The Bank's accounts

The *Banking Department* accounts for the year ended 28 February 1987 show an operating profit, before exceptional items, of £76.2 million, compared with £87.8 million in 1985/86. During the year, there was one exceptional item—a release of £6.3 million from the provision for payments under indemnity given to Minories Finance Ltd[1] (formerly Johnson Matthey Bankers Limited).

After a payment in lieu of dividend of £30.0 million (compared with £39.4 million) and a tax charge of £18.3 million, the profit transferred to reserves amounts to £34.2 million, compared with £43.9 million last year.

The current cost profit before tax and dividend was £74.3 million (some £8.2 million less than in the historical cost accounts). After tax and dividend payments the current cost profit was £26.0 million.

The *Issue Department* accounts are shown on page 32. In accordance with the Currency and Bank Notes Act 1928, the assets of the Issue Department comprise securities of an amount in value sufficient to cover the fiduciary note issue. The profits of the note issue are payable to the Treasury and amounted to £1,362.9 million compared with £1,396.8 million in 1985/86.

(1) In 1984/85 a provision of £34.0 million was made for payment under indemnity to Johnson Matthey Bankers Limited. An earlier release of £7.0 million from the provision was made in 1985/86.

Report of the Auditors

To the Governor and Company of the Bank of England

We have audited the accounts of the Banking Department on pages 19 to 31, and the statements of account of the Issue Department on page 32, in accordance with approved Auditing Standards.

In our opinion

1 The accounts on pages 19 to 29 give a true and fair view of the state of affairs of the Banking Department at 28 February 1987 and of the profit and source and application of funds for the year then ended.

2 The statements of account on page 32 present fairly the outcome of the transactions of the Issue Department for the year ended 28 February 1987 and its balances at that date.

3 The abridged supplementary current cost accounts of the Banking Department on pages 30 and 31 have been properly prepared in accordance with the policies and methods described in notes 1 to 3.

DELOITTE HASKINS & SELLS

Chartered Accountants

London
7 May 1987

Banking Department

Profit and loss account
for the year ended 28 February 1987

1986			1987
£000			£000
87,787	Operating profit before exceptional items	(*Note 2*)	76,202
	Exceptional items:		
7,000	Movement in provision for payment under indemnity		6,276
11,528	Surplus over book value on disposal of investment		—
106,315			82,478
39,400	Payment to the Treasury under Section 1(4) of the Bank of England Act 1946	(*Note 4*)	30,000
66,915	Profit before taxation		52,478
22,957	Taxation	(*Note 5*)	18,321
43,958	Profit transferred to reserves	(*Note 7*)	34,157

The notes on pages 22 to 28 form part of these accounts.

Banking Department

Balance sheet: 28 February 1987

1986			1987	
£000			£000	£000
14,553	**Capital**	(*Note 6*)	14,553	
447,200	**Reserves**	(*Note 7*)	581,611	
461,753				596,164
	Current liabilities			
3,935,507	Public deposits	(*Note 8*)	1,923,560	
850,237	Bankers' deposits	(*Note 9*)	954,061	
1,164,419	Other accounts		1,111,840	
39,400	Payable to the Treasury	(*Note 4*)	30,000	
5,989,563				4,019,461
6,451,316				4,615,625

The notes on pages 22 to 28 form part of these accounts.

Balance sheet: 28 February 1987

1986 £000			1987 £000	£000
	Liquid assets			
10,651	Notes and coin		4,242	
226,042	Cheques in course of collection		173,664	
4,738,495	Treasury and other bills	(*Note 10*)	2,393,458	
4,975,188				2,571,364
399,562	**Investments**	(*Note 11*)		402,106
718,236	**Advances and other accounts, less provisions**			1,198,528
125,080	**Subsidiary companies**	(*Note 12*)		100,123
233,250	**Premises and equipment**	(*Note 13*)		343,504
6,451,316				4,615,625

R Leigh-Pemberton *Governor*

George Blunden *Deputy Governor*

Adrian Cadbury *Director*

H C E Harris *Chief of Corporate Services*

Notes on the Banking Department accounts

1 Accounting policies

a Form of presentation of accounts
Although the Bank's constitution is not governed by the Companies Act 1985, the accounts have been prepared so as to comply with the requirements of that Act and the Statements of Standard Accounting Practice issued by the accountancy bodies in so far as they are appropriate.

The accounts have been prepared on the historical cost basis of accounting, modified to include the revaluation of certain fixed assets and in accordance with Sections 257 to 260 of, and Schedule 9 to, the Companies Act 1985.

b Treasury, Local Authority and other bills
Treasury, Local Authority and other bills are stated at cost plus accrued interest.

c Investments
Securities of, or guaranteed by, the British Government, and Other securities are stated in the balance sheet at cost less provisions.

Profits and losses on realisation are taken to profit and loss account in the year in which they arise.

d Premises and equipment
Freehold and leasehold premises are stated at a professional valuation on an open-market value for existing use basis as at 28 February 1987. No account is taken of the liability to taxation which could arise if the premises were disposed of at their revalued amounts.

Equipment is stated at cost less accumulated depreciation. Fully depreciated items have been written out of the accounts.

Depreciation, on a straight line basis, is charged as follows:

Freehold premises	over the estimated future life
Leasehold premises	over the period of lease or estimated future life
Computers	over periods ranging from three to five years
Other equipment	over periods ranging from three to twenty years

e Bad and doubtful debts
Appropriate provision is made for bad and doubtful debts.

f Foreign currency translation
Assets and corresponding liabilities in foreign currencies are translated into sterling at the exchange rates ruling at 28 February.

g Commitments on behalf of the Treasury
Commitments in foreign currencies and gold, or on a gold basis, undertaken in the name of the Bank for account of the Treasury, principally in the course of operating the Exchange Equalisation Account, are not included in these accounts as the Bank is concerned in such transactions only as agent.

h Deferred tax
Deferred tax is provided on the liability method in respect of all material timing differences except where it is expected that the relevant timing difference will not reverse in the foreseeable future.

j Retirement benefits

The profit of the year bears the cost of providing pensions in respect of current service. Any unfunded liability in respect of past service disclosed by an actuarial valuation is met either by a special contribution to, or by an increase in the current contribution rate of, the relevant pension fund.

The Bank of England Pension Fund is reviewed annually and full actuarial valuations are obtained every three years. A full valuation is taking place as at 28 February 1987 and the results will be available in the autumn. A full actuarial valuation is obtained yearly in respect of the Court Pension Scheme.

There is no unfunded liability in respect of past service.

2 Operating profit

The operating profit is arrived at after taking account of the following:

1986 *£ thousands*		1987 £ thousands
	Income	
	Interest:	
543,497	Treasury and other bills	186,465
	Securities of, or guaranteed by, the	
48,455	British Government	48,067
33,385	Advances	22,843
	Interest and dividends:	
1,695	Listed securities	1,912
6,095	Unlisted securities	5,389
47,940	Charges for services to the Government	50,080
2,136	Rents	2,798
	Charges	
488,367	Interest paid to depositors	123,160
600	Directors' emoluments (*Note 3*)	627
70	Auditors' remuneration	85
46	Hire of computers and other equipment	49
8,458	Depreciation of premises and equipment	9,631
189	Loss on disposal of fixed assets	44

3 Directors' and employees' emoluments

The aggregate emoluments of the Governors and Directors for the year ended 28 February were:

1986		1987
£11,230	Fees	£11,392
*£589,108**	Other emoluments, including remuneration of Governors and Executive Directors and contributions to Directors' Pension Scheme	£615,763

*Includes £14,067 paid by a subsidiary company.

The Governor's emoluments, excluding pension contributions, totalled £99,550 (1986 £90,085).

The emoluments of the highest paid Director, for whom the Bank made no pension contributions, totalled £106,307. In the year ended 28 February 1986 no Director's emoluments exceeded those of the Governor.

The following table shows for the year ended 28 February the number of other Directors and of employees of the Bank receiving remuneration in excess of £30,000 (excluding pension contributions), within the bands stated.

1986 *Directors*	*1986* *Employees*		1987 Directors	1987 Employees
10		£0–£ 5,000	12	
1		£10,001–£15,000	—	
1		£15,001–£20,000	—	
—	*93*	£30,001–£35,000	—	122
—	*42*	£35,001–£40,000	—	58
—	*24*	£40,001–£45,000	—	28
—	*21*	£45,001–£50,000	—	27
—	*11*	£50,001–£55,000	—	17
—	*4*	£55,001–£60,000	—	7
4	*2*	£60,001–£65,000	—	2
1	—	£65,001–£70,000	3	3
—	—	£75,001–£80,000	1	—

The aggregate remuneration of the employees of the Bank was £72.5 million (1986 £66.6 million).

4 Payment to the Treasury

1986		1987
£ thousands		£ thousands
18,750	Payable 5 April	14,650
20,650	Payable 5 October	15,350
39,400		30,000

5 Taxation

The charge for taxation comprises:

1986		1987
£ thousands		£ thousands
14,050	UK corporation tax at an average rate of 35.416% (1986 40.416%) based on the profits of the year	14,721
469	Income tax on franked investment income	517
4	Prior year adjustment	(534)
8,434	Deferred tax	3,617
22,957		18,321

The deferred tax liability of £10,376,000 is included in Other accounts and is comprised as follows:

1986		1987
£ thousands		£ thousands
(2,987)	Short-term timing differences	376
9,746	Accelerated capital allowances	10,000
6,759		10,376

Tax of £2,600,000 (1986 £nil) has not been provided in respect of further accelerated capital allowances as the provision at 28 February 1987 is considered adequate.

The potential liability for deferred taxation in respect of capital gains on unrealised revaluation surpluses less deficits, which is not provided in the accounts, is £28,600,000 (1986 £8,300,000).

6 Capital

The entire capital comprising £14,553,000 of Bank Stock is held by the Treasury Solicitor on behalf of Her Majesty's Treasury.

7 Reserves

			£ thousands
	General reserve	Revaluation surplus	Total
Balance at 1 March 1986	286,017	161,183	447,200
Retained profit of the year	34,157	—	34,157
Revaluation deficit on property sold during year	—	396	396
Surplus on revaluation of properties	—	99,858	99,858
Balance at 28 February 1987	320,174	261,437	581,611

8 Public deposits

Public deposits are the balances on government accounts, including Exchequer, National Loans Fund, National Debt Commissioners and dividend accounts.

9 Bankers' deposits

1986 *£ thousands*		1987 £ thousands
673,702	Cash ratio deposits	740,281
176,535	Other deposits	213,780
850,237		954,061

10 Treasury, Local Authority and other bills

1986 *£ thousands*		1987 £ thousands
144,170	British Government Treasury bills	94,115
219,448	Local Authority bills	36,337
4,374,877	Other bills	2,263,006
4,738,495		2,393,458

11 Investments

1986 £ thousands *Book value*	1986 £ thousands *Valuation*		1987 £ thousands Book value	1987 £ thousands Valuation
377,043	*462,066*	Securities of, or guaranteed by, the British Government	379,593	473,677
		Other securities:		
7,487	*41,506*	Listed	7,487	53,617
15,032	*60,779*	Unlisted	15,026	54,026
399,562	*564,351*		402,106	581,320

Valuation represents middle-market values except for unlisted investments which are at Directors' valuation.

The principal holdings of equity share capital included in Other securities are as follows:

1986 *Percentage held*		1987 Percentage held
	Over 20%	
27	Agricultural Mortgage Corporation p.l.c. shares of £1 Share capital and reserves as at 31 March 1986 £35,191,000 Profit for the year ended 31 March 1986 £2,784,000	27
29	Portals Holdings p.l.c. ordinary stock Share capital and reserves as at 31 December 1986 £89,277,000 Profit for the year ended 31 December 1986 £12,752,000	28

As a matter of policy, the Bank does not seek to influence the above companies' commercial or financial decisions.

Both the above companies are incorporated in Great Britain.

1986		1987
	Under 20%	
15	Investors in Industry p.l.c. shares of £1 (Incorporated in Great Britain)	15
10	Bank for International Settlements shares of 2,500 Swiss gold francs (25% paid) (Incorporated in Switzerland)	10

12 Subsidiary companies

This comprises:

1986		1987
£ thousands		£ thousands
92,082	Investments in subsidiary companies	92,082
32,998	Amounts owing by subsidiary companies	8,041
125,080		100,123

(a) Minories Finance Ltd (formerly Johnson Matthey Bankers Limited)

At 28 February 1986, the Bank held the entire issued capital of Johnson Matthey Bankers Limited (JMB), comprising 50 million £1 ordinary shares and 25 million redeemable £1 shares, together with £25 million of variable rate subordinated unsecured loan stock. The loan stock was redeemed at par on 21 May 1986. The redeemable shares are redeemable at par on 30 September 1995. Interest of £0.7 million received on the loan stock has been dealt with in the profit and loss account on page 19. Following the sale of the JMB group's principal business the company changed its name to Minories Finance Ltd (MFL) on 11 August 1986.

The Bank gave an indemnity to JMB in respect of losses expected to arise on the ultimate realisation of its loan book as at 30 September 1984. Half this liability was offset by amounts receivable from a number of banks and members of the London gold market under a related counter-indemnity given by them to the Bank. At 28 February 1986 the amount paid and provided in the Bank's accounts under the indemnity was £27 million. The indemnity was determined as at 31 March 1986 at a total cost to the Bank of £20.7 million and accordingly the over-provision has been credited to the profit and loss account.

MFL has followed a programme of realising its assets and sold its principal business to Mase-Westpac on 18 May 1986 at a premium of £17.5 million over net value of the assets and liabilities transferred. MFL's other subsidiaries have also been sold at an aggregate premium over their net asset values of £6.2 million, leaving the company to realise its remaining outstanding loans and advances. The Bank is party to normal warranties and indemnities given by MFL in connection with the disposals. The net asset value of MFL at 28 February 1987 exceeds the cost of the Bank's investment.

The Auditors' report on MFL's accounts for the year ended 30 June 1986 stated that 'the group is currently, or may become, party to claims against or by third parties which may involve substantial amounts'. No account has been taken of these claims as it is not practicable to judge the outcome at this stage. Having consulted the company's legal advisers, the directors of MFL consider that the claims against the group are without merit.

Third party proceedings, involving claims in substantial amounts have been instituted against the Bank in connection with the affairs of MFL. In the opinion of the Directors, based on legal advice, the Bank has a good defence against these claims. Accordingly, no provision has been made.

The accounts of MFL have not been consolidated with those of the Bank because, in the opinion of the Directors, it would be misleading to include its assets and liabilities with those of the Banking Department in view of the circumstances of the acquisition of the company by the Bank and the company's realisation policy.

(b) Other subsidiaries

Investments in subsidiary companies, all of which are wholly owned and registered in England, are stated in the Bank's balance sheet at cost (which is not in excess of the net tangible assets of the subsidiaries) and include:

BE Services Ltd	5,000 shares of £1
EBS Investments Ltd	100 shares of £1
The Securities Management Trust Ltd	1,000 ordinary shares of £1
Slater, Walker Ltd	100,000 ordinary shares of £1 10,000,000 deferred shares of £1
Debden Security Printing Ltd	100,000 ordinary shares of £1

The accounts of EBS Investments Ltd and Slater, Walker Ltd have not been consolidated with those of the Bank because, in the opinion of the Directors, it would be misleading to consolidate their assets and liabilities with those of the Banking Department in view of the circumstances of the acquisition of these companies by the Bank through involvement in the support operations. The accounts of BE Services Ltd, The Securities Management Trust Ltd and Debden Security Printing Ltd have not been consolidated with those of the Bank as the amounts are considered to be not material.

The net aggregate profits of the subsidiary companies attributable to the Bank, which have not been dealt with in the accounts of the Banking Department, and which are stated by reference to audited accounts are as follows:

1986 *£ thousands*		1987 £ thousands
2,356	For the year ended 28 February 1987	2,768
20,563	Since acquisition	23,331

Included within Current liabilities is a total of £3,001,000 (1986 £2,095,000) due, in the normal course of business, to subsidiary companies.

13 Premises and equipment

£ thousands

	Freehold premises	Leasehold premises (50 years and over unexpired)	Leasehold premises (under 50 years unexpired)	Equipment	Total
Cost or valuation					
At 1 March 1986	143,196	79,448	2,068	37,623	262,335
Additions	7,054	1,299	—	13,895	22,248
Disposals	(1,868)	—	—	(1,736)	(3,604)
Adjustment in respect of fully depreciated assets	—	—	—	(4,003)	(4,003)
Surplus/(deficit) on revaluation	39,343	44,353	(2,013)	—	81,683
At 28 February 1987	187,725	125,100	55	45,779	358,659
Accumulated depreciation					
At 1 March 1986	9,941	4,134	313	14,697	29,085
Charge for the year	2,798	1,054	99	5,680	9,631
On disposals	(164)	—	—	(1,219)	(1,383)
Adjustment in respect of fully depreciated assets	—	—	—	(4,003)	(4,003)
Written back on revaluation	(12,575)	(5,188)	(412)	—	(18,175)
At 28 February 1987	—	—	—	15,155	15,155
Net book value at 28 February 1987	187,725	125,100	55	30,624	343,504
Net book value at 28 February 1986	*133,255*	*75,314*	*1,755*	*22,926*	*233,250*
Cost or valuation at 28 February 1987 comprised:					
At 1987 valuation	187,725	125,100	55	—	312,880
At cost	—	—	—	45,779	45,779
	187,725	125,100	55	45,779	358,659

The figures relating to property interests reflect a professional valuation of Bank freehold and leasehold premises by St Quintin, Chartered Surveyors, as at 28 February 1987, on an open-market value for existing use basis.

Contracts for capital expenditure authorised by the Directors and outstanding at 28 February 1987 totalled £27,167,081 (1986 £6,114,280). Further capital expenditure authorised at that date, but not contracted for, is estimated at £6 million (1986 £26 million).

14 Transactions with Directors

The following particulars are given relating to transactions, arrangements and agreements entered into by the Bank of England with Directors, and persons connected with the Directors, of the Bank:

	Number of Directors	Total amount £ thousands
Loans	4	140

There were no quasi loans or other credit transactions that would be required to be shown under the Companies Act 1985. None of the Directors had a material interest, directly or indirectly, at any time during the year in any other significant transaction or arrangement with the Bank or any of its subsidiaries.

15 Charitable donations

Charitable donations during the year amounted to £143,000; no political contributions were made.

16 Contingent liabilities

Contingent liabilities, offset by corresponding obligations of third parties, arise in the normal course of business. In addition there are forward contracts for the purchase and sale of foreign currencies. It is not envisaged that any irrecoverable liability will arise from these transactions.

Since 1930 there has also been a contingent liability, denominated in Swiss gold francs, in respect of uncalled capital on the Bank's investment in the Bank for International Settlements. The sterling equivalent of this liability based on the gold market price on 28 February 1987 was £220 million (1986 £195 million). There are further contingent liabilities, excluding the matters referred to in Note 12, of £21 million (1986 £20 million).

