated as at the last day of that year.

This defines terms that are used in the definition of small business.

(12) The Treasury may, by order made by statutory instrument, amend the figure for the time being specified in subsections (10) and (11)(c).

(13) A statutory instrument containing an order under subsection (12) is subject to annulment in pursuance of a resolution of either House of Parliament.”

This will give the Treasury power to make an order (subject to negative resolution) to vary the amount of £1 million used in the definition of small business.

3 (1) In article 3 of the Building Societies Act 1986 (Substitution of Specified Amounts and Modification of the Funding Limits Calculation) Order 2007 (S.I. 2007/860), in paragraph 3, for “the modification required by this article” substitute “the modifications required by this article and by section 7(3)(aa)”.

This is a consequential amendment to the Building Societies Act 1986 (Substitution of Specified Amounts and Modification of the Funding Limit Calculation) Order 2007 (SI 2007/860) (the 2007 Order). The 2007 Order provides that a limited amount of deposits held in a society’s EEA subsidiaries are to be disregarded in calculating the funding limit.

The amendment ensures that, for the purposes of calculating the amount to be disregarded under the 2007 Order, the value of total group funds is the value it would be without the modification made by the 2007 Order and the modification made by new section 7(3)(aa) above.

(2) The amendment by this paragraph of a provision contained in subordinate legislation is without prejudice to any power to amend that provision by subordinate legislation.

Although the Bill will amend a provision of the 2007 Order, it does not affect any other powers to amend the provision.

Ability to create floating charges

4 (1) Omit section 9B (restriction on creation of floating charges).

This will repeal section 9B of the Building Societies Act 1986 which restricts a building society's power to create floating charges. Consequently, a building society will be permitted to create floating charges over its assets. Floating charges are 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.

The present ban on floating charges means building societies are prevented from entering into ordinary transactions which, as a result of the financial crisis, require them to grant security over assets which may be characterised as fluctuating assets, rather than fixed assets. For example, at the moment, a society cannot enter into fairly routine overnight "delivery by value" transactions by creating security which could be characterised as a floating charge.

Such floating charges, however, will not give the holder the right to appoint an administrator or an administrative receiver (unless appointed under the Building Societies (Financial Assistance) Order 2010). An administrator cannot be appointed because Schedule B1 to the Insolvency Act 1986 (under which companies can create floating charges which enable the holder to appoint an administrator) does not apply to building societies, because societies are subject to the version of Part 2 of the Insolvency Act 1986 as it had effect before the Enterprise Act 2002 (section 249(1) and (2) of the Enterprise Act 2002). An administrative receiver cannot be appointed because Schedules 15 and 15A to the Building Societies Act 1986 (which apply companies winding up and insolvency legislation to building societies) will continue to provide that, in the provisions of the Insolvency Act 1986 which apply to societies, a reference to an administrative receiver does not apply to a society (paragraph 3(2)(b) of schedule 15 and paragraph 2(2)(b) of Schedule 15A to the Building Societies Act 1986).

(2) In Schedule 15A (application of other companies insolvency legislation to building societies), omit the following paragraphs —

- (a) paragraph 18 (which modifies section 15 of the Insolvency Act 1986);
- (b) paragraph 20 (which modifies section 19 of that Act);
- (c) paragraph 40 (which modifies Article 28 of the Insolvency (Northern Ireland) Order 1989);
- (d) paragraph 42 (which modifies Article 31 of that Order).

These are amendments to Schedule 15A to the Building Societies Act 1986 (which applies company insolvency legislation to building societies) to ensure that an administration order of the court under Part 2 of the Insolvency Act 1986 can apply to a floating charge.

(3) In consequence of the amendment made by sub-paragraph (1) –

- (a) in section 1(1A)(b), for “, (9A) and (9B)” substitute “and (9A)”;
- (b) in the Building Societies Act 1997, omit section 11;
- (c) in section 11(3) of the Banking (Special Provisions) Act 2008, for paragraph (c) substitute –
 - “(c) sections 8 and 9A of the Building Societies Act 1986 (restrictions on raising funds and borrowing and on transactions involving derivative instruments etc);”;
- (d) in section 251 of the Banking Act 2009, omit subsection (7);
- (e) in the Financial Services Act 2012, omit section 55.

These consequential amendments remove references in various enactments to the existing restrictions in section 9B on a building society’s power to create floating charges.

Annual business statements

5 (1) Section 74 (duty of directors to prepare annual business statement) is amended as follows.

This will amend section 74 of the Building Societies Act 1986 which requires a building society to prepare an annual business statement, and for officers (as well as directors) to make disclosures for the statement. The definition of “officers” in the Building Societies Act 1986 includes any secretary or manager of the society. In practice this means that, currently, societies make disclosures for the top two tiers of management – a far greater level of disclosure than companies are required to make.

(2) In subsection (4), omit the words from “and other officers” to “them”.

(3) In subsection (8), omit “or other officer”.

This will remove the duty on officers (who are not directors) of a building society to notify their interests to the society for the purposes of the statement.

Consequential amendments will be made by secondary legislation to the Societies (Accounts and Related Provisions) Regulations 1998 so that disclosure requirements do not apply to such officers. The requirements for disclosures from directors are not affected.

Summary financial statements

6 (1) Section 76 (summary financial statement for members and depositors) is amended as follows.

This will amend section 76 of the Building Societies Act 1986 which requires directors of a society to prepare a summary financial statement for each financial year.

(2) After subsection (8A) insert –

“(8AA) The society shall also –

- (a) publish the summary financial statement and (where applicable) the auditor’s report on a web site, and
- (b) ensure that the statement and (where applicable) the report may be accessed on the web site until the publication of the next summary financial statement.”

This means that a society will be required to publish the latest summary financial statement and (where applied under section 78(6)) the auditor’s report on a website, and make sure it is accessible online until the publication of the next year’s statement. The requirement to publish the auditor’s report applies only if the report has been qualified by the auditor.

(3) After subsection (8D) insert –

“(8E) If, at any time during the period beginning with the publication of the summary financial statement and ending with the publication of the next summary financial statement, an individual for the first time subscribes for shares in the society, the society shall at that time notify the individual of the information in subsection (8C)(c)(i) to (iii).

Any individual who becomes a shareholder during the year must be notified by the society of the following: (i) the online publication of the latest summary financial statement and (where applicable) the

auditor's report; (ii) the website address; (iii) where on the website, and how, the information may be accessed.

(8F) In a case where subsection (8E) applies, the society is not required under section 115B (right to hard copy version) to send the individual a version of the summary financial statement or (where applicable) the auditor's report in hard copy form (within the meaning of that section)."

A new shareholder is not entitled to a hard copy of the summary financial statement or (where applicable) the auditor's report. In practice, new members must access the information online.

(4) Omit subsections (9) to (9E).

This will remove the existing obligation on societies to send the summary financial statement and (where applied under section 78(6)) the auditor's report to new shareholding members. Instead societies will have to publish the documents on a website, and notify new shareholders, in accordance with the provisions above.

(5) In subsection (11), for "subsection (9)" substitute "subsection (8AA) or (8E)".

The existing criminal offence in subsection 11 for failure to send the summary financial statement or auditor's report to new shareholders is updated to reflect the new requirement to publish those documents online, i.e. it will be an offence to fail to publish the documents online or to notify new shareholders as required.

7 In consequence of the amendments made by paragraph 6 –

(a) in section 78(6), for "subsections (8) and (9) of section 76 extend" substitute "subsection (8) of section 76 extends";

(b) in paragraphs 7(3) and 8(3) of Schedule 2, omit "the summary financial statement,".

These are consequential amendments to the Building Societies Act 1986 to make sure the rest of the Act is consistent with the changes described above.

Transfers of business: distributions and share rights

8 (1) Section 100 (regulated terms etc: distributions and share rights) is amended as follows.

Section 100 of the Building Societies Act 1986 sets out distributions and share rights on a transfer of a society's business.

(2) For subsection (8) substitute –

“(8) The terms of a transfer of a society's business may confer a right to acquire shares in the successor on a member of the society only if the member.

(a) held shares in the society throughout the period of two years ending with the qualifying day, or

(b) on that day, holds deferred shares in the society that are of a class described in the transfer agreement; and it is unlawful for any right in relation to shares to be conferred in contravention of this subsection.”

If a right to acquire shares is given to members on a transfer of business (demutualisation) then the right must be restricted to members who have either held shares for at least two years; or who hold deferred shares of a class described in the transfer agreement.