17 Date of approval

The Court of Directors approved the accounts on pages 19 to 31 on 7 May 1987.

Banking Department

Statement of source and application of funds for the year ended 28 February 1987

1986 £000		1987 £000
	Source of funds	
87,787	Operating profit before exceptional items	76,202
	Adjustment for items not involving the movement of funds:	
8,646	Depreciation, net of losses on disposal of fixed assets	9,675
—	Other	(6,878)
96,433	Funds generated by operations	78,999
	Funds from other sources:	
1,929	Repayment of taxation	8
11,535	Disposal of Other securities	—
84	Disposal of premises and equipment	2,177
75,000	Repayment from subsidiary	25,000
184,981		106,184
	Application of funds	
15,346	Payment of taxation	15,437
14,089	Payment under indemnity	4,935
25,300	Payment to the Treasury	39,400
75,100	Investment in subsidiaries	—
14,342	Purchase of premises and equipment	22,248
40,804	Increase/(decrease) in working capital (see below)	24,164
184,981		106,184
	Analysis of increase/(decrease) in working capital	
76,420	Current assets	(2,401,280)
(244,718)	Advances and other accounts	480,293
(2,730)	Advances to subsidiary companies	43
(171,028)		(1,920,944)
	Less:	
(211,832)	Current liabilities, excluding taxation and payment to the Treasury	(1,945,108)
40,804		24,164

Banking Department

Current cost profit and loss account for the year ended 28 February 1987

1986 *£ millions*				1987 £ millions
106.3	Operating profit as in historical cost accounts			82.5
	Current cost adjustments:			
0.8	Additional depreciation charge	(*Note 2*)	3.3	
—	Fixed asset disposal		(0.3)	
6.8	Monetary working capital	(*Note 3*)	5.2	8.2
98.7	Current cost operating profit			74.3
	Payment to the Treasury under Section 1(4) of the Bank of			
39.4	England Act 1946			30.0
59.3	Current cost profit before taxation			44.3
23.0	Taxation			18.3
36.3	Current cost profit for the year			26.0

Current cost balance sheet: 28 February 1987

1986 *£ millions*			1987 £ millions
14.5	Capital		14.5
567.8	Reserves	(*Note 4*)	667.6
582.3			682.1
5,989.6	Current liabilities		4,019.4
6,571.9			4,701.5
4,975.2	Liquid assets		2,571.4
479.3	Investments		487.2
718.2	Advances		1,198.5
125.1	Subsidiary companies		100.1
274.1	Premises and equipment	(*Note 5*)	344.3
6,571.9			4,701.5

The notes on page 31 form part of these accounts.

1 Basis

The current cost information has been prepared on the basis of current cost asset valuations and the operating capital maintenance concept. The current cost information should be read in conjunction with the notes to the historical cost accounts.

2 Accounting policies

(a) Except as indicated below, the accounting policies adopted have been the same as those described in note 1 on pages 22 and 23.

(b) Assets and liabilities are included in the current cost balance sheet on the following bases:

Premises—The figures relating to property interests reflect a professional valuation of Bank freehold and leasehold premises by St Quintin, Chartered Surveyors, as at 28 February 1987, on an open-market value for existing use basis.

Equipment—The majority of the figures for equipment were calculated by using *Price Index Numbers for Current Cost Accounting* produced by the Central Statistical Office.

Figures for the remainder (mainly computer assets) were calculated with reference to suppliers' current price lists.

Investments—British Government stocks are stated at cost less provision; other securities are at market or Directors' valuation.

Other assets and liabilities—These are stated at the amounts shown in the historical cost accounts.

(c) Additional depreciation has been charged on premises and equipment in respect of the difference between the depreciation based on the current replacement cost and the depreciation charge in the historical cost accounts.

3 Monetary working capital adjustment

The adjustment has been calculated by applying the change in the UK retail price index during the year to the average of the opening and closing totals of net monetary assets. British Government stocks have been treated as monetary items and included at book value in this calculation.

4 Reserves

	1987 £ millions
Balance at 1 March 1986	567.8
Surplus on revaluation of premises, equipment and investments	68.6
Monetary working capital adjustment	5.2
Current cost profit for the year	26.0
Balance at 28 February 1987	667.6
Reserves comprise:	
Current cost reserve	172.6
Revenue reserve	233.6
Revaluation reserve	261.4
	667.6

5 Premises and equipment

1986 *£ millions* *Net*		1987 £ millions Gross	 Depreciation	 Net
247.2	Premises	312.9	—	312.9
26.9	Equipment	69.3	37.9	31.4
274.1		382.2	37.9	344.3

Issue Department

Account for the year ended 28 February 1987

1986		1987	
£000		£000	£000
	Income and profits:		
196,163	Securities of, or guaranteed by, the British Government	371,576	
1,248,844	Other securities	1,039,747	
191	Other receipts	18	1,411,341
	Expenses:		
29,498	Cost of production of Bank notes	30,685	
15,199	Cost of issue, custody and payment of Bank notes	14,623	
3,744	Other expenses	3,162	48,470
1,396,757	Payable to the Treasury		1,362,871

Statement of balances: 28 February 1987

1986		1987	*1986*		1987
£000		£000	*£000*		£000
	Notes issued:		*11,015*	Government debt	11,015
12,309,767	In circulation	12,846,075		Other securities of, or guaranteed by, the British	
10,233	In Banking Department	3,925	*2,023,271*	Government	1,252,867
			10,285,714	Other securities	11,586,118
12,320,000		12,850,000	*12,320,000*		12,850,000

Notes:

1 The income and profits, and value of securities, include the effects of the quarterly revaluation of marketable securities, in accordance with the requirements of the National Loans Act 1968. The last such valuation was made at 26 February 1987.

2 The Court of Directors approved the above statements of account on 7 May 1987.

R Leigh-Pemberton *Governor*

George Blunden *Deputy Governor*

Adrian Cadbury *Director*

H C E Harris *Chief of Corporate Services*

Banking Act 1979

Annual report by the Bank of England 1986/87

This report on the exercise by the Bank of its functions under the Banking Act 1979 during the year to 28 February 1987 is presented to the Chancellor of the Exchequer, and by him to Parliament, pursuant to section 4(1) of the Act.

Annual report under the Banking Act 1979

Annual report by the Bank of England: 1986/87

The opening section of last year's report, 'Developments in the system of banking supervision', summarised the measures which would be implemented to strengthen bank supervision in the United Kingdom, following the findings and recommendations of the Leigh-Pemberton Committee on Banking Supervision[(1)] and the proposals contained in the White Paper[(2)] subsequently issued by the Government. This year's report concentrates on the progress made in 1986/87 and looks forward to developments in the current year including, notably, enactment of the new Banking Bill.

I The Board of Banking Supervision

The Board of Banking Supervision is an important element of the new arrangements, offering expert, practitioner-based advice to the Governor on all matters concerning banking supervision. It has met monthly since June 1986 following agreement with the Chancellor of the Exchequer that it should operate before its formal establishment upon the enactment of the Banking Bill.

The Board's own Annual Report appears on pages 79 to 81 as an Annex.

II Market developments and supervisory issues

The past year has been challenging for bank managements and supervisors alike, with considerable developments in supervision taking place against a background of rapid structural change in banking and financial markets.

Systemic developments, together with strategic changes, have affected core banking business and taken many institutions into new areas. While a few of the largest UK banks are aiming to provide both commercial and investment banking services globally and are moving towards the universal banking pattern familiar in Europe, others are continuing to concentrate on traditional banking operations or at least have less ambitious investment banking strategies. The medium-sized banks are even more diverse, with some aiming to become global securities houses, some adopting specialist investment banking strategies and others emphasising retail financial services.

Although previously homogeneous classes of institution are beginning to fragment, the following analysis of British banks looks at two groups of broadly comparable institutions: the eight largest British banks and the members of the Accepting Houses Committee.[(3)] This classification is becoming less apt as the structure of the UK banking system changes but is reasonable for a review of the past five years.

The figures reflect the aggregate position of the two groups of banks and are not averages of individual banks' positions.

Profitability

British banks have been changing their structures

(1) *Report of the Committee set up to consider the System of Banking Supervision* (Cmnd 9550).
(2) *Banking Supervision* (Cmnd 9695).
(3) Appendix I contains definitions of the terms used in Part II and identifies sources of information. Not all the columns in the tables balance, on account of rounding.

and strategies during a period of improving profitability and capital ratios, as shown below:

Large British banks: earnings

	1986	1985	1984	1983	1982
Pre-tax profits (£ billions)	3.80	3.25	2.48	2.22	1.98
Post-tax profits (£ billions)	2.45	1.76	1.11	1.42	1.45
Pre-tax return on equity (per cent)	24.5	24.3	19.2	17.1	17.2
Post-tax return on equity (per cent)	15.8	13.2	8.5	10.9	12.5
Pre-tax return on total assets (per cent)	1.19	1.09	0.85	0.88	0.91

Profits before tax have steadily improved and there has been a considerable increase in the return achieved on shareholders' funds since 1982. For the years to 1984, this may be partly explained by increased gearing on shareholders' funds: the ratio of total borrowings (including deposits *and* all subordinated debt) to shareholders' funds (plus minority interests) rose from 19.2 to 23.2 between end-1982 and end-1984.

During 1985 and 1986, gearing (on shareholders' funds) fell back to 16.9 while the return on total assets sharply increased. This suggests that the continuing improvement in return on equity may be partly attributable to a combination of a higher return from on-balance-sheet assets and the growth of off-balance-sheet business (with the associated increase in fee income), which on the whole is not currently captured in the Bank's risk asset ratio and has therefore probably been undertaken without significant capital allocations (see below).

Throughout the period, banks have been aiming to improve capital ratios by issuing debt eligible for inclusion in the capital base for supervisory purposes. There has in consequence been a steady rise in levels of capital gearing (that is, long-term subordinated debt to shareholders' funds); from 27% at end-1982 to 62% at end-1986. This balance sheet restructuring will probably have helped to underpin the improved return on equity while at the same time enabling banks to increase their risk asset ratios (see below).

The after-tax picture has been significantly affected by variable effective tax rates. The 1984 decline in post-tax profits and profitability was principally caused by substantially higher effective tax rates following that year's Finance Act. Since then, the tax rate has been declining with the gradual reduction in corporation tax rates and, in 1986, on account of significant transfers from non-tax-allowable general provisions to specific provisions. The post-tax return on equity has accordingly been rising faster than the pre-tax return since 1984.

In the case of the AHC members, increased levels of corporate finance business and, to a lesser extent, investment management income accounted for much of the rise in earnings in 1985 and are expected to produce still better results in 1986:

AHC earnings[(a)]

	1985	1984	1983	1982
Pre-tax profits (£ billions)	0.37	0.26	0.23	0.21
Post-tax profits (£ billions)	0.24	0.15	0.14	0.15
Pre-tax return on equity (per cent)	24.5	20.2	19.5	19.0
Post-tax return on equity (per cent)	16.2	11.9	11.7	13.7

(a) The AHC data reflect the aggregate position of the supervised banks and not of the wider financial services groups. In some cases, some operations have been transferred during the period out of the bank to other parts of the group.

Capital ratios

Large British banks: capital ratios

£ billions	1986	1985	1984	1983	1982
Total assets	334.6	303.1	315.7	271.1	243.1
Weighted assets	251.7	236.0	245.4	208.0	179.8[(a)]
Adjusted capital base	26.3	23.0	18.6	16.9	13.7[(a)]
Risk asset ratio (per cent)	10.5	9.7	7.6	8.1	7.6[(a)]

(a) Excluding the TSB.

The late 1970s and early 1980s saw a decline in banks' capital ratios, among both British and foreign banks, prompting the G10 Governors to call in 1982 for an improvement. In the United Kingdom, the recovery was delayed by the 1984 fall in earnings and the need to make substantial deferred tax provisions on account of the changes to capital allowances in that year's Finance Act. This was, however, followed by two years of substantial improvement so that, over the three years to end-1986, the eight largest banks' aggregate capital resources grew considerably faster (56%) than total assets (23%).

This is largely the result of greater retentions combined with substantial issues of perpetual subordinated debt, which qualified as a primary capital component for the first time in 1985, although in some cases improved earnings have made substantial rights issues feasible:

Large British banks: sources of new capital[a]

£ billions	1986	1985	1984	1983	1982
Retained earnings	1.87	1.35	0.77	0.99	1.12
Share issues[b]	1.32	0.70	0.28	0.25	—
Primary perpetual debt issues	1.35	4.05	—	—	—
Non-primary perpetuals	(0.10)	(0.23)	1.20	—	—
Term subordinated debt	(0.29)	0.05	1.29	0.68	0.45
Other	0.10	—	—	—	—
	4.25	5.92	3.54	1.92	1.57

(a) Banks' capital has also been affected by, inter alia, property revaluations, bad debt provisioning policies and changes in deferred tax provisions.
(b) Principally rights issues but in 1986 including the net proceeds (so far received) of the TSB flotation.

The AHC ratios have also improved, again through retentions from increased earnings and the issue of primary perpetual debt:

AHC: capital ratios

£ billions	1986	1985	1984	1983	1982
Total assets	30.0	24.7	24.5	22.1	18.4
Acceptances	4.2	3.5	3.6	2.9	2.9
Weighted assets	18.6	16.2	16.0	12.7	11.4
Adjusted capital base	2.3	1.7	1.4	1.2	1.1
Risk asset ratio (per cent)	12.3	10.4	8.7	9.1	9.3

Capital adequacy: the quality of assets and capital

In assessing the recent improvements in capital ratios, it is important to note that, at present, the risk asset ratio does not build in the risks arising from a wide range of off-balance-sheet exposures, which have grown considerably in recent years. Some of the new capital should therefore be regarded as supporting this business (see Part VIII below).

The make-up, and therefore the risk profile, of banks' balance sheets has also been changing (see below). For example, there has been an increase in lending to the personal sector for house purchase, which tends to be high quality business (see Part III below). On the other hand, the average quality of loan portfolios may have fallen following the loss of a certain amount of new prime name company business to the capital markets.

The main uncertainty regarding asset quality, however, is the value of banks' claims on a number of heavily indebted countries and the adequacy of the provisions made against those claims. Since 1982 the total of general and specific provisions, domestic and international, has been rising as a proportion of customer advances, partly reflecting increased provisions against sovereign lending. In 1986 banks made significant transfers from general to specific provisions against their exposures to problem debtor countries.

Finally, capital adequacy depends on the quality of banks' capital, as measured by the amount of primary capital relative to total capital.

Large British banks and AHC: capital constituents

£ billions	1986	1985	1984	1983	1982
Shareholders' funds	19.28	15.41	13.41	14.13	12.62
Preference shares	0.04	0.04	0.03	0.02	0.02
Primary perpetuals	5.80	4.12	—	—	—
General provisions	1.42	1.82	1.86	1.31	0.81
Minority interests	0.45	0.40	0.78	1.08	0.93
Primary capital	26.98	21.79	16.08	16.54	14.38
Secondary capital	5.85	6.21	6.80	4.27	3.25
Total capital	**32.83**	**28.00**	**22.87**	**20.81**	**17.63**
Of which (per cent):					
Primary capital	*82.2*	*77.8*	*70.3*	*79.5*	*81.6*
Secondary capital	*17.8*	*22.2*	*29.7*	*20.5*	*18.4*

As the table shows, following the dip in 1984, the proportion of total capital represented by primary capital has returned to its 1982 level. Increased retentions have helped greatly, but the improvement is due principally to the £6 billion of perpetual debt issued since 1985, and the resulting shift away from term debt which had previously been growing sharply. (With difficult secondary market conditions, the new issue market in perpetuals has effectively been closed in recent months, but this has not of itself affected the high quality capital characteristics of subordinated perpetuals.)

Business trends

(a) Loan portfolios

The make-up of banks' loan portfolios has changed considerably in recent years. Since widespread international debt problems emerged in 1982, new syndicated lending to sovereign and overseas borrowers has declined and many of the most highly rated corporate borrowers have tended to look directly to the bond markets rather than to the banks for finance. (In some cases, the British banks have been able to continue to share in this business by acting as managers and underwriters. In doing so they have competed against the overseas securities houses, which were not participants in the syndicated lending market.)

Banks have also placed greater emphasis on managing the shape of their loan portfolios, with some swapping international debt and ceding other types of loan in order to reduce credit risks. At the same time, banks have been trying to increase the liquidity of their portfolios, which has probably been helped by the increased securitisation and hence marketability of financial assets.

Banks have, however, remained an important direct source of working capital finance for companies and, in addition, last year there was a slight reversal of earlier trends, with a rise in the arrangement of syndicated credits for borrowers in OECD countries.

There is perhaps therefore a risk of exaggerating the changes in banks' business. This may apply particularly to the AHC members. For many the nature of their banking activities has developed, with some moving from leasing and syndicated lending to the provision of customised products, but as a group their total lending to third parties (together with acceptance business) and hence the use of their balance sheets has in fact increased from £8.3 billion at end-1983 to £11.1 billion at end-1986. Intra-group loans have also risen, largely to fund new operations.

An important growth area for the 'Large British banks' has been the domestic personal sector. Their lending for house purchase has more than doubled over the past four years and now accounts for around one-fifth of total sterling advances. It has increased even more rapidly than other personal lending, which has itself almost doubled since 1982:

Large British banks: personal lending

£ billions, *percentages in italics*	1986	1985	1984	1983	1982
Total lending for house purchase	20.6	16.8	14.0	12.7	8.3
As percentage of personal advances	*53.9*	*52.0*	*50.9*	*52.5*	*47.1*
As percentage of total sterling advances	*22.2*	*20.7*	*19.7*	*19.8*	*15.3*
Other lending to persons	17.6	15.5	13.5	11.4	9.3
As percentage of total sterling advances	*19.0*	*19.2*	*19.0*	*17.9*	*17.2*

Just as the banks have emerged as competitors for the building societies in the residential mortgage market, the banks are in turn likely to face competition in the non-mortgage consumer lending market from those societies which utilise the provisions of the Building Societies Act 1986 enabling them to widen their activities. This will increase already intense competition which, together with the rise in individuals' financial commitments, could lead to tighter margins and greater risks.

(b) Funding

The increased commitment of many banks to the residential mortgage market may be partly attributable to more stable funding. The recent introduction of high-interest-bearing personal accounts by the major British retail banks has helped in this respect, with amounts deposited offsetting—and to some extent bringing about—the fall in traditional 7-day savings accounts and allowing banks to limit the recourse which they might otherwise have had to the wholesale markets. Non-interest-bearing current accounts have held up well, however, their attraction increased for personal customers by the introduction of free banking for those who stay in credit.