This will replace the existing section 100(8) in the Building Societies Act 1986 to make it clear that the subsection applies to any right (i.e. not only a priority right) to acquire shares which is conferred on members. This is to correct the existing provision which, by referring to priority rights, has not worked as intended (see H.C. Treasury Committee, Ninth Report, Session 1998-99, July 22, 1999)¹.

The new subsection makes specific provision for holders of deferred shares, a form of capital instrument issued by building societies.

At present, only shareholders who have held shares in the society for at least two years are eligible to acquire shares on the

¹<http://www.publications.parliament.uk/pa/cm199899/cmselect/cmtreasy/605/60506.htm>, bullet-points 44-48

transfer of business (demutualisation). This will change so that holders of deferred shares will be eligible, irrespective of how long they have held the shares. There will be no change to the position that other shareholders must have held shares in the building society for at least 2 years to be eligible to acquire shares on a demutualisation.

(3) In subsection (9), for the words from “who” to “and” substitute “who —

(a) held shares in the society throughout the period of two years ending with the qualifying day, or

(b) on that day, hold deferred shares in the society that are of a class described in the transfer agreement; and”.

If a right to receive a cash distribution is given to members on a transfer of business (demutualisation) to an existing company, then the right must be restricted to members who have either held shares for at least two years; or who hold deferred shares of a class described in the transfer agreement.

The amendment in subsection (9), like the new subsection (8), makes specific provision for holders of deferred shares, a form of capital instrument issued by building societies.

At present, only shareholders who have held shares in the society for at least two years are eligible to receive a cash distribution on the transfer of business (demutualisation) to an existing company. This will change so that holders of deferred shares will be eligible, irrespective of how long they have held the shares. There will be no change to the position that other shareholders must have held shares in the building society for at least 2 years to be eligible to receive cash on a demutualisation.

Methods of communicating with members etc

This inserts new sections 115A to 115C into the Building Societies Act 1986 which contain new provisions relating to website communication by a society. A person can already access documents online, but only where he has specifically agreed to do so. The new provisions create a mechanism for a person’s consent to be deemed to be given in certain circumstances, and therefore make it easier for societies to use electronic communications with members.

9 After section 115 insert —

“115A Deemed agreement to use of web site

(1) For the purposes of this Act, a person is to be taken to have agreed with a building society to access a document, information or facility on a web site if —

- (a) the person has been asked individually by the society to agree to access documents, information or facilities generally, or the document, information or facility in question, on a web site, and
- (b) the society has not received a response within the period of 28 days beginning with the date on which the society’s request was received.

This is subject to subsections (2) to (4).

This means that a person is deemed to have agreed to access a document, information or facility on a website if the person has been asked individually and has agreed to do so; or has been asked and the society has not received a response within 28 days. The “deemed consent” mechanism will not apply in the circumstances described below.

(2) A person is not to be taken to have so agreed if the society’s request —

- (a) did not state clearly what the effect of a failure to respond would be, or
- (b) was sent less than 12 months after a previous request made to the person for the purposes of this section in respect of the same or a similar description of document, information or facility.

Deemed consent will not be valid if the society either: did not clearly set out in the request what would happen if the person did not respond; or had already made a similar request within the last 12 months.

(3) A person who is taken to have made an agreement by virtue of subsection (1) may revoke the agreement.

Any person is able to revoke their deemed consent.

(4) Subsection (1) does not apply in relation to the following documents —

- (a) a statement required to be sent to members by paragraph 1(1) of Schedule 16 (statements in connection with proposed mergers);
- (b) a merger statement (within the meaning of Part 2 of that Schedule) required to be sent to members by paragraph 3 of that Schedule;
- (c) a transfer statement or transfer summary (within the meaning of Part 1 of Schedule 17) required to be sent to members by paragraph 4(1) or (2) of that Schedule;
- (d) a transfer proposal notification (within the meaning of Part 1A of Schedule 17) required to be sent to members by paragraph 5B(1) of that Schedule.

Deemed consent does not apply to every document that is required to be sent by a society: i.e. statements in connection with proposed mergers or transfers of business cannot be supplied by being made available on a website, unless the person has specifically agreed that is the case under existing provisions.