(c) Income sources

These business developments have started to show through in sources of income, with a relative fall in the contribution of net interest income and an increase in fees and commissions. This trend is particularly marked for the AHC, principally on account of record corporate finance and underwriting profits:

AHC: sources of income

£ millions	1986[a]	1985	1984	1983
Net interest	252	227	218	182
Foreign exchange dealing	60	43	29	25
Investment trading	(9)	19	15	17
Fees and commissions	426	367	291	219
Other	225[b]	71	62	56
	954	727	615	499

(a) Including annualised nine-month figures for some banks.
(b) The large 'other' item in 1986 reflects a few banks' significant profits from the realisation of long-term investments.

To a lesser extent trading, fees and other income has also become more important for the largest four UK banks, with fees increasing by almost 75% since 1982 (although growth has recently been dampened by the move to 'free-if-in-credit-banking'):

Four London clearers' sources of income[a]

£ billions	1986	1985	1984	1983	1982
Net interest	8.3	7.8	7.5	6.5	5.9
Foreign exchange	0.4	0.3	0.3	0.2	0.2
Fees and commissions	3.3	3.0	3.0	2.5	1.9
Other	0.6	0.5	0.5	0.3	0.4
	12.6	11.6	11.3	9.6	8.4

(a) This and the following table cover the Barclays, Lloyds, Midland and National Westminster groups.

The interest margins (net interest income/average interest earning assets) secured by the four London clearers from both their domestic and international operations have, however, remained fairly stable since 1982 (after a decline in domestic margins in 1981 and 1982 when nominal interest rates fell).

Four London clearers' interest margins

Percentages	1986	1985	1984	1983	1982
Domestic	5.49	5.58	5.52	5.46	5.91
International	1.96	2.11	2.14	2.13	2.10

At around $5\frac{1}{2}$%, domestic margins are more than double international margins, reflecting higher spreads in domestic business together with the continued value of the 'endowment' effect of large sums held in non-interest-bearing UK current accounts. In addition, international loan portfolios include a higher proportion of low margin advances to top sovereign and company borrowers.

Diversification: securitisation and investment banking

In part, the trends emerging in income sources reflect the major developments of recent years: the growth of off-balance-sheet business, product innovation, increasing participation in the securities markets and banks' moves into investment banking and securities trading and distribution, both in the United Kingdom and overseas.

As highlighted above, banks' off-balance-sheet business has grown significantly over the past few years, often through the use of new instruments and normally with an element of risk for the banks. The supervisory response to such new products and services can affect their development. For example, in April 1985 the Bank incorporated banks' underwriting commitments under Note Issuance Facilities in the risk asset ratio, which probably accelerated the trend towards non-underwritten eurocommercial paper programmes. The coming period should see the introduction of capital requirements for off-balance-sheet business generally (see Part VIII below).

The banks' commitment to diversification and, in particular, to the securities markets became apparent in the stream of strategic stakes and acquisitions in the period leading up to Big Bang. Four of the 'Large British banks' have taken such stakes in or acquired a total of seven former Stock Exchange brokers and jobbers. Ten of the AHC members have acquired (or taken significant shareholdings in) twenty Stock Exchange member firms. As an indicator, this underestimates the interest in the securities markets since a significant number of banks have opted to establish securities operations by hiring skilled and experienced staff rather than by making acquisitions. In addition, many of the 'Large British banks' and AHC members have for many years been active as issuing houses in the domestic capital markets and as managers, distributors and market-makers in the Eurobond markets, where they compete with overseas securities houses as well as foreign commercial banks with securities operations here.

Diversification and the increasing involvement in domestic and international securities markets have, however, raised a number of prudential issues, in particular the assessment of risk and the quality of earnings. On the one hand, looked at in the round, diversification may reduce a bank's overall risks by achieving greater balance in its portfolio of exposures. A broader base may also help to stabilise earnings where different activities experience different peaks and troughs.

On the other hand, while the risks from taking on large credit exposures may continue to represent the most serious threat to many banks' stability, it is clear that trading losses incurred in investment banking and securities operations can significantly damage the earnings of even the largest institutions and will need to be very carefully controlled by the more modestly capitalised houses.

In addition, the overall risks of banking groups could rise from their being exposed to clients or sectors from a range of their activities; for example, if they are providing loan finance to a company, underwriting its capital market issues and trading its securities.

Diversification: organisation and corporate structures

The most significant single event of 1986/87 was Big Bang, shortly before which banks were able to take their holdings in Stock Exchange member firms over 29.9%. In most cases banks chose to make 100% acquisitions, so that in future years the earnings and assets of their securities arms will be fully consolidated. These changes, which of course were widely expected, contributed to a series of corporate restructurings and reorganisations which were already in train. The ground has not yet settled but so far levels of functional integration vary considerably as do banks' divisional structures: a recent trend is towards market segmentation by type of client. Delivery systems (for example, the clearers' branch network) are also changing. Formal legal structures are equally variable and do not always mirror a bank group's functional and managerial arrangements.

Although there are no formal banking supervisory requirements on group structures and organisation, they are nevertheless important to the Bank's supervision as inappropriate or weak arrangements can lead to poor performance and, in particular, to poor risk controls and internal systems, reducing the ability of group management to direct the business effectively. The Bank therefore addresses structural issues, often as part of its consolidated supervision of bank groups (see Part IX below).

In addition, legal structure and functional organisation are relevant to the arrangements being put in place to ensure co-operation between banking and other financial services supervisors, particularly given the number of bank groups which are now headed by a holding company with investments in a number of businesses, banking being only one.

III Supervisory concerns and responses

These recent trends in banking markets have produced the following general issues for bank supervisors:

- the assessment of new types of risk and, in particular, the need to incorporate new activities into capital adequacy ratios
- the ability of managements to monitor and control their new activities and to ensure that adequate systems are in place and are properly used
- co-operation between supervisors, international as well as domestic, and covering other financial services as well as banking.

In addition, 1986/87 saw a range of issues relating to specific groups of banks.[1]

Domestic licensed institutions

Following a number of revocations and a few failures among the population of small domestic licensed institutions during the early 1980s (see Part XI below), enhanced monitoring by the Bank has effectively raised standards for this group, particularly in the area of systems, controls and management capability.

At the same time, some smaller institutions have recently come under pressure on account of market developments. In particular, it has been difficult for them to match the consumer lending terms offered by the larger banks and other lenders without compromising on asset quality.

In the face of tougher competitive conditions and the tighter supervisory regime, a number of smaller institutions have been reassessing the benefits of keeping a licence, with some withdrawing from deposit-taking. These have typically been individually or family controlled locally-based businesses which have experienced difficulty in meeting the standards of management and control systems required for authorised deposit-taker status.

By contrast, other companies concentrating on personal lending have been growing rapidly, often attracting outside capital. The Bank carefully monitors growth rates, using them as one measure for deciding whether to increase its supervisory monitoring.

A previous concern regarding a number of smaller institutions was concentrated loan portfolios. This remains a problem in some cases and the Bank continues to press management to reduce concentrations, but the general picture is much improved. Particular emphasis is also placed on loan book quality, control systems and depth of management, with visits to institutions concentrating on these areas, as described in Part IV below.

With growing interest in the UK financial services industry, licensed institutions have been changing hands more frequently than in the past. In 1986/87, the ownership[2] of some fourteen domestic licensed institutions changed, in four cases following specific encouragement from the Bank to find a solution to problems with their business. Comments made by the Bank may also have played a role in some other cases.

As explained in previous annual reports, the Bank has to be satisfied that the new shareholder-controllers will develop the business prudently and that, under new ownership, the institution will continue to satisfy the other criteria for authorisation.

Overseas institutions

The 1979 Banking Act applies to overseas banks which therefore need to satisfy the statutory criteria for authorisation in order to operate in the United Kingdom.

The Bank's role in the supervision of overseas banks is guided by the terms of the revised Basle Concordat[3] (see the 1983/84 and 1984/85 Annual Reports) which recommends that, as the host supervisor of branches, the Bank should generally look to the parent authority for reassurance about the overall financial soundness and management of an institution.

To meet the requirements of the Act and in the light of the Concordat, the Bank therefore needs a good understanding of the home supervisory regime and to this end it stepped up its bilateral contacts with overseas authorities last year and increased the number of visits to them.

On the occasions where problems arise, in addition

(1) Throughout this report the term 'bank' covers both recognised banks and licensed deposit-taking institutions, except where the contrary is clear from the context.
(2) Ownership in this context means control of 50% or more of voting rights.
(3) *Principles for the supervision of banks' foreign establishments*, issued in June 1983.

to discussing them with the local management of an overseas bank's UK branch, Banking Supervision Division discusses the issues with the parent supervisory authority and the bank's head office so as to ensure that a programme of remedial action is agreed by all concerned. Such cases were discussed with eight overseas supervisors during 1986/87. In general, improvements were needed in lending procedures and controls, and in other control systems and the quality of management information.

Two particular issues have been pursued with overseas banks in recent years. First, the Bank has expressed concern that some institutions did not use objective credit assessment criteria, in some cases relying instead on the 'good name' of the borrower or guarantor.

Second, the Bank encourages branches of overseas banks to diversify their lending away from home country business, so as to avoid undue concentrations of risk and the liquidity difficulties which could arise if problems developed. The Bank has therefore monitored levels of home country lending and, where necessary, has sought to agree with branch management a prudent limit on such business, in the light of the circumstances of the bank and country concerned.

UK institutions' operations overseas

Just as the Bank looks at overseas banks' UK operations, it also looks at UK banks' overseas offices as part of its consolidated supervision (described in Part IX below and more fully in the 1985/86 Annual Report). During 1986/87 officials visited a number of UK banks' offices in the Far East and South East Asia, taking the opportunity to hold discussions with local bank supervisors.

Banks' advisory functions: corporate finance questionnaire

Following evidence of the disturbing role of a few banks in the Guinness/Distillers takeover, the Bank has been reviewing the standards and systems of a wide range of banks' corporate finance operations and in particular the way in which they handle client relationships. It is essential that adequate systems and controls are in place for this type of business and are properly used and that operations are conducted with integrity and in line with best market practice, as lapses could have a material impact on a bank's financial strength, as well as its reputation and standing.

Over seventy banks have so far answered a questionnaire issued in January 1987 covering the functions and structure of their corporate finance divisions, personnel policies and control and compliance arrangements, and on the basis of these answers are currently discussing the management of their corporate finance activities with the Bank.

Consumer credit questionnaire

Bank lending to the personal sector continued to grow rapidly in 1986. The growth of the past few years is not of itself necessarily a matter for supervisory concern, but there are signs that some lenders have adopted more generous approaches to lending than hitherto, for example by lending higher proportions of security or on higher income multiples. This may be associated with a lowering of credit standards which could lead in due course to increased bad debt experience.

Accordingly, a sample of thirty-six institutions have answered a questionnaire issued in January 1987, seeking statistical information on their activities in this area (including arrears experience) and an indication of the terms and conditions (including margins) on which they lend.

Asset sales

There is considerable interest in establishing a secondary mortgage market in the United Kingdom. In particular, a number of banks are considering arrangements whereby they would transfer mortgage loans to a separate vehicle funded from the capital markets. One objective for banks is to reduce their risk assets for supervisory purposes. In order for this to be achieved, the Bank will need to be satisfied that there is no residual credit risk to the ceding bank. The Bank is discussing the details of its policy with the banking community in the light of the Code of Practice drawn up by the joint Whitehall/Industry Secondary Mortgage Market Working Group.

IV Developments in the supervisory system

Investigations, visits and reviews

Last year's report highlighted the Bank's increased use of visits and investigations. There are a number of means available to the Bank to extend its understanding of an institution's business. First, informal (or non-statutory) reviews:

- visits by a divisional manager, together with supporting analysts, to discuss the business generally
- visits to review specific areas by teams usually comprising a seconded banker, a seconded accountant and a member of the permanent staff (see Part XIV below for an explanation of the position of seconded staff)
- information packages prepared and/or independent accountants' reports commissioned by an institution, after discussions with the Bank.

Second, two types of statutory enquiry or investigation used when the Bank considers depositors' interests may be threatened:

- special information packages and/or independent accountants' reports required from an institution under section 16 of the Banking Act
- investigations under section 17 of the Act, usually by a leading firm of chartered accountants.

The visits by seconded staff have become an integral and regular part of the Bank's supervision, supporting the division's discussions with management based on prudential returns. They are designed to improve the Bank's understanding of an institution's operations and management and can last from a few days to over a week, depending on the nature of the business and the purpose of the visit.

Seventy-five informal reviews were conducted during 1986/87 with the agreement of the institutions concerned. The focus was on operating and control systems and loan book quality, with eighteen reviews covering loan books, nine systems and forty-eight both.

Forty-six of these reviews covered domestic institutions. The remaining twenty-nine covered subsidiaries and branches of overseas banks, in some cases following an application to move from the licensed to the recognised tier.

At the Bank's instigation, sixteen institutions agreed to commission accountants to report on various aspects of their business.

On a few occasions the Bank used its formal Banking Act powers to require information or to appoint investigators. Section 16 of the Act was used to require information from one institution and the Bank used its section 17 powers four times to appoint investigating accountants to report on the state and conduct of an institution's business. This was in line with previous years:

Use of section 17 powers

Year to end-February	1987	1986	1985	1984	1983
Number of investigations	4	5	3	4	2

The Bank had the benefit of some form of report in every case where it revoked a licence (see Part XI below).

Timeliness and accuracy of prudential returns

The foundation of the Bank's supervisory system remains regular discussions with management on the basis of prudential statistical returns. Procedures for monitoring the submission and completion of returns have been enhanced, with new computerised systems being introduced last year to help identify banks with a poor reporting record. Seventy-four institutions were asked to improve their reporting standards, usually in fairly minor respects. However, further action did have to be taken in eight cases.

Changes to the Banking Act

A number of minor modifications were made to the

1979 Act during 1986/87. These are summarised in Appendix 5 below. Over the years a substantial number of statutory instruments have been issued under the Act. A list is set out in Appendix 4.

V Policy notices

At the beginning of the year the Bank issued policy notices on consolidated supervision[1] (see Part IX below) and the treatment of subordinated debt in a bank's capital base.[2] Both were described in Part II of last year's Annual Report.

Capital adequacy

Since the 1980 *Measurement of capital* paper was first issued, a number of minor modifications have been made to the risk asset ratio, the cornerstone of the Bank's system for measuring capital adequacy. These were described in a notice (BSD/1986/4) issued in June 1986, which set out changes to the risk weightings given to plant and equipment financed by hire purchase and leasing, holdings of bills, and lending to building societies; and indicated how redeemable preference shares are included in a bank's capital base.

The notice also covered reductions in share capital. The Companies Act 1985 provides for purchases of own shares where, inter alia, shareholders have granted the necessary authority. In all cases, irrespective of the position under company law, banks should seek the prior consent of the Bank before making any reduction in share capital. The Bank will wish to ensure that a bank's capital will still be adequate after any such reduction.

In December 1986, the High Court ruled that UK-incorporated companies can issue multi-currency share capital. The Bank has no objection of supervisory principle to banks issuing ordinary shares in a foreign currency. However, the Bank expects to be consulted in all cases prior to an issue and will take account of the change in the currency make-up of a bank's obligations in supervising foreign currency exposure.

The application of capital adequacy policy continues to be based on setting minimum or 'trigger' risk asset ratios for individual institutions in the light of their particular circumstances, as described in the 1984/85 and 1985/86 Annual Reports. Institutions are expected to observe a prudent margin over their 'trigger' ratios.

The US/UK Convergence Proposals announced in January 1987 represent a very important development in the area of capital adequacy. They are described in some detail in Part VIII below.

VI The Banking Bill

The Banking Bill has completed its passage through both Houses of Parliament. As soon as practicable after Royal Assent, its provisions will be brought into force.

The Bill has a similar structure to the Banking Act 1979 (which will be repealed) but with several material changes following the Leigh-Pemberton Committee report and the subsequent White Paper. The main provisions are summarised below.

Prohibition on deposit-taking

The scope of the prohibition on deposit-taking will remain much the same but, in order to be able to keep abreast of market developments, HM Treasury will be empowered to amend by order the definition of 'deposit' and 'deposit-taking business'.

The Bank will be given new powers to investigate illegal deposit-taking. There will also be powers for the Court, on application by the Bank, to order the early repayment of deposits accepted illegally.

Minimum authorisation criteria and abolition of the two-tier system

The current two-tier system of authorisation (recognised banks and licensed institutions) is to be replaced by a unified system with a single category of authorised institution.

(1) *Consolidated supervision of institutions authorised under the Banking Act 1979* (BSD/1986/3).
(2) *Subordinated loan capital issued by recognised banks and licensed deposit-takers* (BSD/1986/2).

All authorised institutions will have to meet the same statutory prudential requirements. In summary, these are that an institution's directors, controllers and managers are fit and proper persons to hold their positions; that the business is effectively directed by at least two individuals; that, in the case of UK-incorporated institutions, it has as many non-executive directors as are considered appropriate by the Bank, having regard to its circumstances; that the business is conducted prudently—which covers, inter alia, adequate capital, liquidity, provisions for bad and doubtful debts, accounting and other records, and internal controls; that the business is carried on with integrity and the professional skills appropriate to the nature and scale of its activities; and that, when authorisation is granted, the institution has net assets of not less than £1 million.

As under the current 1979 Act, these will be *minimum* statutory criteria and the Bank will retain the discretion to set prudential standards on a case-by-case basis in the light of its assessment of an institution's particular circumstances.

All institutions which are recognised banks or licensed institutions under the 1979 Act (on a day to be specified) will be deemed to be authorised institutions under the new Act.

Banking names and descriptions

A UK-incorporated authorised institution will be permitted to use a banking name provided it has at least £5 million of paid-up share capital and/or undistributable reserves. Institutions authorised following the introduction of the 1979 Act may resurrect any banking name which they then had to drop, irrespective of whether they have £5 million of share capital and reserves.

As at present, authorised institutions from overseas will be entitled to use the name under which they carry on business in their country of origin, but following the move to a single tier of authorisation there will no longer be any need to qualify names with 'licensed deposit taker'.

All authorised institutions will be able to use banking descriptions.

The Bank will be empowered to object to the name or proposed name of an applicant institution where it considers the name is misleading or otherwise undesirable. The Bank will have similar powers to object to proposed name changes by authorised institutions.

Changes of directors, controllers and managers

All institutions will be required to notify the Bank of changes of their directors, controllers and managers. The Bank will however be able to modify this requirement for an institution whose principal place of business is outside the United Kingdom. The definitions of 'controller' and 'manager' are slightly wider than those in the 1979 Act.

In addition, any person who becomes a *significant* shareholder in a UK-incorporated authorised institution will be required to notify the Bank; in brief, a 'significant shareholder' is defined as a person entitled to exercise, or control the exercise of, between 5% and 15% of an institution's voting power (or that of its holding company).

Takeovers and mergers

A person proposing to become a shareholder-controller of a UK-incorporated authorised institution will be obliged to give *advance* notice to the Bank. Similar requirements will apply to existing shareholder-controllers who propose to take their shareholding over 50% or over 75%. The Bank will be empowered to object on prudential grounds.

Failure to give the Bank prior notice or proceeding when the Bank has objected will be criminal offences, which could lead to prosecution. In addition, the Bank will be able to take steps against those who proceed in spite of its objection, for example by freezing voting rights, and on application by the Bank the Court will be empowered to order the sale of the shares concerned.

The Bank will also be able to object to an existing shareholder-controller of a UK-incorporated authorised institution which it considers does not satisfy (or no longer satisfies) the 'fit and proper' requirement. After giving due notice, it will be able to take action in such cases, again including freezing voting rights.

HM Treasury will be empowered to direct the Bank to give a notice of objection to a person proposing to become a shareholder-controller of a UK-incorporated authorised institution where, if the acquisition were to proceed, it could serve a notice of disqualification or restriction on the institution under section 183 of the Financial Services Act 1986. This will effectively enable HM Treasury to block an acquisition on the grounds that the proposed shareholder-controller is from a country which does not offer reciprocal access to UK entities in the field of banking, insurance or investment business.

Large exposures

Authorised institutions whose principal place of business is in the United Kingdom will be obliged to report to the Bank exposures of over 10% of capital and to give *prior notice* of proposed transactions exposing them to the risk of losing over 25% of capital. (See Part VII below which contains summaries of two consultative papers on large exposures issued last year.)

Information and investigations

It will be a criminal offence for any person knowingly or recklessly to provide information for supervisory purposes which is false or misleading in a material particular; and for an authorised institution to fail to provide information in its possession which it knows or has reasonable cause to believe is relevant to the Bank's supervision of it.

The Bank's powers to require information and documents for the purposes of bank supervision are being extended to cover, inter alia, holding companies, subsidiaries, sister subsidiaries, directors, controllers, significant shareholders and managers of authorised institutions. The powers of investigators appointed by the Bank are being similarly increased and provision is made for investigations into the ownership and control of authorised institutions.

Information received by the Bank for supervisory purposes will continue to be subject to strict confidentiality safeguards, but new provision is made for disclosure to other regulatory bodies and government departments (but not the Inland Revenue), adding to the amendments already made to the 1979 Act (see Appendix 5 below).

Auditors

UK-incorporated authorised institutions will be required to notify the Bank of changes in their auditors. An auditor will also have to give notice to the Bank if he resigns, does not seek reappointment, or decides to qualify his opinion on an institution's accounts.

Provision is also made to release auditors (and reporting accountants) from constraints on their disclosing to the Bank information about an authorised institution obtained in the course of their audit (or examination), provided the disclosure is made in good faith and the information is relevant to the Bank's supervision of the institution concerned. (See Part VII below for the Bank's proposals on the role of the accountancy profession in bank supervision.)

Revocations and restricted authorisations

As at present, the Bank will be able to give directions as to the conduct of an institution's business when it initiates revocation procedures. In addition, however, where it has grounds for revocation, the Bank will also have the alternative option of placing restrictions on the business where it considers that remedial action is needed but outright revocation is not warranted.

This is similar to the provision in the 1979 Act which enables the Bank to impose conditions on a licence. However, in future, the Bank will not need to revoke in order to restrict the business and, in contrast to the existing conditional licence (which has a maximum one-year term), a restricted authorisation may either have a limited duration (maximum three years) or no time-limit. A time-limited authorisation may be appropriate where, for example, an institution was conducting a programme of orderly repayment of deposits. The circumstances in which the Bank may exercise its revocation or restriction powers will be somewhat wider than at present.

Deposit Protection Scheme

The Deposit Protection Scheme will be extended to cover all authorised institutions, including those overseas banks now exempt. In addition, the cover is being increased to 75% of the first £20,000 (previously £10,000) of sterling deposits made with an institution's UK offices.

Appeals

Any institution aggrieved by a decision of the Bank to refuse it authorisation, to revoke its authorisation, impose a restriction or give a direction may appeal to a tribunal, whose role will be to determine whether, for the reasons adduced by the appellant, the decision was unlawful or not justified by the evidence on which it was based. Appeals may also be made against a notice by the Bank objecting on prudential grounds to a person becoming or continuing to be a shareholder-controller. Individuals may appeal in their own right against a finding by the Bank that they are not 'fit and proper' to hold their position with an applicant or authorised institution.

Representative offices

Overseas banks proposing to establish representative offices in the United Kingdom will have to give *prior* notification to the Bank; at present, notification is required only after establishment. The Bank will be empowered to object to the name of the institution if it appears misleading (or otherwise undesirable) and to require the provision of information and documents. In addition, HM Treasury will have reserve powers to impose an authorisation and regulatory regime on representative offices.

VII Policy initiatives: consultative papers

Banking Supervision Division issued the following consultative papers during 1986/87:

- Off-balance-sheet business (March 1986)
- Reports to supervisors: requirements for branches of overseas banks (May 1986)
- Large exposures (July 1986)
- Sterling liquidity (July 1986)
- Banks and securities business (July 1986)
- Accounting and other records and internal control systems and the reporting accountants' reports thereon (November 1986)
- Convergence of capital adequacy in the UK and US[1] (January 1987)
- The role of audit committees in banks (January 1987)
- Sterling liquidity (January 1987)
- Large exposures (February 1987)

Each of these papers is still under discussion with interested parties. They are summarised in this and the following two Parts. (A full list of current policy notices and consultative papers issued by Banking Supervision Division, including two consultative papers issued since the Bank's year-end, can be found in Appendices 2 and 3.)

The role of the accountancy profession in bank supervision

Adequate records and control systems are essential for sound banking. Similarly, it is vital that the prudential returns made to the Bank should be complete, accurate and timely. The Bank considers that the accountancy profession has a positive and constructive part to play in this area and, building on the Leigh-Pemberton report and the December 1985 White Paper, last year's Annual Report explained the role envisaged for the accountancy profession in bank supervision. Briefly, for each authorised institution, an independent firm of accountants will prepare three separate reports on various aspects of its business: annually on its internal control systems; annually on its accounting and other records; and, as requested by the Bank, on its prudential statistical returns. These reports will be addressed to the institution concerned and made available to the Bank.

Progress was made during 1986/87 on the

(1) A Bank of England paper issued together with a joint US/UK paper: *Agreed proposal of the United States Federal Banking Supervisory Authorities and the Bank of England on primary capital and capital adequacy assessment.*

implementation of these arrangements. First, as described in Part VI above, the new Banking Bill includes among the minimum criteria for authorisation an express requirement that each institution maintains adequate accounting and other records, and adequate control systems.

In addition, the Bank issued two consultative papers on the role of reporting accountants. The May 1986 paper explained how the arrangements were expected to apply to UK branches of overseas banks and, in particular, recorded the Bank's strong preference that a UK firm of accountants should be responsible for the three reports described above.

The November 1986 paper explained the Bank's approach to the new statutory requirement that banks maintain adequate records and control systems, outlined the matters which institutions should take account of in order to comply with the new legislation and set out how reporting accountants should report to the Bank. The Bank will issue a formal Guidance Note once the Banking Bill has been enacted.

A third paper,[1] issued shortly after the year-end, covered reporting accountants' examinations of prudential returns to the Bank.

The new reporting system can work only if all parties are able to communicate freely and in good faith. As described in Part VI above, the Banking Bill will make this possible, by enabling accountants to disclose information to the Bank without contravening a duty to their clients and, in certain circumstances, enabling the Bank to disclose information to accountants.

A number of pilot examinations designed to test the proposals are currently under way.

The accountancy profession is preparing a guideline on the audit of banks, the reports on accounting and other records and control systems, and the relationship of auditors and reporting accountants with the Bank.

Audit committees and non-executive directors

The 1985 White Paper emphasised the important role of bank audit committees, defined as a sub-committee of the board of directors, usually chaired by a non-executive director, with a general responsibility for ensuring that management is performing satisfactorily in the area of accounts, records, controls, systems and compliance.

The January 1987 consultative paper encouraged the appointment of audit committees and made suggestions regarding their establishment, functions and effective operation. It also described the important contribution which non-executive directors can make to audit committees; as described in Part VI above, once the new Banking Bill is passed, a UK-incorporated bank will have to have as many non-executive directors as the Bank considers appropriate.

Some small authorised institutions may find it difficult to appoint sufficient suitable non-executive directors for an audit committee to be established. The Bank is nevertheless committed to the principle that banks and banking groups should have an audit committee and that, unless there are sound reasons to the contrary, *all* authorised institutions should appoint at least one non-executive director to undertake some audit committee functions.

Large exposures

Experience suggests that large exposures to a single entity (or connected group) are a frequent cause of bank failures and difficulties. For some years, the Bank has placed particular emphasis on controlling and monitoring large exposures in its supervision.

The Bank's policy on large exposures, which will supplement the statutory requirements for notification of exposures, was set out in the July 1986 consultative paper. The Bank believes that an exposure to a single party should not normally

(1) *The reporting accountants' report on Bank of England returns used for prudential purposes*, issued in March 1987.

exceed 10% of a bank's capital base and that those that do need thorough examination and justification; and that no such exposure should exceed 25% of the capital base apart from in the most exceptional circumstances. As described in Part VI above, the Banking Bill will require banks to notify the Bank of '10% exposures' and to give prior notification of '25% exposures'; it does not impose statutory limits on the size of exposures and in fact gives the Bank discretion to determine the capital resources and relevant exposures of an institution for these purposes.

The policy is designed to capture the total exposure to a counterparty (or group of associated counterparties). This will therefore be calculated as the sum of all claims together with, inter alia, undrawn facilities, contingent liabilities, other counterparty risks and equity holdings.

The definition of capital used is the capital base of the bank concerned as defined in the 1980 *Measurement of capital* paper (as amended).

The policy also covers, inter alia, large exposures to borrowers connected with the bank; sectoral and interbank exposures; the special position of bank subsidiaries, where parental capital can sometimes be taken into account; the application to UK bank groups; and the position of UK branches of overseas banks.

The February 1987 consultative paper represented the latest consultative stage in the development of the Bank's approach to large exposures and built on the July 1985 and July 1986 papers. It included some new proposals and also draft instructions for the reporting arrangements.

The latest paper explained how the policy will apply to underwriting commitments. The Bank proposes that underwriting exposures should be reported as the amount of an issue being underwritten. Different rules will apply to lead underwriting: during the underwriting period, exposures will be valued at one sixth of the amount of an issue, with the effect that exposures exceeding 60% of a bank's capital base should be notified to the Bank after they have been undertaken; and those exceeding 150% of capital should be notified in advance. The Bank's approach to individual institutions' lead underwriting exposures will vary according to its assessment of their skills and experience.

Sterling primary liquidity

In September 1986 and ahead of Big Bang, the arrangements were formally ended whereby eligible banks[1] undertook to maintain secured balances (known as 'club money') with the discount houses, gilt-edged jobbers and Stock Exchange money brokers. These arrangements had incidentally played a part in ensuring that the banking system had adequate liquidity and that individual banks maintained a minimum stock of sterling liquid assets. With the termination of this requirement, replacement arrangements were therefore needed on prudential grounds. While these were being prepared, eligible banks were asked not to make any significant changes to their liquidity policies.

Building on the July 1986 consultative paper, the January 1987 paper proposed a list of high quality, or 'primary', sterling liquid assets and that each authorised institution should hold primary liquid assets equivalent to not less than 12% of its gross sterling liabilities with a maturity of sight to eight days.

Institutions at the centre of the banking system will be required to hold this level of primary liquidity directly (as they need to maintain stocks of high quality sterling liquid assets for their own operational purposes). Initially these 'primary liquidity institutions' will be settlement members of the CHAPS and Town Clearing Company Ltd.

Other institutions will be free to choose whether to hold their primary sterling liquidity directly or, alternatively, indirectly in the form of short-term sterling deposits with the UK offices of primary liquidity institutions (which will need to cover these

(1) Banks whose bills are eligible for discount at the Bank of England.

liabilities with additional holdings of primary liquid assets).

It should be emphasised that these proposals supplement the Bank's basic approach to monitoring banks' liquidity, set out in the 1982 *Measurement of liquidity* paper. This rests on the assessment of a bank's maturity mismatch over a series of maturity bands and was most recently described in Part III of the 1984/85 Annual Report.

VIII Convergence: the US/UK proposals

It has been apparent for some years that greater international convergence is needed in banking supervisory standards. This has been widely recognised by bank supervisors and much has already been done in the Basle Supervisors' Committee, the European Community and other regional groupings to promote harmonisation of banking supervisory practices (see Part XIII below).

Towards the end of 1986 the US and UK bank supervisors found themselves at much the same stage in their thinking about capital adequacy, which made it natural to work together to produce a common framework for the measurement and assessment of capital adequacy in their two countries; and to agree a common minimum primary capital ratio which would apply to all banks in both countries. The result was a consultative paper,(1) published jointly by the Bank of England and the US supervisory authorities on 8 January 1987, inviting comments on a proposed agreed framework.

Although they stem from bilateral US/UK discussions, the proposals build on much of the work previously undertaken within the Basle Supervisors Committee and the EC. This multilateral work continues (particularly in the Basle Committee and within the EC) with a view to advancing convergence of capital adequacy standards in a number of countries.

Summary of the proposals

In broad summary, the US/UK joint paper proposes a risk-based framework for measuring banks' capital adequacy focusing primarily on credit risk. It covers *all* on and off balance sheet business with any significant credit risk and is designed to be applied on both a consolidated and an unconsolidated basis.

The agreed proposals are similar to the Bank's existing system of capital adequacy assessment, using a ratio of capital to aggregated weighted assets and exposures as the key measure. The principal changes proposed for the United Kingdom are the stress placed upon primary capital and the inclusion for the first time within the risk ratio of *all* main categories of off-balance-sheet activity giving rise to significant credit risk (which would remedy the gap in the current UK ratio referred to in Part II above).

All transactions giving rise to credit risk would be allocated one of five risk weights—0%, 10%, 25%, 50% and 100%—primarily reflecting the relative creditworthiness of the counterparty to the transaction. Maturity and the existence of cash or government security collateral would also be taken into account in some cases.

Each bank would be required to maintain a ratio of primary capital to total risk assets. For most banks this ratio would exceed a published minimum common to both the United Kingdom and the United States.

While it is proposed to introduce the new system as soon as possible after consultations with other banking supervisors and the banking community, it is likely that not all banks will be able to meet the additional reporting requirements straight away. A transitional period may therefore be necessary during which banks can set up the necessary reporting systems.

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(1) *Agreed proposal of the United States Federal Banking Supervisory Authorities and the Bank of England on primary capital and capital adequacy.*

Off-balance-sheet risk

In recent years, off-balance-sheet business has grown to constitute a significant proportion of banking activity in London, but is presently captured in the risk asset ratio in a piecemeal fashion, with many important items excluded altogether from the calculation, although the Bank does take account of levels of off-balance-sheet business in its broad assessment of capital adequacy. The proposal to include *all* off-balance-sheet activities within the risk asset ratio framework therefore represents a major step forward in the United Kingdom.

The Bank's initial approach to and analysis of off-balance-sheet operations was set out in the March 1986 consultative paper. As the associated credit risks are in principle similar to those arising from on-balance-sheet business, the paper outlined a framework for including off-balance-sheet exposures in the Bank's existing risk asset ratio. The Convergence paper's treatment of off-balance-sheet risk is based on a similar framework.

Under the Convergence proposals, off-balance-sheet activities are incorporated into the risk asset ratio in two steps. First, a 'deemed credit risk equivalent' is derived using a credit conversion factor. This credit equivalent is then weighted according to type of obligor and, where appropriate, other factors, such as the maturity of the instrument, using the rules proposed for on-balance-sheet assets.

The conversion factors range from 100% for instruments/facilities which are direct credit substitutes (such as guarantees and acceptances), through 50% for trading contingencies (such as commercial letters of credit) and committed facilities with over five years' original maturity, down to 10% for short-term commitments (such as borrowing facilities reviewable and unconditionally withdrawable at least annually).

Whereas the conversion factors for commitments and contingent exposures can be expressed as simple fractions of the amount of the facility, the credit exposure to counterparties arising from interest and exchange rate instruments (such as swaps, options, and forward rate agreements) varies with movements in market rates. For each such contract, the credit equivalent amount is therefore calculated as the sum (where positive) of its current market value and an estimate—derived using a formula—of the potential credit exposure arising from prospective movements in rates over its remaining life.

This system and the underlying methodology were described in a second joint US/UK paper(1) issued after the year-end, which also discussed some valuation issues and the concept of netting exposures where a bank has more than one contract with the same counterparty. It is designed to catch the *credit exposure to counterparties* arising out of foreign currency and interest rate contracts and not the risks in running open foreign currency positions or interest rate mismatches.

IX Diversification and banking groups

Consolidated supervision

Last year's Annual Report described the Bank's policy on the supervision of banking groups,(2) which is based principally on consolidated statistical returns and the annual report and accounts of group companies. The Bank expects to hold at least one meeting each year with *group level* management to discuss the overall financial health of the group.

Banks are now required to provide a consolidated balance sheet return (the CBS) and a consolidated supervisory return (the Q7) at six-monthly intervals. They have two months from their reporting date to submit the returns, although those whose business is mainly in the United Kingdom are expected to complete the returns within one month.

(1) *Agreed Proposal: credit equivalent amounts for interest rate and foreign exchange rate related instruments*, issued on 4 March 1987.
(2) Set out in *Consolidated supervision of institutions authorised under the Banking Act 1979* (BSD/1986/3).

Arrangements to deal with supervisory overlap

With the development of diversified and integrated financial conglomerates, the erosion of traditional boundaries between financial markets and the restructuring of the UK securities industry, many groups—and in some cases single institutions—now provide a wide range of financial services. In consequence, a large number of banks and other financial institutions will be supervised by more than one body, particularly once the Financial Services Act regime is implemented, underlining the need for proper co-ordination between supervisors. This has important implications for the Bank's consolidated supervision of banking groups since co-operation is needed with supervisors responsible for non-banking operations.

The 1986 Building Societies and Financial Services Acts and the new Banking Bill make this possible by enabling information exchanges between supervisors, hitherto a constraint on the regulation of diversified financial intermediaries.

(a) Groups

The task of establishing a co-operative framework for supervising financial groups falls to an interdepartmental working group drawn from the Bank, HM Treasury, the Department of Trade and Industry and the Securities and Investments Board (SIB). The Government has endorsed the group's recommendation that the desired degree of co-operation can best be achieved through extra-statutory arrangements.

As explained in Part II of last year's report, while each supervisor will retain its statutory responsibilities, a lead regulator will be appointed for each conglomerate, charged with promoting exchanges of information and co-ordinating any necessary remedial action. During 1986/87, the working group concentrated on identifying conglomerates requiring a lead regulator, deciding the appropriate lead regulator in each case, and agreeing the general procedures to be followed by lead regulators.