115B Right to hard copy version

- (1) Where a person has received a document or information from a building society otherwise than in hard copy form, the person is entitled to require the society to send the person a version of the document or information in hard copy form.
- (2) The society must send the document or information in hard copy form within 21 days of receipt of the request from the person.
- (3) The society may not make a charge for providing the document or information in that form.
- (4) Subsection (1) does not apply if the recipient of the document or information is the FCA or the PRA.

A person has a right to receive, free of charge, a hard copy of any document or information that was supplied to him by other means (e.g. electronic communication) within 21 days of his request.

- (5) A building society that fails to comply with this section is to be treated as having contravened rules made under section 137A of the Financial Services and Markets Act 2000.

If a building society fails to provide a hard copy on request, it will be treated as though it has breached rules made under section 137A of the Financial Services and Markets Act 2000, which is the Financial Conduct Authority's general rule making power. The effect of this is that the FCA can take disciplinary measures if a society fails to comply with this new section 115B.

(6) For the purposes of this section a person is treated as receiving a document or information from a building society if –

- (a) the society is required by this Act to send the document or information to the person, and
- (b) the requirement to send it is treated as satisfied.

This means that, if a society has satisfied a requirement under the Building Societies Act 1986 to send a document or information to a person, then that person is treated as having received that document or information.

(7) For the purposes of this section –

- (a) a document or information is sent or supplied in hard copy form if it is sent or supplied in a paper copy or similar form capable of being read, and
- (b) a document or information can be read only if it can be read with the naked eye, or (to the extent that it consists of images) it can be seen with the naked eye.

This sets out what is meant by sending a document in hard copy.

115C Other agreed forms of communication

(1) A document or information that is sent or supplied by a building society otherwise than in hard copy form or electronically or by means of a web site is validly sent or supplied if it is sent or supplied in a form or manner that has been agreed by the intended recipient.

(2) For the purposes of this section “hard copy form” is to be read in accordance with section 115B(7).”

An intended recipient may agree with a society to receive a document in a way that is not by hard copy or by electronic means. The definition of hard copy is provided above in subsection 7.

10 In the following provisions, omit “, in a manner agreed between him and the society,” –

section 60(7B)(c),

section 61(7D)(c),

section 68(6B)(c),

section 69(15B)(c),

section 76(8C)(c).

11 In section 81(3B)(c), omit “, in a manner agreed for the purpose between him and the society,”.

12 (1) Schedule 2 is amended as follows.

(2) In paragraph 20A(1B)(c), omit “, in a manner agreed between him and the society,”.

(3) In paragraphs 22B(2)(c) and 33(5C)(c), omit “, in a manner agreed between him and the society for that purpose,”.

(4) In paragraph 24(1B)(b), omit “in a manner agreed between the society and that member,”.

(5) In paragraph 32(2D)(c), omit “, in a manner agreed between the society and the member,”.

(6) In paragraph 33A(9)(c), omit “, in a manner agreed for the purpose between him and the society”.

13 In paragraphs 3(2B)(c) and 9(2B)(c) of Schedule 8A, omit “in a manner agreed between the society and that person,”.

14 (1) Schedule 11 is amended as follows.

(2) In paragraph 4(9C)(c), omit “, in a manner agreed between him and the society,”.

(3) In paragraph 7(7C)(c), for “in a manner agreed between the society and that person, he” substitute “the person”.

(4) In paragraph 8(3B)(c), omit “, in a manner agreed between him and the society for the purpose,”.

These changes make various related amendments to existing website communication provisions in the Building Societies Act 1986 Act which require a person to agree how to receive notification that a document is available online. Each of the amendments will remove references to agreeing the *manner of notification*, so that there is simply a duty on the society to notify the person that a document is available online.

Financial year

15 (1) Section 117 (financial year of building societies) is amended as follows.

This will effectively replace section 117 of the Building Societies Act 1986 relating to the financial year of a building society.

(2) For subsection (1) substitute —

“(1) A building society’s financial years (apart from its final financial year) are determined according to its year-end date in each calendar year. For provision about a building society’s final financial year, see subsection (1G).

A society’s financial year is determined by its year-end date in each year, except for its final financial year for which there is specific provision in subsection (1G).

(1A) The year-end date of a building society established before 25th August 1894 is —

(a) the date up to which, as at 1st January 1987, the accounts of the society were annually made up, or

(b) if the society has, at any time before the day on which subsection (1) comes into force (“the relevant day”), altered its financial year in exercise of a power within subsection (1B), 31st December.