(b) Single institutions

Special arrangements are also needed for single institutions subject to multiple authorisation. The Bank has accordingly held discussions with the SIB and a number of prospective Self-Regulating Organisations under the Financial Services Act, with a view to developing arrangements which minimise problems of supervisory overlap. The Bank's July 1986 consultative paper proposed that one supervisor should be delegated to monitor the institution's financial position on behalf of the others, with the Bank normally being the monitoring supervisor for banks. The financial services supervisors would in all cases continue to monitor compliance with their conduct of business rules.

In particular, further work has been undertaken on the position of the many banks undertaking securities business which are likely to require authorisation from The Securities Association. Shortly after the year-end the Bank and The Securities Association issued a draft Memorandum of Understanding under which The Securities Association would normally delegate to the Bank the monitoring of banks' compliance with its securities business capital requirements.

As the Bank monitors banks' capital positions on a quarterly basis, it is proposed that, in order to guard against any competitive inequality which could otherwise arise from The Securities Association requiring more frequent reporting from non-bank securities companies, the Bank should set a capital limitation for each bank's securities business at the beginning of each quarter and should monitor compliance as frequently as The Securities Association requires. Where the capital limitation was breached, the Bank would seek an explanation and would notify The Securities Association of any areas of concern. As appropriate, the Bank would agree any remedial measures with The Securities Association and would ensure their implementation.

Banks and securities business

Market developments have brought about an increase in banks' securities portfolios and trading activities. At present, the risk asset ratio treatment of securities positions is fairly simple, providing a basic proxy for position risk (ie the risk that prices move unfavourably) in a primarily credit risk based measurement of capital adequacy; for example, by giving a 10% weight to British government Treasury bills, despite the absence of credit risk. As reported in the Bank's July 1986 consultative paper, the Bank is reviewing position risk and developing risk coefficients for securities positions.

Under the terms of the draft Memorandum of Understanding with The Securities Association (see above), it is hoped that common risk measures and capital adequacy rules will be agreed for securities business. The Bank's work on position risk is therefore proceeding in consultation with the SIB and The Securities Association, with the aim of producing capital requirements broadly equivalent for banks' and non-banks' securities operations.

Discount houses

The discount houses (which are all authorised under the Banking Act) are now supervised by a new division of the Bank, Wholesale Markets Supervision Division, which was formed in November 1986 and whose operations are described in the Bank's *Report and accounts.* Wholesale Markets Supervision Division has inherited this and some other functions from Money Markets Division. The supervision of discount houses is carried out on the basis described in previous Annual Reports (see in particular the reports for 1983/84 and 1984/85).

Wholesale Markets Supervision Division will also be responsible for supervising some institutions in respect of certain wholesale market transactions; institutions will be exempt from the Financial Services Act in respect of such transactions provided they are on a list drawn up by the Bank. It is proposed that, where an institution on the Bank's list for wholesale market transactions is also authorised under the Banking Act, there will be no additional capital adequacy requirements for such business and extra meetings with the institution should not be required, questions relating to wholesale market transactions normally being covered by the existing supervisory arrangements.

X Authorised institutions

The population of authorised institutions

A list of recognised banks and licensed institutions at the Bank's year-end, showing changes during 1986/87, is attached at Appendix 8. The list is regularly updated and is available from the Bank on request.

The following table shows the number of recognised banks and licensed institutions over the past five years:

End-February	1987	1986	1985	1984	1983
Recognised banks	298	291	290	290	295
Licensed institutions	290	304	315	308	295
	588	595	605	598	590

Of the institutions authorised at end-February 1987, 254 were overseas institutions with UK branches (252 in February 1986), 67 were UK-incorporated subsidiaries of overseas institutions (65 in 1985/86) and 23 were UK-incorporated joint ventures between overseas institutions and, in some cases, between overseas and UK institutions (24 in 1985/86).

The geographical origin of authorised institutions is very wide, with banks from 77 countries having offices here, as shown in Appendix 7. Institutions also vary considerably by size, as shown below:

Total assets of UK-incorporated institutions[(a)]

	Less than £1m	£ 1-5m	£ 5-50m	£ 50-500m	£ 500m-10bn	£ 10bn+	Median size £m	Mean size £m
1983	32	60	78	99	60	5	44	675
1984	26	57	82	91	72	6	54	818
1985	19	52	77	97	70	6	94	896
1986	16	48	78	96	89	6	121	1032

(a) The population is *UK-incorporated* authorised institutions reporting at end-December in each year (and the TSBs before and since their authorisation).

Changes in authorised population

As can be seen below, the level of applications and new authorisations has been fairly steady in recent years, although there was an increase last year:(1)

Year to end-February	1987	1986	1985	1984	1983
Applications	34	25	23	37	36
Authorisations	37	18	28	26	25

In recent years, a number of the institutions applying (and being authorised) have not been 'traditional' banking businesses. Companies wishing to manage money funds or operate budget accounts are notable examples.

Eighteen institutions were granted recognition as banks during 1986/87 (compared with nine in 1985/86). Of these, nine were overseas institutions operating branches (six in 1985/86), four were subsidiaries of overseas institutions (one in 1985/86) and five were other UK-incorporated institutions (two in 1985/86).

Nineteen institutions were granted deposit-taking licences (compared with eighteen in 1985/86). Of these, seven were overseas institutions opening branches (eight in 1985/86) and three were subsidiaries of overseas institutions (two in 1985/86).

Eleven institutions ceased to be recognised banks (eight in 1985/86). Two surrendered recognition after a decision to cease taking deposits in the United Kingdom; eight surrendered recognition as part of group reorganisations, deposit-taking authority either being granted to, or already existing in, a company elsewhere in the group; and Minories Finance Limited was granted a licence following the surrender by Johnson Matthey Bankers Limited of its recognition.

There were thirty-three deletions from the list of licensed institutions (twenty-nine in 1985/86). Eleven followed the grant of recognised status (seven in 1985/86). One arose from outright revocation during 1986/87 and one from a revocation at the end of the previous financial year (there were four deletions from the list of licensed institutions during 1985/86). One conditional licence expired. Nineteen institutions surrendered their licences (eighteen in 1985/86).

XI Use of Banking Act powers

Statutory criteria for authorisation

The interpretation and application of the criteria for authorisation in Schedule 2 to the Act remain as described in previous reports. The Bank's approach to the 'fit and proper person', 'four eyes' and 'prudent manner' criteria was set out in Part V of the 1983/84 Annual Report.

In Part V(iii) of the 1983/84 report, which explained the Bank's interpretation and application of the 'prudent conduct' criterion, the Bank stressed the importance of applicants having established a successful track record in their chosen field. Since then, a small number of applicants have been advised that, in the Bank's view, they did not have sufficient experience. A few of these are currently working to establish a track record.

Revocations

In 1986/87 the Bank used its powers under section 7 of the 1979 Act to replace two full licences with conditional licences, one of which was subsequently revoked.

The Bank also gave notice of its intention to revoke two conditional licences and one full licence but, in each case, the licences either expired or were surrendered before the revocation process had been completed.

In all cases, it appeared to the Bank that some of the criteria in Schedule 2 to the Act were not fulfilled. Two of the cases where the Bank moved to

(1) The totals include applications withdrawn or refused, applications made in one year with authorisation granted in the next, and reapplications/reauthorisations arising out of group reorganisations and movements between tiers.

revoke a conditional licence followed breaches of conditions.

Reasons for concluding that the 'prudent conduct' criterion was not fulfilled included inadequate capital; inadequate liquidity; inadequate provisions against bad and doubtful debts; excessive connected lending; imprudently large exposures; and deficiencies in procedures for credit assessment, taking of security, loan monitoring and control.

In two cases the Bank concluded that directors and controllers were not 'fit and proper' to hold their positions with the institutions concerned; and in another that the 'four eyes' criterion was not fulfilled as only one person was effectively directing the business.

The following table shows the Bank's use of its revocation powers over the past five years:

Section 7 revocations[(a)]

Year to end-February	1987	1986	1985	1984	1983
Revocation of recognition and grant of a conditional licence	—	1	—	1	—
Outright revocation of full licence	1	5	—	—	1
Revocation of full licence and grant of conditional licence	2	2	2	1	1
Revocation of conditional licence and grant of further conditional licence	—	1	—	—	—
Outright revocation of conditional licence	3	—	2	2	—
Outright revocation of transitional licence	—	—	—	—	4

(a) The table includes cases in the year that the Bank's formal notice of revocation was given. In some cases, the revocation will not have taken effect until the following year and in a few cases the institution surrendered (or a conditional licence expired) before revocation took effect. In addition, the Bank has used its powers more than once in respect of a few institutions. It is *not* therefore a record of licences revoked but of the use of the Bank's powers.

It is important to emphasise that the table is not a record of the number of institutions which have experienced difficulties and where the Bank considered that its powers were exercisable, since a number of institutions have surrendered authorisation rather than face revocation.

Appeals

Last year's report recorded that an appeal was in progress against the Bank's decision to revoke a licence. With the Bank's agreement and after further discussions between the Bank and the company, the appeal was subsequently upheld as the grounds cited by the Bank for its action had been met by satisfactory remedies.

During 1986/87, one institution lodged notice of appeal against the revocation of a conditional licence but, in the event, did not pursue the appeal.

One applicant has appealed against the Bank's decision not to grant a licence. The appeal has not yet been heard.

Liquidations

The Bank did not make any applications under section 18 for winding-up orders during 1986/87. However, after the Bank's year-end, the Bank petitioned for a winding-up order in respect of Consumer Credit Investments Ltd., a licensed deposit-taker. A provisional liquidator was appointed.

One licensed institution, Oriental Credit Ltd, went into voluntary liquidation, as did two formerly authorised institutions, Spring Gardens Securities p.l.c. and PL Investments & Savings Ltd, while they still had deposit obligations outstanding. The Deposit Protection Board[(1)] has made, or is in the process of making, payments to depositors in these cases.

The recent pattern of liquidations of authorised institutions (and those formerly authorised with outstanding deposit liabilities) is:

(1) The Deposit Protection Board, a body corporate set up by the 1979 Act, manages the Deposit Protection Scheme. Copies of its report and accounts for the year ended 28 February 1987 can be obtained from the Secretary, Deposit Protection Board, c/o Bank of England, Threadneedle Street, London, EC2R 8AH.

Liquidations

Year to end-February	1987	1986	1985	1984	1983
Section 18 petitions	—	—	1	2	1
Creditor petitions	—	—	1	—	—
Company petitions	—	—	—	—	1
Voluntary	3	—	3	1	—

Enforcement

During 1986/87 the Bank enquired into some forty-five cases of possible breaches of the 1979 Act, mainly relating to possible illegal deposit-taking. In most instances the position was satisfactorily regularised without prosecution, but in a small number of cases charges under section 1 of the Act are being considered with the Director of Public Prosecutions and the police.

A number of developments are in train. First, the Bank will be extending contacts with other enforcement agencies to include the new regulatory bodies seeking recognition as Self-Regulating Organisations under the Financial Services Act.

Second, once the new Banking Bill is enacted, the Bank will have wide powers to investigate illegal deposit-taking. It will also be entitled to apply to the Court for orders directing the repayment of deposits accepted illegally and confiscating profits from illegal deposit-taking, to seek injunctions to prevent contraventions of the legislation by an unauthorised person and to petition the Court for the winding up of illegal deposit-takers.

XII Control of banking names and descriptions

The Bank wrote in May 1986 to several domestic and overseas banking and securities associations asking them to draw the attention of their members to the prohibition which section 36 of the 1979 Act places on the use of terms such as 'investment bank' and 'investment banking'.

XIII The Bank's international role

This report has highlighted the importance of international supervisory co-operation, a key objective of the G10 Basle Supervisors Committee, the European Community and a number of other regional groups. The Bank places great importance on their work and its contribution to them.

The Basle Supervisors Committee

The Committee on Banking Regulations and Supervisory Practices, which normally meets at the Bank for International Settlements in Basle, brings together supervisors from the Group of Ten industrialised countries and Luxembourg under the chairmanship of Mr W P Cooke, an Associate Director of the Bank.

The general objectives of the Committee have been described in previous reports. Great emphasis is placed on the further development of international co-operation between bank supervisors.

The major issues for the Committee during 1986 included capital adequacy, liquidity, off-balance-sheet risk and interest rate risk. The work on capital has been important in developing the joint US/UK proposals (see Part VIII of this report).

In recent years, the Committee has been developing close relations with other supervisory groups. In 1986 a joint meeting was held with supervisors from the Gulf Co-operation Council and members of the Committee participated in meetings with groups from the Caribbean and the SEANZA countries (South East Asia, the Indian sub-continent, New Zealand and Australia). The Committee also maintained contact with the Commission of Banking Supervisory and Inspection Bodies of Latin America and the Offshore Group of Supervisors.

The Amsterdam conference

Bank officials attended the fourth international conference of banking supervisors hosted by de Nederlandsche Bank in Amsterdam in October 1986. The conference was co-chaired by Mr H J Muller, Executive Director of de Nederlandsche Bank, and Mr W P Cooke in his capacity as Chairman of the Basle Supervisors Committee. Some ninety countries were represented.

There was general acceptance of the importance of enhancing supervisory co-operation. Formal discussions centred on two main topics—capital and capital adequacy and the practical application of the principles of the revised Basle Concordat,[1] with particular emphasis on information flows relevant to effective supervision.

The conference agreed on the value of the risk-related approach to capital adequacy measurement, incorporating banks' on and off-balance-sheet business and with assets/exposures weighted according to broad relative measures of perceived risk; and agreed that supervisory efforts should be concentrated on securing agreement both on the highest quality elements of capital and on comparable minimum standards of capital adequacy for international banks.

The conference considered that greater collaboration was needed on information flows. Stress was put on ensuring adequate data flows to parent authorities on large exposures and on asset quality.

The forum also provided a valuable opportunity for personal contact and exchanges of views between supervisory authorities on a range of issues. The next such conference is to be held in Tokyo during 1988.

The European Economic Community

The bank supervisors of the member states of the EC meet together in two groups: the Banking Advisory Committee established under the 1977 First Banking Co-ordination Directive and the Contact Group of EC Supervisory Authorities.

At the June 1985 Milan summit, Heads of Government gave political impetus to the European Commission's proposals on the opening up of the cross-border market in banking services, which form an important part of the overall plan to complete the internal market of the Community by 1992. To this end, the Commission and the Council of Ministers have been active in the field of Community banking legislation.

In December 1986, the Council adopted the Bank Accounts' Directive, which will standardise the preparation and presentation of banks' accounts. In the same month the Commission adopted Recommendations (which do not have the force of law) on large exposures and deposit guarantee schemes.

Draft directives are being discussed on own funds (capital), the winding up and reorganisation of credit institutions and also on mortgage credit (designed to remove obstacles facing mortgage credit institutions wishing to operate in other member states).

In addition, towards the end of 1986 the Commission outlined its thinking on the scope of a Second Banking Co-ordination Directive. This will be designed to harmonise authorisation criteria so as to enable the exercise of rights of establishment and free supply of banking services across the Community's internal borders.

The Banking Advisory Committee and the Contact Group have continued to develop the observation ratios relating to solvency, profitability and liquidity of banking institutions in member states. In addition, at the invitation of the Banking Advisory Committee, the Contact Group is considering and will report on the links and activities of banking institutions in the broader financial spheres of insurance, securities and investment business.

XIV Administration

Structure of the division

An organogram attached at Appendix 6 shows the current structure of Banking Supervision Division. During 1986/87 the senior management resources of the division were strengthened to cater for the increased policy workload.

The operational side of the division was also reorganised. The three groups supervising overseas

(1) *Principles for the supervision of banks' foreign establishments* June 1983: Basle Supervisors Committee.

banks were split into five groups and, since the year end, have been further reorganised into eight groups. The three groups supervising miscellaneous deposit-taking institutions were also split into five groups.

Staff

Staff numbers have increased considerably in recent years:

Banking Supervision Division: staff members[a]

1 March	1987	1986	1985	1984	1983	1979
Managers	27	26	23	20	17	18
Analysts and assistants	115	86	69	64	57	39
Inward secondees	13	6	3	2	1	—
Total	**155**	**118**	**95**	**86**	**75**	**57**

(a) Excluding support staff (secretaries and filists) and not including staff of the Wholesale Markets Supervision Division which, as noted in Part IX, is now responsibile for supervising the discount houses.

During 1986/87 seven staff were recruited with experience in banking and accountancy. The programme of inward secondments has also been developed. The division currently has four secondees from the clearing banks and six from firms of chartered accountants typically for a period of between one and three years.

On average, at end-February 1987, each manager on the operational side of the division was responsible for thirty-three authorised institutions and each analyst was responsible for seven institutions.

At managerial level and above, staff have spent an average of five years in Banking Supervision.

Training

Both the Leigh-Pemberton Committee Report and the White Paper placed great emphasis on the contribution training makes to developing a professional corps of bank supervisors. The division's new training programme is designed to increase awareness of market developments and to improve technical skills. More in-house training was provided in 1986/87. Graduate recruits now spend time on a training group and division members attend internal computer courses and other seminars. Training is also provided at a number of external institutions, including banks, commercial training companies and the Civil Service College. Specially designed courses have been commissioned from outside bodies on company law and accountancy.

The programme of outward secondments is also proceeding. Over the past few years, six members of the division have been on secondment to commercial institutions, including merchant banks and clearing banks. Five members are currently on secondment: one to a merchant bank, one to a clearing bank, one to a firm of chartered accountants and two to the Department of Trade and Industry's Companies Investigation Branch.

Systems

Considerable progress has been made towards modernising the division's technical resources. A further forty-six personal computers were brought into use during 1986/87. A pilot 'office automation' project was also successfully completed and the system is now being expanded to cover the whole division.

In addition, consultants were employed to help specify the requirements for a computerised management information system which would enable efficient and rapid response to policy changes and market innovation. Their report has been accepted and, with their continuing assistance, the system is now under construction.

It will be integrated with the expanded office automation system to provide an on-line database, links with the Bank's other mainframe systems, word processing, electronic communication and management tools and various local processing facilities. Installation of certain features of the combined systems is being phased over the remainder of 1987, with project completion scheduled for early 1988.

Glossary of terms for Part II

Large British banks	Comprises Barclays, Lloyds, Midland, National Westminster, Bank of Scotland, The Royal Bank of Scotland, Standard Chartered and the TSB Group. All data for these banks are consolidated. Calendar-year-end information except for Bank of Scotland, The Royal Bank of Scotland and the TSBs.
AHC banks	Comprises the sixteen members of the Accepting Houses Committee. Most of the data for the AHC refer to solo authorised institution. Earnings and capital data include these banks' hidden reserves.
Pre-tax profits	Profit before taxation but after provisions.
Post-tax profits	Profit after taxation and before extraordinary items; includes amounts attributable to minority shareholders in subsidiary operations.
Return on equity	Percentage ratio of pre/post-tax profits to average shareholders' funds plus minority interests. Shareholders' funds defined as paid-up share capital and reserves. For AHC banks, shareholders' funds includes inner reserves.
Return on total assets	Percentage ratio of pre-tax profits to average total assets.
Gearing	Ratio of total borrowings (including deposits and all perpetual and term subordinated debt) to shareholders' funds plus minority interests. (This is not the same as the gearing ratio defined in the 1980 *Measurement of capital* paper used for capital adequacy assessment.)
Capital gearing	Percentage ratio of the sum of perpetual and term subordinated debt to shareholders' funds and minority interests.
Total assets	Aggregate balance sheet footings.
Weighted assets	Total assets adjusted in accordance with the risk weightings as set out in *Measurement of capital* (as amended).
Adjusted capital base	Shareholders' funds, general provisions and minorities plus all qualifying subordinated loan capital—less: goodwill, equipment, connected lending of a capital nature, investments in subsidiaries and associates, and holdings of bank paper in excess of concession.
Risk asset ratio	Percentage ratio of adjusted capital base to weighted assets.
Retained earnings	Current year's post-tax profits (as defined) after extraordinary items and distributions.
Primary perpetual debt	Qualifying undated subordinated debt that is eligible for inclusion as primary capital under Bank of England rules. Qualifying criteria require that the debt can only be converted into primary capital instruments, is available at all times to absorb losses, and provides for the deferment of interest payments in certain circumstances.

Non-primary perpetual debt	Undated subordinated debt that either fails to qualify as primary capital or is ineligible in that it exceeds 50% of the total capital base less loan stock and intangibles. This debt would form part of a bank's secondary capital.
Term subordinated debt	Subordinated debt with a fixed maturity and satisfying the Bank of England's conditions for secondary capital.
Primary capital	The total of shareholders' funds, minority interests, general provisions and perpetual subordinated debt subject to certain conditions and limits.
Secondary capital	Perpetual subordinated debt not included in primary capital together with term subordinated debt, subject to certain conditions and limits.
Total capital	The sum of primary capital and secondary capital.
Personal lending	Outstanding loans advanced to UK persons, including lending for house purchase and bridging finance. Dates are for mid-November 1982–85 and for end-November 1986. All figures in this table refer to sterling advances to UK residents only.
Net interest	Gross interest income less interest paid on borrowings.
Foreign exchange	Income from foreign exchange dealing.
Other income	Includes investment income.
Interest margin	Net interest income/average interest-earning assets.
Interest spread	The difference between average interest rate earned on assets and average interest rate paid on interest-bearing funds.
Endowment effect	The benefit received by the retail banks from deploying the 'free' funds generated by their non-interest-bearing current accounts.
Sources of data:	Audited financial statements for the large British banks, with the exception of the tables on capital ratios and mortgage lending. AHC data from Bank of England returns.

Current supervisory notices

The following is a list of policy and practice notices issued by Banking Supervision Division which are currently in force.

Title	Date of issue
Measurement of capital	September 1980
Foreign currency exposure	April 1981
Measurement of liquidity	July 1982
Connected lending; accounts; large exposures; fraudulent invitations; floating charges (BSD/1983/1)	April 1983
Foreign currency options	April 1984
Advertising for deposits (BSD/1985/1)	February 1985
Notice on advertising code of conduct	March 1985
Note issuance facilities/revolving underwriting facilities (BSD/1985/2)	April 1985
Statistical notice to monetary sector institutions (released in conjunction with previous paper)	April 1985
Guide for intending applicants for authority to take deposits; revised questionnaires for directors, controllers and managers (BSD/1985/3)	April 1985
Further notice on advertising code of conduct and attachments	November 1985
Large exposures in relation to mergers and acquisitions (BSD/1986/1)	February 1986
Subordinated loan capital (BSD/1986/2)	March 1986
Consolidated supervision (BSD/1986/3)	March 1986
Measurement of capital (BSD/1986/4) (amendments to the 1980 paper)	June 1986
Statistical notice to monetary sector institutions (released in conjunction with previous paper)	June 1986

Current consultative papers

The following is a list of consultative policy papers issued by Banking Supervision Division which are now being discussed with the banking community and other interested parties.

Title	Date of issue
The relationships between the supervisors, auditors and managements of banks	August 1985
Off-balance-sheet business	March 1986
Accountants' reports to supervisors: requirements for branches of overseas banks	May 1986
Large exposures(1)	July 1986
Banks and securities business	July 1986
Sterling liquidity(2)	July 1986
Accounting and other records and internal control systems and the reporting accountants' reports thereon	November 1986
Convergence of capital adequacy in the United Kingdom and United States(3)	January 1987
The role of audit committees in banks	January 1987
Sterling liquidity(2)	January 1987
Large exposures(1)	February 1987
Agreed proposal: credit equivalent amounts for interest rate and foreign exchange rate related instruments(3) Potential credit exposure on interest rate and foreign exchange rate related instruments(3)	March 1987
The reporting accountants' report on Bank of England returns used for prudential purposes	March 1987

(1) These papers should be read in conjunction.
(2) These papers should be read in conjunction.
(3) These papers were issued together and should be read in conjunction.

Banking Act 1979: orders and regulations

The following Statutory Instruments made under the Banking Act are currently in force. (Copies are available from HM Stationery Office.)

1 SI 1979 No 938 (C 26)
The Banking Act 1979 (Commencement No 1) Order 1979

2 SI 1980 No 347
The Banking Act 1979 (Excepted Persons) Order 1980
—The 1819 Savings Banks
—The Crown Agents

3 SI 1980 No 348 (S 35)
The Banking Act 1979 (Scottish Appeals) Regulations 1980

4 SI 1980 No 353
The Banking Act 1979 (Appeals) Regulations 1980

5 SI 1982 No 188 (C 7)
The Banking Act 1979 (Commencement No 2) Order 1982
—Bringing into operation provisions of the Act relating to the Deposit Protection Scheme, the repeal of certain enactments relating to banks and banking and certain consequential amendments and repeals.

6 SI 1982 No 1681
The Banking Act 1979 (Excepted Persons) Order 1982
—Addition to Schedule 1 of certain international organisations including the IBRD, the IMF and the EIB.

7 SI 1982 No 1808
The Deposit Protection Fund (Excluded Institutions) Order 1982

8 SI 1983 No 1100
The Deposit Protection Fund (Excluded Institutions) Order 1983

9 SI 1984 No 897
The Deposit Protection Fund (Excluded Institutions) Order 1984

10 SI 1984 No 1990
The Deposit Protection Fund (Excluded Institutions) (No 2) Order 1984

11 SI 1985 No 220
The Banking Act 1979 (Advertisements) Regulations 1985

12 SI 1985 No 797 (C 12)
The Banking Act 1979 (Commencement No 3) Order 1985

13 SI 1986 No 100
The Banking Act 1979 (Removal of 1819 Banks) Order 1986

14 SI 1986 No 772
The Deposit Protection Fund (Excluded Institutions) Order 1986

15 SI 1986 No 1712
The Banking Act 1979 (Exempt Transactions) Regulations 1986

—Charities
—Church deposit funds
—Industrial and provident societies
—Agricultural, forestry and fisheries associations

—Retail and other co-operative societies
—Solicitors
—Deposits accepted in the course of estate agency work
—Certain public undertakings
—The National Children's Charities Fund Limited
—Commodity brokers and clearing houses
—Members of The Stock Exchange
—Sterling debt securities
—Sterling commercial paper

16 SI 1987 No 64
The Banking Act 1979 (Advertisements) (Amendment) Regulations 1987

17 SI 1987 No 65
The Banking Act 1979 (Exempt Transactions) (Amendment) Regulations 1987

Minor changes to the Banking Act 1979

A number of changes were made to the Act during 1986/87, principally resulting from other legislation.

Amendments

Amendment to section 8 (the Bank's power to give directions when revoking deposit-taking authority)

Section 8 of the Banking Act was amended by section 185(7) of the Financial Services Act 1986. Directions may now be given at any time after a disqualification notice has been served on an institution by the Treasury under the reciprocity provisions of section 183 of the Financial Services Act.

Amendments to section 18 (winding up on petition by the Bank)

Section 18 of the Banking Act was amended by the Insolvency Acts 1985 and 1986, the relevant provisions of which came into force on 29 December 1986.

Section 18 enables the Bank to petition the Court for the winding up of an authorised institution or a formerly authorised institution with deposit liabilities outstanding. Under the original section 18, the Bank was able to petition on the grounds that the institution was unable to pay sums due and payable to its depositors or that the value of the institution's assets was less than the amount of its liabilities. The amended section enables the Bank to petition on the grounds that the institution has defaulted in an obligation to pay any sum due and payable to a depositor or is otherwise unable to pay its debts within the meaning of section 123 of the Insolvency Act 1986. The amendments slightly extend the Bank's powers to petition for winding-up orders against insolvent institutions. The amendments also empower the Court to make a winding-up order against an institution, on petition by the Bank, if it considers it just and equitable to do so.

Amendments to section 19 (the Bank's confidentiality obligations)

The Financial Services Act 1986 amended section 19 of the Banking Act to allow the Bank to disclose confidential information (that is, information to which the provisions of section 19 apply) more widely than before. In consequence, the Bank is now able to pass confidential information to, inter alia, UK insurance or financial services supervisors; the Secretary of State in respect of his Financial Services or Insurance Companies Act functions; inspectors appointed under the Financial Services Act to investigate any possible contravention of sections 1, 2, 4 or 5 of the Company Securities (Insider Dealing) Act 1985; and overseas banking, insurance or financial services supervisors.

On 29 December 1986 provisions of the Insolvency Acts 1985 and 1986 were brought into force which amended section 19 to allow the Bank to disclose information in connection with most proceedings under Parts I to VII of the Insolvency Act 1986 or under Part XVIII or XX of the Companies Act 1985.

In addition, on 1 January 1987, the provision allowing the Bank to disclose confidential information to the Building Societies Commission came into force under the Building Societies Act 1986. From that date, the Bank and the Commission have been able to disclose confidential information to each other in connection with their respective functions.

Orders and regulations

A full list of current orders and regulations is contained in Appendix 4. The following were introduced under the Act during 1986/87:

1986 No 769 The Banking Act 1979 (Exempt Transactions) (Amendment) Regulations 1986
These regulations, which came into operation on 20 May 1986, exempt from the section 1 prohibition on deposit-taking any deposits taken in connection with issues by companies of sterling commercial paper which meets certain specified requirements set out in the regulations. For example, the paper may not be redeemed within seven days but must be redeemed within one year beginning with the date of issue; the shares of the company or its parent guarantor must be listed on The Stock Exchange and its net assets must be not less than £50 million; and the minimum deposit accepted must be £500,000.

1986 No 772 The Deposit Protection Fund (Excluded Institutions) Order 1986
This added the Norddeutsche Landesbank Girozentrale to the list of institutions which are exempt from the requirement to contribute to the Deposit Protection Fund and whose liabilities are not covered by the protection offered by section 28 in the event of insolvency. This order came into operation on 21 May 1986.

1986 No 1712 The Banking Act 1979 (Exempt Transactions) Regulations 1986
These regulations consolidated, with amendments, the Banking Act 1979 (Exempt Transactions) Regulations 1983 as already amended, which prescribed certain transactions to which the section 1 prohibition on deposit-taking does not apply. These revised regulations came into operation on 27 October 1986.

There were five amendments of substance. The first amended the former regulation 8, now regulation 7. Previously the acceptance of a deposit by a co-operative society was an exempt transaction if, amongst other things, at least ninety per cent of the society's shares (by reference both to the total number of such shares and to their nominal value) were held by certain shareholders. The amended regulation requires that at least seventy-five per cent of the votes which may be cast to determine the conduct of the society's affairs and at least ninety per cent of its shares by reference to their nominal value be held by such shareholders.

The second was the omission of the former regulation 9, which concerned the taking of deposits by the British Railways Board as the British Railways Savings Bank; this amendment followed the granting of a licence to the British Railways Savings Company Ltd.

The third concerned the list (now in Schedule 2) of public bodies which are allowed to accept deposits from each other. The list now omits British Airports Authority, British Airways Board, British National Oil Corporation, British Telecommunications and British Gas Corporation, in most cases following privatisation. British Gas p.l.c., British Airways p.l.c. and BAA p.l.c. (which succeeds the British Airports Authority) were listed in Schedule 2 but regulation 10(2) provided that the companies were subject to these provisions only so long as they remain wholly owned by the Crown.

The fourth made fresh provision for members of The Stock Exchange (including traded option brokers) to take account of the ending of the distinction between stockbroking and stockjobbing members.

The fifth substantive amendment enables sterling commercial paper of the minimum redemption value of £500,000 to be issued at a discount and provides, by way of clarification, that the statement referred to in regulation 15(e)(iii) should be made by the company accepting the deposit or its guarantor parent company.

1987 No 64 The Banking Act 1979 (Advertisements) (Amendment) Regulations 1987
These regulations, which came into force on 16 February 1987, amend the Banking Act 1979 (Advertisements) Regulations 1985 so as to exclude from their scope an application form for securities if there is provided with it a statement of the approved listing particulars for the purposes of The Stock Exchange (Listing) Regulations 1984; and also such applications accompanied by a statement of listing particulars for the purposes of any listing

rules made pursuant to section 142(6) of the Financial Services Act 1986.

1987 No 65 The Banking Act 1979 (Exempt Transactions) (Amendment) Regulations 1987
These regulations, which came into force on 16 February 1987, amend the Banking Act 1979 (Exempt Transactions) Regulations 1986. They amend the definition of 'company' and provide a definition of 'the listing rules'. This was in the light of the commencement on 16 February 1987 of Part IV of the Financial Services Act 1986 (concerning the official listing of securities) and the repeal on that date of related provisions.

The following order was made under the Trustee Savings Banks Act 1985:

1986 No 1223 (C36) Trustee Savings Banks Act 1985 (Appointed Day) (No 4) Order 1986
This order, which came into force on 21 July 1986, inter alia, removed trustee savings banks from the list of institutions in Schedule 1 to the Banking Act exempted from the section 1 prohibition on deposit-taking. The exemption was redundant following the granting of recognition to the three banking subsidiaries of the Trustee Savings Bank Group p.l.c.

The following order was made under the Financial Services Act 1986:

1986 No 2246 (C88) Financial Services Act 1986 (Commencement No 3) Order 1986
This order, made on 17 December 1986, brought into force various provisions of the Financial Services Act. Among these is the repeal of paragraph 9 of Schedule 1 to the Banking Act (which excepts from the section 1 prohibition on deposit-taking members of The Stock Exchange in the course of business as stockbrokers or stockjobbers). The paragraph was no longer necessary because of the revised regulation for acceptance of deposits by members of The Stock Exchange referred to above. This provision came into force on 12 January 1987.

Appendix 6
Banking Supervision Division organogram

- **The Governors** — **Board of Banking Supervision**
  - **R D Galpin**, *Executive Director* - - - **W P Cooke**, *Associate Director*
    - - - - S Procter, *Adviser to the Governor*
    - R A Barnes, *Assistant Director, Policy and Resources*
      - D M Sutherland[1], J F Rippon, *Managers, Group 1, Legal including Banking Act Enforcement*
      - R H Farrant, *Senior Manager*
        - J C W Osborn, *Manager, Group 2, General policy*
      - D J Mallett, *Senior Manager, Accountancy and Special Issues*
      - Kingsley Roberts, *Manager, Administration, Staff training*
      - D A Reeves, *Manager, Statistics, Computers, Foreign exchange*
      - C J C Sparkes[2], *Manager, Confidential enquiries*
    - Brian Quinn, *Assistant Director, Head of Banking Supervision*
      - *United Kingdom retail banks and merchant banks*
        - D T R Carse, *Manager, Group 3 major English clearers*
        - J B C Atkinson, *Manager, Group 4, Scottish and other UK clearers*
        - T P Sweeney, *Manager, Group 5, UK merchant banks*
      - B S P Gent, *Deputy Head, Miscellaneous deposit-takers, Remaining UK recognised banks*
        - C J F Ball, *Manager, Group 6, A–Ca*
        - M J Fuggle, *Manager, Group 7, Ch–E*
        - W D R Swanney, *Manager, Group 8, F–I*
        - Miss W M Hyde, *Manager, Group 9, J–O*
        - J C Cleland, *Manager, Group 10, P–Y*
      - J S Beverly, *Deputy Head, Overseas banks—North America and Western Europe*
        - D A Ware, *Manager, Group 11, France, Scandinavia, Belgium and Luxembourg*
        - P J Marr, *Manager, Group 12, USA*
        - Mrs J V Coppel, *Manager, Group 13, Canada, Austria, Germany, Switzerland, Liechtenstein*
        - Miss J M Haddon, *Manager, Group 14, Ireland, Italy, Greece, Netherlands, Portugal, Spain*
      - J W Anderson, *Deputy Head, Overseas banks—Rest of the world*
        - P C Hayward, *Manager, Group 15, Japan, Israel, Turkey*
        - J M Hayden, *Manager, Group 16, Australasia, Indian Sub-Continent, Afghanistan, Eastern Europe, South Africa*
        - C P Mann, *Manager, Group 17, Middle East, Cyprus*
        - R D Chalmers, *Manager, Group 18, Far East, Latin America, Other Africa*

(1) Secretary of Board of Banking Supervision.
(2) Secretary of Deposit Protection Board.

Geographical representation of overseas institutions

The following table shows the geographical origins and status of foreign banks and quasi-banks represented in the United Kingdom at end-February 1987.

Country of ownership	Branch operations	Subsidiary operations	Controlling (15% or more) stake in consortium banks	Representative offices[1]	Total
Afghanistan	—	1	—	—	1
Argentina	1	—	—	1	2
Australia	9	4	—	1	14
Austria	3	—	—	3	6
Bahamas	—	—	—	2	2
Bahrain	2	—	—	4	6
Bangladesh	1	—	—	—	1
Barbados	1	—	—	—	1
Belgium	3	1	—	—	4
Bermuda	—	—	—	2	2
Brazil	4	—	1	6	11
Bulgaria	—	—	—	1	1
Canada	6	4	—	1	11
Cayman Islands	—	—	—	1	1
Chile	—	—	—	1	1
China	1	—	—	—	1
Colombia	—	—	—	1	1
Cuba	—	1	—	—	1
Cyprus	3	2	—	—	5
Czechoslovakia	1	—	—	—	1
Denmark	3	2	—	1	6
Ecuador	—	—	—	1	1
Egypt	2	—	—	—	2
Finland	2	1	2	2	7
France	13	4	1	7	25
German Democratic Republic	—	—	—	1	1
Germany, Federal Republic	14	—	1	3	18
Ghana	1	—	—	—	1
Gibraltar	—	—	—	2	2
Greece	1	—	—	1	2
Hongkong	3	2	1	—	6
Hungary	—	1	—	—	1
India	9	—	—	—	9
Indonesia	1	—	—	3	4
Iran	5	—	1	—	6
Iraq	1	—	—	—	1
Ireland	6	3	—	—	9
Israel	2	2	—	2	6
Italy	10	2	2	22	36
Japan	23	4	2	17	46
Jordan	1	1	1	—	3
Kuwait	1	—	1	2	4
Lebanon	3	—	—	3	6
Liechtenstein	—	1	—	—	1
Luxembourg	2	—	—	4	6
Malaysia	2	—	—	—	2
Mexico	4	—	1	2	7
Netherlands	6	1	—	2	9
New Zealand	2	—	—	—	2
Nigeria	5	—	—	1	6
Norway	1	1	1	1	4
Pakistan	5	—	—	—	5

(1) This covers only those representative offices included in a list published by the Bank.