This sets out the existing position that a society established before 25 August 1894 can have any financial year-end date, unless it has exercised a power to alter it to 31 December.

(1B) The powers referred to in subsection (1A)(b) are —

(a) the power conferred by section 70(2) of the Building Societies Act 1960,

(b) the power conferred by section 128(2) of the Building Societies Act 1962, and

(c) the power conferred by subsection (3) of this section (as it had effect immediately before the relevant day).

This lists the powers that have been available to a society established before 25 August 1894 to alter its financial year-end date to 31 December.

(1C) The year-end date of a building society established on or after 25th August 1894 and before the relevant day is 31st December.

This sets out the existing position that a society established on or after 25 August 1894, but before this amendment comes into force, has a year-end date of 31 December.

(1D) The year-end date of a building society established on or after the relevant day is the last day of the month in which the anniversary of its establishment falls.

A society established on or after the date this amendment comes into force will have a year-end date that is calculated by reference to the anniversary of its establishment.

(1E) The financial year of a building society established before the relevant day is the period of 12 months ending with the year-end date of the society (but see subsection (1G)).

This sets out the existing position that the financial year of a society established before the date this amendment comes into force is the 12 month period up to its financial year-end date.

(1F) In the case of a building society established on or after the relevant day —

(a) the initial financial year of the society shall be the period of more than 6 months, but not more than 18 months, beginning with the date of its establishment and ending with its year-end date, and

(b) its subsequent financial years are successive periods of 12 months beginning immediately after the end of the previous financial year and ending with its year-end date (but see subsection (1G)).

The financial year of a society established on or after the date this amendment comes into force will be: in the case of its initial financial

year, a period of more than 6 months but less than 18 months; and, for each subsequent financial year, a 12 month period.

(1G) The final financial year of a building society is a period of less than 12 months that begins immediately after the end of the previous financial year and ends with the date as at which the society makes up its final accounts.

The final financial year of a society will be the period less than 12 months from the date of its last year-end date to the date of its final accounts. It applies to all societies, irrespective of when a society was established.

(1H) This section has effect subject to section 117A (alteration of financial year)."

The provisions which set out the existing position on year-end date and financial year, described above, are subject to the new provision in section 117A which allows any society to alter its year-end date in certain circumstances.

(3) Omit subsections (2) and (3).

Existing subsections (2) and (3) of section 117 will be deleted as they become obsolete with the new provisions described above.

16 After section 117 insert –

"117A Alteration of financial year

New section 117A will allow a society to alter its financial year-end date to any date in the year by notifying the Financial Conduct Authority. As described above, this is different from the present situation, whereby societies must either have a year-end date of 31 December or, in the case of older societies with a different year-end date, can only change their financial year end date to the 31 December.

(1) A building society may by notice given to the FCA specify a new year-end date.

(2) A notice given under subsection (1) has effect in relation to –

(a) the financial year in which the notice is given ("the current financial year"), and

(b) subsequent financial years.

(3) The notice must state whether the current financial year –

(a) is to be shortened, so as to come to an end on the first occasion on which the new year-end date falls or fell after the beginning of the current financial year, or

(b) is to be extended, so as to come to an end on the second occasion on which that date falls or fell after the beginning of the current financial year.

Societies must provide certain information in the notice to the FCA to specify a new year-end date.

(4) A notice extending a building society's financial year is not effective if given less than 5 years after the end of an earlier financial year of the society that was extended under this section.

Societies may only change their year-end date once every five years.

(5) A financial year of a building society may not be extended so as to exceed 18 months and a notice under subsection (1) is ineffective if the current financial year as extended in accordance with the notice would exceed that limit."

Societies may not extend their year-end date so it exceeds 18 months.

17 In Schedule 20 (transitional and saving provisions), omit paragraph 16 (existing financial years).

Makes consequential changes to the Building Societies Act 1986 to remove existing provision (transitional arrangements) relating to financial years which are no longer required.

18 The amendments made by paragraphs 15 to 17 have effect in relation to financial years beginning on or after the day on which those amendments come into force."

This provides that new sections 117 and 117A will apply to financial years beginning on or after the day on which the amendments come into force.