Country of ownership	Branch operations	Subsidiary operations	Controlling (15% or more) stake in consortium banks	Representative offices[1]	Total
Panama	—	—	—	1	1
Philippines	2	—	—	—	2
Poland	1	—	—	—	1
Portugal	3	—	—	2	5
Qatar	1	—	—	—	1
Rumania	—	—	1	—	1
Saudi Arabia	3	—	1	2	6
Singapore	4	—	—	—	4
South Africa	4	—	—	2	6
South Korea	6	—	—	4	10
Spain	6	1	—	8	15
Sri Lanka	1	—	—	—	1
Sweden	—	5	2	4	11
Switzerland	10	1	1	10	22
Taiwan	1	—	—	—	1
Thailand	3	—	—	—	3
Turkey	2	1	—	5	8
United Arab Emirates	4	—	—	1	5
Uruguay	—	—	—	1	1
United States	39	20	8	16	83
USSR	—	1	—	—	1
Venezuela	—	—	—	2	2
Yemen Arab Republic	—	—	—	1	1
Yugoslavia	—	—	1	8	9
Zambia	1	—	—	—	1
Totals	**254**	**67**	**29[2]**	**168**	**518[3]**

(1) This covers only those representative offices included in a list published by the Bank.
(2) Representing 19 institutions. In addition there are four other consortium banks.
(3) Representing 508 institutions.

Appendix 8

Authorised institutions

List of institutions recognised or licensed at 28 February 1987

1 Recognised banks

ANZ Merchant Bank Ltd.
A P Bank Ltd.
Alexanders Discount p.l.c.
Algemene Bank Nederland N.V.
Allied Arab Bank Ltd.
Allied Bank of Pakistan Ltd.
Allied Irish Banks p.l.c.
Allied Irish Investment Bank p.l.c.
American Express Bank Ltd.
Amsterdam-Rotterdam Bank N.V.
Anglo-Romanian Bank Ltd.
Henry Ansbacher & Co.Ltd.
Arab Bank Ltd.
Arab Banking Corporation B.S.C.
Arbuthnot Latham Bank Ltd.
Associated Japanese Bank (International) Ltd.
Atlantic International Bank Ltd.
Australia & New Zealand Banking Group Ltd.

B.A.I.I. p.l.c.
Banca Commerciale Italiana
Banca Nazionale del Lavoro
Banco Central, S.A.
Banco de Bilbao S.A.
Banco de la Nación Argentina
Banco de Santander, S.A.
Banco de Vizcaya S.A.
Banco di Roma S.p.A.
Banco di Sicilia
Banco do Brasil S.A.
Banco do Estado de São Paulo S.A.
Banco Espirito Santo e Comercial de Lisboa
Banco Exterior—U.K. S.A.
Banco Hispano Americano Ltd.
Banco Mercantil de São Paulo S.A.
Banco Nacional de Mexico S.N.C.
Banco Português do Atlântico
Banco Real S.A.
Banco Totta & Açores E.P.
Bancomer, S.N.C.
Bangkok Bank Ltd.
Bank Julius Baer & Co. Ltd.
Bank Bumiputra Malaysia Berhad
Bank für Gemeinwirtschaft A.G.
Bank Hapoalim B.M.
Bank Leumi (U.K.) p.l.c.
Bank Mees & Hope N.V.
Bank Mellat
Bank Melli Iran
Bank of America International Ltd.
Bank of America N.T. & S.A.
Bank of Baroda
The Bank of California N.A.
Bank of Ceylon
Bank of China
Bank of Cyprus (London) Ltd.
Bank of India
The Bank of Ireland
Bank of London & South America Ltd.
Bank of Montreal
The Bank of New York
Bank of New Zealand
The Bank of Nova Scotia
Bank of Scotland
The Bank of Tokyo, Ltd.
Bank of Tokyo International Ltd.
Bank of Wales p.l.c.
The Bank of Yokohama Ltd.
Bank Saderat Iran
Bank Sepah
Bankers Trust Company
Banque Belge Ltd.
Banque Belgo-Zairoise S.A.
Banque Bruxelles Lambert S.A.
Banque Française du Commerce Extérieur
Banque Indosuez
Banque Internationale pour l'Afrique Occidentale S.A.
Banque Nationale de Paris p.l.c.
Banque Nationale de Paris S.A.
Banque Paribas
Barclays Bank p.l.c.
Barclays de Zoete Wedd Ltd.
Baring Brothers & Co.Ltd.
Bayerische Hypotheken—und Wechsel—Bank A.G.
Bayerische Landesbank Girozentrale
Bayerische Vereinsbank
Berliner Bank A.G.
The British Bank of the Middle East
The British Linen Bank Ltd.
Brown, Shipley & Co.Ltd.

CIC—Union Européenne, International et Cie
Caisse Nationale de Crédit Agricole
Canadian Imperial Bank of Commerce
James Capel Bankers Ltd.
Carolina Bank Ltd.
Cassa di Risparmio delle Provincie Lombarde
Cater Allen Ltd.
Central Bank of India
Charterhouse Bank Ltd.
Chase Investment Bank Ltd.
The Chase Manhattan Bank, N.A.
Chemical Bank
Chemical Bank International Ltd.
Cho-Hung Bank
Christiania Bank og Kreditkasse
The Chuo Trust & Banking Company Ltd.
Citibank N.A.
Citicorp Investment Bank Ltd.
City Merchants Bank Ltd.
Clive Discount Company Ltd.
Clydesdale Bank p.l.c.
Commercial Bank of Korea Ltd.
The Commercial Bank of the Near East p.l.c.
Commerzbank A.G.
Commonwealth Bank of Australia
Continental Illinois National Bank and Trust Company of Chicago
Co-operative Bank p.l.c.
Copenhagen Handelsbank A/S
Coutts & Co.
Crédit Commercial de France
Crédit du Nord
Crédit Lyonnais
Credit Lyonnais Bank Nederland N.V.
Crédit Suisse
Credit Suisse First Boston Ltd.
Creditanstalt-Bankverein
Credito Italiano
The Cyprus Popular Bank

The Dai-Ichi Kangyo Bank, Ltd.
The Daiwa Bank, Ltd.
Den Danske Bank af 1871 Aktieselskab
Den norske Creditbank p.l.c.
Deutsche Bank A.G.
Deutsche Genossenschaftsbank
Discount Bank and Trust Co.
Dresdner Bank A.G.

EBC Amro Bank Ltd.
The English Trust Company Ltd.
Enskilda Securities-Skandinaviska Enskilda Ltd.
Euro-Latinamerican Bank p.l.c.
European Arab Bank Ltd.
European Brazilian Bank p.l.c.

Fidelity Bank N.A.
First City National Bank of Houston
First Interstate Bank of California
First Interstate Capital Markets Ltd.
The First National Bank of Boston
The First National Bank of Chicago
First National Bank of Maryland
First National Bank of Minneapolis
First Wisconsin National Bank of Milwaukee
Robert Fleming & Co.Ltd.
French Bank of Southern Africa Ltd.
The Fuji Bank, Ltd.

Gerrard & National Ltd.
Ghana Commercial Bank
Girobank p.l.c.
Girozentrale und Bank der österreichischen Sparkassen A.G.
Grindlays Bank p.l.c.
Guinness Mahon & Co.Ltd.
Gulf International Bank B.S.C.

Habib Bank A.G. Zurich
Habib Bank Ltd.
Hambros Bank Ltd.

Hanil Bank
Havana International Bank Ltd.
Hessische Landesbank-Girozentrale-
Hill Samuel & Co.Ltd.
C.Hoare & Co.
The Hokkaido Takushoku Bank, Ltd.
The Hongkong and Shanghai Banking Corporation
Hungarian International Bank Ltd.

The Industrial Bank of Japan, Ltd.
InterFirst Bank Dallas, N.A.
International Commercial Bank p.l.c.
International Mexican Bank Ltd.
International Westminster Bank p.l.c.
Irving Trust Company
Istituto Bancario San Paolo di Torino
Italian International Bank p.l.c.

Japan International Bank Ltd.
Leopold Joseph & Sons Ltd.

Kansallis-Osake-Pankki
King & Shaxson Ltd.
Kleinwort Benson Ltd.
Korea Exchange Bank
Korea First Bank
The Kyowa Bank, Ltd.

Lazard Brothers & Co.Ltd.
Libra Bank p.l.c.
Lloyds Bank p.l.c.
Lloyds Bank (France) Ltd.
Lloyds Merchant Bank Ltd.
London & Continental Bankers Ltd.
London Interstate Bank Ltd.
The Long-Term Credit Bank of Japan, Ltd.

Malayan Banking Berhad
Manufacturers Hanover Ltd.
Manufacturers Hanover Trust Company
Marine Midland Bank N.A.
Mase Westpac Ltd.
Mellon Bank, N.A.
Merrill Lynch International Bank Ltd.
Midland Bank p.l.c.
The Mitsubishi Bank Ltd.
The Mitsubishi Trust and Banking Corporation
The Mitsui Bank Ltd.
The Mitsui Trust & Banking Company Ltd.
Samuel Montagu & Co.Ltd.
Morgan Grenfell & Co.Ltd.
Morgan Guaranty Trust Company of New York
Moscow Narodny Bank Ltd.

NCNB National Bank of North Carolina
National Australia Bank Ltd.
National Bank of Abu Dhabi
National Bank of Canada
National Bank of Detroit
National Bank of Greece S.A.
The National Bank of Kuwait S.A.K.
The National Bank of New Zealand Ltd.
National Bank of Pakistan
National Westminster Bank p.l.c.
NatWest Investment Bank Ltd.
Nedbank Ltd.
Nederlandsche Middenstandsbank N.V.
The Nippon Credit Bank, Ltd.
Noble Grossart Ltd.
Northern Bank Ltd.
The Northern Trust Company

Orion Royal Bank Ltd.
Oversea-Chinese Banking Corporation Ltd.
Overseas Union Bank Ltd.

Philippine National Bank
Postipankki (UK) Ltd.
Privatbanken Ltd.
Punjab National Bank

Qatar National Bank S.A.Q.
Quin Cope Ltd.

Rafidain Bank
Rea Brothers Ltd.
Republic Bank Dallas, N.A.
Republic National Bank of New York
Reserve Bank of Australia
The Riggs National Bank of Washington, D.C.
N.M.Rothschild & Sons Ltd.
The Royal Bank of Canada
The Royal Bank of Scotland p.l.c.
Royal Trust Bank

S.F.E. Bank Ltd.
The Saitama Bank, Ltd.
The Sanwa Bank, Ltd.
Saudi International Bank (Al-Bank Al-Saudi Al-Alami Ltd.)
Scandinavian Bank Group p.l.c.
J.Henry Schroder Wagg & Co.Ltd.
Seccombe Marshall & Campion p.l.c.
Security Pacific National Bank
Shanghai Commercial Bank Ltd.
Singer & Friedlander Ltd.
Société Générale
Société Générale Merchant Bank p.l.c.
Sonali Bank
Standard Chartered Bank
Standard Chartered Bank Africa p.l.c.
Standard Chartered Merchant Bank Ltd.
State Bank of India
The Sumitomo Bank, Ltd.
The Sumitomo Trust and Banking Company Ltd.
Svenska Handelsbanken p.l.c.
Swiss Bank Corporation
Swiss Bank Corporation International Ltd.
Syndicate Bank

TSB England & Wales p.l.c.
TSB Northern Ireland p.l.c.
TSB Scotland p.l.c.
The Taiyo Kobe Bank Ltd.
Texas Commerce Bank N.A.
The Thai Farmers Bank Ltd.
The Tokai Bank, Ltd.
The Toronto-Dominion Bank
The Toyo Trust & Banking Company Ltd.

UBAF Bank Ltd.
Uco Bank
Ulster Bank Ltd.
Ulster Investment Bank Ltd.
Union Bank of Switzerland
Union Discount Company Ltd.
United Bank Ltd.
The United Bank of Kuwait Ltd.
United Overseas Bank Ltd.

S.G.Warburg & Co.Ltd.
Westdeutsche Landesbank Girozentrale
Westpac Banking Corporation
Wintrust Securities Ltd.
Württembergische Kommunale Landesbank Girozentrale

The Yasuda Trust and Banking Co.Ltd.
Yorkshire Bank p.l.c.

Zambia National Commercial Bank Ltd.
Zivnostenská Banka National Corporation

2 Licensed deposit-taking institutions

A1 Credit p.l.c.
ANZ Finance Ltd.
Adam & Company p.l.c.
Afghan National Credit & Finance Ltd.
African Continental Bank Ltd.
Airdrie Savings Bank
Aitken Hume Ltd.
Ak International Ltd.
Al Baraka International Ltd.
Al Saudi Banque S.A.
Alliance Trust (Finance) Ltd.
Allied Banking Corporation
Allied Dunbar & Co. p.l.c.
Allied Irish Finance Co.Ltd.
Anglo-Yugoslav (LDT) Ltd.
Arab African International Bank
Arab Bank Investment Co.Ltd.
Argonaut Securities Ltd.
Armada Investments Ltd.
Assemblies of God Property Trust
Associated Credits Ltd.
Associates Capital Corporation Ltd.
Auban Finance Ltd.
Authority & Co.Ltd.
Avco Trust Ltd.

B.C. Finance Ltd.
BMI (Hampshire) Ltd.
Badische Kommunale Landesbank Girozentrale
Banca Nazionale dell'Agricoltura SpA
Banca Serfin S.N.C.
Banco de Sabadell
Banco di Napoli
Banco di Santo Spirito
Bank Handlowy w Warszawie S.A.
Bank Negara Indonesia 1946
Bank of Credit and Commerce International S.A.
Bank of Ireland Finance Ltd.

Bank of New England N.A.
The Bank of Nova Scotia Trust Company (United Kingdom) Ltd.
Bank of Oman Ltd.
Bank of Seoul
Bank Tejarat
Bankers Trust International Ltd.
Banque du Liban et d'Outre-Mer
Banque Worms
The Baptist Union Corporation Ltd.
Barbados National Bank
Barclays Bank Trust Company Ltd.
Barclays Bank UK Ltd.
Thomas Barlow & Bro.Ltd.
Barrie Vanger & Co.Ltd.
Beirut Riyad Bank S.A.L.
Benchmark Trust Ltd.
Beneficial Trust Ltd.
Boston Trust & Savings Ltd.
Bradford Investments p.l.c.
British Credit Trust Ltd.
British Railways Savings Company Ltd.
Bunge Finance Ltd.
Burns-Anderson Trust Company Ltd.
Business Mortgages Trust p.l.c.
Byblos Bank S.A.L.

Canada Permanent Mortgage Corporation (UK) Ltd.
Canara Bank
Castle Phillips Finance Co.Ltd.
Cayzer Ltd.
Cedar Holdings Ltd.
Chancery Securities p.l.c.
The Charities Aid Foundation Money Management Company Ltd.
Charter Consolidated Financial Services Ltd.
Chartered Trust p.l.c.
Charterhouse Japhet Credit Ltd.
Chesterfield Street Trust Ltd.
Citibank Trust Ltd.
City Trust Ltd.
Close Brothers Ltd.
Clydesdale Bank Finance Corporation Ltd.
Combined Capital Ltd.
Commercial Financial Services Ltd.
Consolidated Credits & Discounts Ltd.
Consumer Credit Investments Ltd.
The Continental Trust Ltd.
Coutts Finance Co.
Craneheath Securities Ltd.
Credito Italiano International Ltd.
Cue & Co.
Cyprus Credit Bank Ltd.
Cyprus Finance Corporation (London) Ltd.

Daiwa Europe Finance p.l.c.
Dalbeattie Finance Co.Ltd.
Darlington Merchant Credits Ltd.
Dartington & Co.Ltd.
The Development Bank of Singapore Ltd.
The Dorset, Somerset & Wilts Investment Society Ltd.
Dryfield Finance Ltd.
Duncan Lawrie Ltd.
Dunsterville Allen p.l.c.

E.T.Trust Ltd.
Eagil Trust Co.Ltd.
East Anglian Securities Trust Ltd.
East Midlands Finance Co.Ltd.
Eccles Savings and Loans Ltd.
Edington p.l.c.
Ensign Finance Ltd.
Equatorial Trust Corporation p.l.c.
Everett Chettle Associates
Exeter Trust Ltd.

FIBI Financial Trust Ltd.
Fairmount Trust Ltd.
Family Finance Ltd.
Federated Trust Corporation Ltd.
FennoScandia Ltd.
Financial and General Securities Ltd.
James Finlay Corporation Ltd.
Finova Finance Ltd.
First Bank of Nigeria Ltd.
First Commercial Bank
First Co-operative Finance Ltd.
First Indemnity Credit Ltd.
First National Boston Ltd.
First National Securities Ltd.
Fleet National Bank
Ford Financial Trust Ltd.
Ford Motor Credit Co.Ltd.
Foreign & Colonial Management Ltd.
Forward Trust Ltd.
Robert Fraser & Partners Ltd.

Goldman Sachs Ltd.
Goode Durrant Trust p.l.c.
Gota (UK) Ltd.
Granville Trust Ltd.
H.T.Greenwood Ltd.
Gresham Trust p.l.c.
Greyhound Guaranty Ltd.
Grosvenor Acceptances Ltd.
Gulf Guarantee Trust Ltd.

HFC Trust & Savings Ltd.
Habibsons Trust and Finance Ltd.
The Hardware Federation Finance Co.Ltd.
Harris Trust and Savings Bank
Harrods Trust Ltd.
Harton Securities Ltd.
The Heritable & General Trust Ltd.
Hill Samuel Personal Finance Ltd.
Holdenhurst Securities Ltd.

IBJ International Ltd.
IFICO Trust Ltd.
Industrial Funding Trust Ltd.
The Investment Bank of Ireland Ltd.
Investors in Industry p.l.c.
Investors in Industry Group p.l.c.
Iran Overseas Investment Corporation Ltd.
ItaB Group Ltd.

Jabac Finances Ltd.
Jordan Finance Consortium p.l.c.
Jyske Bank

Keesler Federal Credit Union
Kredietbank N.V.

Laurentian Financial Services Ltd.
Legal & General (Money Managers) Ltd.
Liechtenstein (UK) Ltd.
Little Lakes Finance Ltd.
Lloyds Bowmaker Ltd.
Lloyds Bowmaker Finance Ltd.
Lombard Acceptances Ltd.
Lombard & Ulster Ltd.
Lombard North Central p.l.c.
Lombard Street Investment Trust Co.Ltd.
London and Arab Investments Ltd.
London Law Securities Ltd.
London Scottish Finance Corporation p.l.c.
Lordsvale Finance Ltd.

MLA Finance Ltd.
McNeill Pearson Ltd.
Manchester Exchange Trust Ltd.
W.M.Mann & Co. (Investments) Ltd.
Manufacturers Hanover Export Finance Ltd.
Manufacturers Hanover Finance Ltd.
The Mardun Investment Co.Ltd.
Matheson Trust Co.Ltd.
Medens Trust Ltd.
Meghraj & Sons Ltd.
Mercantile Credit Company Ltd.
Mercury Provident p.l.c.
The Methodist Chapel Aid Association Ltd.
Middle East Bank Ltd.
Midland Bank Finance Corporation Ltd.
Midland Bank Trust Company Ltd.
Midland Montagu Ventures Ltd.
Milford Mutual Facilities Ltd.
Minories Finance Ltd.
Minster Trust Ltd.
Moneycare Ltd.
Moorgate Mercantile Holdings p.l.c.
Mount Credit Corporation Ltd.
Multibanco Comermex S.N.C.
Muslim Commercial Bank Ltd.
Mutual Trust and Savings Ltd.
Mynshul Trust Ltd.

N.I.I.B. Group Ltd.
National Bank of Dubai
National Bank of Egypt
National Bank of Fort Sam Houston
National Bank of Nigeria Ltd.
National Commercial Bank
National Guardian Finance Corporation Ltd.
New Nigeria Bank Ltd.
Nomura International Finance p.l.c.
Norddeutsche Landesbank Girozentrale
The North of Scotland Finance Co.Ltd.
North West Securities Ltd.
Northern Bank Development Corporation Ltd.
Northern Bank Executor & Trustee Company Ltd.
Norwich General Trust Ltd.

Omega Trust Co.Ltd.
Oppenheimer Money Management Ltd.

Österreichische Länderbank A.G.
Overseas Trust Bank Ltd.

PKFinans International (UK) Ltd.
PaineWebber International Trust Ltd.
The People's Trust & Savings Ltd.
Philadelphia National Bank
Philadelphia National Ltd.
Phillips & Drew Trust Ltd.
Pointon York Ltd.
Prestwick Investment Trust p.l.c.
Provincial Trust Ltd.

Rabobank Nederland
(Coöperatieve Centrale Raiffeisen-Boerenleenbank B.A.)
Ralli Investment Company Ltd.
R.Raphael & Sons p.l.c.
Rathbone Bros. & Co.
Reliance Trust Ltd.
Riyad Bank
Roxburghe Guarantee Corporation Ltd.
Royscot Trust Ltd.
The Rural and Industries Bank of Western Australia

S.P.Finance Ltd.
St. Michael Financial Services Ltd.
Saudi American Bank
Schroder Leasing Ltd.
Scottish Amicable Money Managers Ltd.
Seattle-First National Bank
Secure Homes Ltd.
Security Pacific Trust Ltd.
Shawlands Securities Ltd.
Shire Trust Ltd.
The Siam Commercial Bank, Ltd.
Smith & Williamson Securities
Southsea Mortgage & Investment Co.Ltd.
Spry Finance Ltd.
Standard Property Investment p.l.c.
State Bank of New South Wales
State Bank of South Australia
State Bank of Victoria
State Street Bank and Trust Company
Sterling Trust Ltd.
Swiss Cantobank (International)
Swiss Volksbank

TCB Ltd.
T.C.Ziraat Bankasi
The Teachers & General Investment Co.Ltd.
Thames Trust Ltd.
Thorncliffe Finance Ltd.
Trade Development Bank
Treloan Ltd.
Trucanda Trusts Ltd.
The Trust Bank of Africa Ltd.
Tullett and Riley Money Management Ltd.
Turkish Bank Ltd.
Türkiye İş Bankasi A.Ş.
Tyndall & Co.

Ulster Bank Trust Company
Union Bank of Finland Ltd.
Union Bank of India
Union Bank of Nigeria Ltd.
United Dominions Trust Ltd.
United Mizrahi Bank Ltd.
United Overseas Bank (Banque Unie pour les Pays d'Outre-Mer)
Unity Trust p.l.c.

Venture Finance Ltd.
Vernons Trust Corporation
Volkskas Ltd.

Wagon Finance Ltd.
Wallace, Smith Trust Co.Ltd.
Welbeck Finance p.l.c.
Western Trust & Savings Ltd.
Whiteaway Laidlaw & Co.Ltd.
Wimbledon & South West Finance Co.Ltd.
N.H.Woolley & Co.Ltd.

H.F.Young & Co.Ltd.

Changes to the list

The following changes were made during the year to the list of authorised institutions:

Additions

1 Recognised banks

B.A.I.I. p.l.c.
Bank Mees & Hope N.V.
Banque Internationale à Luxembourg S.A.
Banque Nationale de Paris S.A.
Caisse Nationale de Crédit Agricole
Christiania Bank og Kreditkasse
Copenhagen Handelsbank A/S
The English Trust Company Ltd.
Enskilda Securities-Skandinaviska Enskilda Ltd.
Kansallis-Osake-Pankki
King & Shaxson Ltd.(1)
Mase Westpac Ltd.
The National Bank of Kuwait S.A.K.
Republic National Bank of New York
Svenska International Ltd.
TSB Northern Ireland p.l.c.
TSB Scotland p.l.c.
Union Discount Company Ltd.

2 Licensed deposit-taking institutions

Alliance Trust (Finance) Ltd.
Bank Negara Indonesia 1946
Banque Worms
Bradford Investments p.l.c.
The Charities Aid Foundation Money Management Company Ltd.
Daiwa Europe Finance Ltd.
Edington p.l.c.
Granville Trust Ltd.
Jyske Bank
Minories Finance Ltd.
Mutual Trust and Savings Ltd.
The National Commercial Bank
Nomura International Finance Ltd.
St.Michael Financial Services Ltd.
Saudi American Bank
Shire Trust Ltd.
T.C.Ziraat Bankasi
United Overseas Bank
(Banque Unie pour les Pays d'Outre-Mer)
Bridgeover Ltd.
Bridgeway Finance Ltd.
Buchanan Securities Ltd.
Caisse Nationale de Crédit Agricole
Calculus Finance p.l.c.
Cattles Holdings Finance Ltd.
CE Coates & Co.Ltd.
Commonwealth Savings Bank of Australia
Co-operative Bank (Commercial) Ltd.
Copenhagen Handelsbank A/S
The English Trust Company Ltd.
Enskilda Securities-Skandinaviska Enskilda Ltd.
Farmers (WCF) Finance Ltd.
Granville Finance Ltd.
Grindlays Industrial Finance Ltd.
H.&J.Finance Co. (Midlands) Ltd.
Investment Trustees Ltd.
Kansallis-Osake-Pankki
Lodhi Finance Ltd.
The National Bank of Kuwait S.A.K.
Oriental Credit Ltd.
Punjab & Sind Bank
Republic National Bank of New York
Spring Gardens Securities p.l.c.
Svenska International Ltd.

Deletions

1 Recognised banks

American National Bank and Trust Company of Chicago
The Bank of Tokyo Trust Company
Chase Bank (Ireland) Ltd.
Christiania Bank (UK) Ltd.
King & Shaxson Ltd.(1)
King & Shaxson p.l.c.(1)
Lloyds Bank International Ltd.
Mercantile Bank Ltd.
Minories Finance Ltd.
The Union Discount Company of London p.l.c.
Wells Fargo Bank N.A.

2 Licensed deposit-taking institutions

Abbey Finance Co.Ltd.
The Alliance Trust p.l.c.
Allied Bank International
B.A.I.I. p.l.c.
Bank Mees & Hope N.V.
Banque Internationale à Luxembourg S.A.
Bradford Investments

Name changes

1 Recognised banks

Barclays Merchant Bank Ltd.	*to*	Barclays de Zoete Wedd Ltd.
Central Trustee Savings Bank Ltd.	*to*	TSB England & Wales p.l.c.
Charterhouse Japhet p.l.c.	*to*	Charterhouse Bank Ltd.
Chase Manhattan Ltd.	*to*	Chase Investment Bank Ltd.
Commercial Bank of Wales p.l.c.	*to*	Bank of Wales p.l.c.
County Bank Ltd.	*to*	NatWest Investment Bank Ltd.
Crocker National Bank	*to*	Wells Fargo Bank N.A.
Euro-Latinamerican Bank Ltd.	*to*	Euro-Latinamerican Bank p.l.c.
European Brazilian Bank Ltd.	*to*	European Brazilian Bank p.l.c.
Gerrard & National p.l.c.	*to*	Gerrard & National Ltd.
HongkongBank Ltd.	*to*	James Capel Bankers Ltd.
Johnson Matthey Bankers Ltd.	*to*	Minories Finance Ltd.
PK Christiania Bank (UK) Ltd.	*to*	Christiania Bank (UK) Ltd
Rea Brothers p.l.c.	*to*	Rea Brothers Ltd.
The Royal Trust Company of Canada	*to*	Royal Trust Bank
Scandinavian Bank Ltd.	*to*	Scandinavian Bank p.l.c.
Scandinavian Bank p.l.c.	*to*	Scandinavian Bank Group p.l.c.
Smith St.Aubyn & Co.Ltd.	*to*	King & Shaxson Ltd.(1)
Svenska International Ltd.	*to*	Svenska Handelsbanken p.l.c.

2 Licensed deposit-taking institutions

A1 Credit Ltd.	*to*	A1 Credit p.l.c.
Commercial Credit Services Ltd.	*to*	Commercial Financial Services Ltd.
Daiwa Europe Finance Ltd.	*to*	Daiwa Europe Finance p.l.c.
Equatorial Trust Corporation Ltd.	*to*	Equatorial Trust Corporation p.l.c.
Grindlays Humberclyde Ltd.	*to*	ANZ Finance Ltd.
Knowsley & Co.Ltd.	*to*	Authority & Co.Ltd.
London & Pacific Trust Ltd.	*to*	PaineWebber International Trust Ltd.
Edward Manson & Co.Ltd.	*to*	Benchmark Trust Ltd.
Mercury Provident Society Ltd.	*to*	Mercury Provident p.l.c.
Midland Bank Equity Holdings Ltd.	*to*	Midland Montagu Ventures Ltd.
Nomura International Finance Ltd.	*to*	Nomura International Finance p.l.c.
Omnibank A.G.	*to*	Swiss Cantobank (International)
St.Margaret's Trust Ltd.	*to*	RoyScot Trust Ltd.
Universal Credit Ltd.	*to*	Hill Samuel Personal Finance Ltd.

(1) Following the acquisition of Smith St. Aubyn (Holdings) p.l.c. by King & Shaxson Holdings p.l.c., the business of King & Shaxson Ltd. has been merged into that of Smith St. Aubyn & Co. Ltd. The latter company is carrying on the enlarged business under the name of King & Shaxson Ltd.

Annual Report by the Board of Banking Supervision

Board of Banking Supervision
Membership as at 28 February 1987

Chairman:	The Rt Hon Robert Leigh-Pemberton	*ex officio*
	George Blunden	*ex officio*
	R D Galpin	*ex officio*
	J A Caldecott	
	Sir Peter A Graham OBE	
	A J Hardcastle	
	N J Robson	
	Deryk Vander Weyer CBE	

Establishment of the Board

The Board was established in May 1986 on an informal basis. This implemented the agreement between the Governor and the Chancellor of the Exchequer, announced in the White Paper *Banking Supervision* in December 1985, that the Board should be established as soon as possible to operate on a non-statutory basis until legislation took effect. The arrangements were modelled closely on the statutory provisions expected to be included in the Banking Bill to be introduced later in the year; the provisions in the Bill currently before Parliament are consistent with these expectations.

Role of the Board

The Board has provided a forum within which the Governor and other ex-officio members gain expert, practitioner-based, advice on all matters relating to the Bank's responsibilities for supervising deposit-takers. Its remit has therefore been extremely wide, and similar to that provided for the new statutory Board in the banking legislation. Specifically, it has covered advice on:

(i) the general principles and policy of supervision of institutions authorised under the Banking Act;

(ii) the development and evolution of supervisory practice;

(iii) the administration of banking supervisory legislation, including advice on particular cases;

(iv) the structure, staffing and training of the Banking Supervision Division.

As with the proposed statutory Board, the functions are advisory. Executive responsibility remains with the Bank.

The Board meets monthly. It considers monthly reports submitted by the Banking Supervision Division, designed to keep the Board abreast of all significant developments in the division's work. More detailed papers on particular subjects of importance are also offered for discussion including, notably, drafts of all consultative papers intended for publication. In addition, the independent members raise other matters which they feel warrant discussion by the Board. The Assistant Directors responsible for the work of the division attend the Board's meetings, together with other members of the staff as appropriate.

Work of the Board

The Governor announced on 15 May that he had appointed, with the agreement of the Chancellor, Mr Andrew Caldecott, Mr (later Sir) Peter Graham, Mr Alan Hardcastle, Mr Nigel Robson and Mr Deryk Vander Weyer as independent members of the Board. They, together with the Governor, Deputy Governor and Mr Galpin as ex-officio members, served throughout the period under review. Sir Peter Graham felt it right not to attend meetings of the Board after the appointment on 6 February 1987, at the request of Standard Chartered Bank, of investigators under section 17 of the Banking Act. He had earlier informed the Governor of his intention to resign with effect from April 1987, before assuming executive chairmanship of Standard Chartered Bank.

Since the end of the period under review, Sir Donald Barron and Mr Harry Taylor have been appointed to the Board, bringing the number of independent members to six, in line with the membership proposed in the Banking Bill.

The Board met nine times during the period to the end of February 1987.

In anticipation of the provisions in the Banking Bill requiring notice to be given to the Chancellor of the Exchequer of any case in which it is decided that the advice of the independent members should not be followed, the Board agreed that, in the interim, any such disagreement between the independent members and the ex-officio members should be reported to the Chancellor by the ex-officio members. No such disagreements occurred.

The period was marked by the issue of a number of important consultative papers on aspects of banking supervision, including: the regulation of banks and securities business; large exposures; sterling primary liquidity; accounting records and internal control; and the role of audit committees in banks. Drafts of all these papers were considered by the Board before publication.

The most complex questions arose in relation to the first two papers mentioned in the preceding paragraph. The Board returned several times during the year to matters concerning the supervision of financial conglomerates following implementation of the Financial Services Act. It was particularly interested in the discussions in which the Bank was engaged with other regulatory bodies, aimed at establishing satisfactory arrangements for banks which would also be subject to authorisation by the Securities and Investments Board or by one or more of the Self-Regulating Organisations. Members recognised the importance of giving a high priority to this work both to ensure that potential problems of supervisory 'overlap' were minimised and that adequate arrangements for liaison between supervisors were put in place.

Similarly, the Board considered on several occasions the development of the Bank's large exposures policy. This raised difficult issues, reflecting the technical complexity of the subject and the need for precision in defining how exposures are to be calculated and assessed (since breach of the reporting provisions in the new legislation is to be a criminal offence). The treatment of lead underwriting exposures, for example, required particular consideration. Such exposures tend to be large in relation to the capital of the underwriting bank, but of very short duration. The large exposures policy, on the other hand, applies a prudential control to concentrations in banks' business and can take very limited account of the relative lack of credit or position risk attaching to particular exposures. The Board has been closely involved in reviewing the question of the balance which must be struck in such cases between proper supervisory prudence and competitive considerations.

The Board was kept informed of progress made in the Bank's discussions with the US federal banking supervisory authorities about a common approach to primary capital and capital adequacy assessment. The Board welcomed this initiative which was felt to be potentially of great significance.

The Board followed closely the progress of the new Banking Bill; and independent members offered advice on a number of clauses, notably those relating to the Board itself, to the question of the size criterion for the use of banking names and to the provisions for controlling bank takeovers and mergers.

In addition, various issues were discussed by the Board at the suggestion of independent members. In particular, the Board reviewed the adequacy of the Bank's revised procedures for dealing with instances of late or inaccurate reporting of prudential data by banks. Similarly, the Board considered the Bank's approach to the control of foreign exchange risks in banks. In both areas, members were content with the arrangements being implemented by the Bank.

The Board was very conscious of the need for supervisors to remain alert to changes occurring in the market place. It was informed of a number of matters on which the Banking Supervision Division, in response to such developments, sought additional information in order to keep under review its supervisory practice. In this regard, the Board noted, in particular, the detailed inquiries undertaken by the division into the controls and standards applied by banks to their corporate finance activities.

Arrangements established with the division have involved the reporting to the Board of all individual cases in which the possibility of use of the Bank's powers under the Banking Act has arisen. During the year the Board was informed of over 60 such cases. These covered a wide range of circumstances—for example, where the emergence of a new shareholder-controller required the Bank to consider formally whether action under the Act was required. In most cases, the Bank had no present prudential concerns. As described in the Bank's Annual Report under the Banking Act, in only a small proportion of the cases reported to the Board did the Bank need to use its statutory powers.

Independent members of the Board took the opportunity during the period to familiarise themselves with the division and its working procedures; a number of briefing meetings were held with senior staff of the division and members visited the division to meet others of the staff. The Board has kept under review the division's staff budget and taken a close interest in developments in staffing and training.

Addresses and telephone numbers

London	Head Office	Threadneedle Street London EC2R 8AH	*01-601 4444* [1]
	Registrar's Department	New Change London EC4M 9AA	*01-601 4444*
	Clearing Centre	161 City Road London EC1V 1PA	*01-601 4444*
	Printing Works	Langston Road Loughton Essex IG10 3TN	*01-508 6221*
Branches	Birmingham	PO Box 3 55 Temple Row Birmingham B2 5EY	*021-643 8571*
	Bristol	PO Box 10 Wine Street Bristol BS99 7AH	*0272 277251*
	Leeds	King Street Leeds LS1 1HT	*0532 441711*
	Manchester	PO Box 301 Faulkner Street Manchester M60 2HP	*061-228 1771*
	Newcastle	PO Box 2BE Pilgrim Street Newcastle upon Tyne NE99 2BE	*0632 611411*
Agencies	Glasgow	25 St Vincent Place Glasgow G1 2EB	*041-221 7973*
	Liverpool	Lancaster House Mercury Court Tithebarn Street Liverpool L2 2QP	*051-227 2553*
	Southampton Area	PO Box 15 Canister House 27 Jewry Street Winchester Hampshire SO23 8LP	*0962-840161*

(1) Enquiries relating to this *Report* or to the *Quarterly Bulletin* may be made on 01-601 4030.