

Building Societies in the UK: A Politician's Perspective

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The first recorded Building Society was formed over 200 years ago in 1775 at Ketley, now a part of Birmingham, England. Almost all the early societies were fully mutual terminating societies; members contributed towards the cost of building houses for all of the members, and when they had been housed the society was wound up. Although the last terminating society was not dissolved until 1980, these early societies were a million miles from the sophisticated movement of today.

The first recognisable development came with the formation of the permanent building societies, which began to appear in the 1830s and 1840s. They had essentially the same characteristics as today's building societies - interest was paid on deposits and housing finance advanced to borrowers with interest charged on the loan - but they were still very different from the societies of today. For example, branch networks only began to be established in the 1930s, and it was not until the 1960s that the major expansion took place. This was followed in the 1970s by a major growth in the number of shareholders. Throughout the period since the war there has been a sustained growth in the numbers of borrowers.

By 1980 it had become clear that the building society movement had vastly outgrown the constraints under which it operated. This is perhaps not surprising when you realise that the main legislative framework for societies during most of this period was the Building Society Act of 1874. Subsequent legislation amending the 1874 Act was passed in 1894, 1939 and 1960 mainly as a response to some supposed failure of the system. All of these Acts were consolidated in 1962 but most of the framework of legislation still derived from the 1874 Act, whose main feature was to:- 'Limit Building Societies to building and owning land for the purposes of conducting their business'. Change was long overdue and it was the building societies themselves that responded. Following the setting up of a working group in 1981, two separate reports were produced, the first - 'The future constitution and powers of Building Societies' in 1983 and a

revised report, 'New legislation for Building Societies' in 1984.

Simultaneously, the movement launched a public relations offensive which included Clive Thornton (the then Chief General Manager of the Abbey National, and a law unto himself) describing the Building Societies on a television chat show as: "the highest form of socialism". Mrs Thatcher responded!

Seriously, the Government did respond to the reports - initially with a Green Paper in 1984 - 'Building Societies: a new framework' and eventually a Building Societies Bill, which received its Royal Assent on the July 25 1986. The rationale for the legislation, according to the Government, was a combination of 'diversification' and 'deregulation'. Yet whilst the Bill extended the range of activities in which societies could engage, it also remained essentially prescriptive. So much so that the provisions of the Act had to be substantially modified over time, relaxing the controls on societies in recognition of the changes taking place in both the housing and financial services markets. For example in the savings market, societies have faced considerable competition from banks and national savings products over the last 15 years. In response the societies have had to diversify their range of savings products such that, from a position in 1980 where almost 90 per cent of retail deposits were held in ordinary accounts, by 1989 less than 8 per cent were held in these accounts.

Despite the successive relaxation of the 1986 Act, the Government was finally forced, in 1994, to review its working. This included examining deregulatory measures and exploring, in the words of the Minister:

The scope for a further liberalisation of building societies legislation. In considering the issues, we shall pay particular attention to the interest and security of societies' members and investors.

The emphasis on members' rights was an extension of a theme first elaborated in the 1986 Act and highlighted by the Minister in the Second Reading Debate:

The Building Societies Bill therefore contains a series of measures designed to enhance the opportunities for member

participation and to make the mutual system work more efficiently.

After some considerable delay - during which the Building Societies Association and the All Party Group were knocking continuously on the Treasury's door - Angela Knight (who it must be said worked tenaciously behind the scenes to persuade the Government of the need for this Act) finally brought the Bill before Parliament on the March 10 1997. In that opening Debate the Minister was candid as to the reason why this measure was coming forward within days of the announcement of the General Election:

We seek to give Societies a level playing field because, currently, it is tilted against them. The Bill will introduce permissive legislation because none of us can second guess the future, especially in the financial sector, which is a fast moving market.

The rest is history.

The reason I have gone through the recent history in some detail is to illustrate the broad policy themes being pursued by the UK Government in relation to building society legislation:

- 1) The government has responded to changes in the mortgage and savings markets, some of which have been brought about by government deregulation affecting those markets.
- 2) The legislative changes have attempted to create or recreate a level playing field in the market.
- 3) Changes to liberalise the legislation and move from a prescriptive to a permissive regime have been accompanied by attempts to improve the accountability of societies to their members.
- 4) Even accepting that the 1986 and 1997 Acts allowed conversions and takeovers, the overwhelming rationale was to underpin and enhance competition in the marketplace.

Let me illustrate these themes by looking at the two most controversial aspects of the 1997 Act. The decision was made to take away the five year protection of a converted society when it chooses to acquire other authorised financial institutions. This decision was taken in the context of the market at that time, and with the perception that it disadvantaged some institutions over others. The Minister said:

It quite clearly would be unfair on other financial institutions if one type of institution which is protected is uniquely allowed to go on the acquisition trail.

The decision was also made not to include in the Act a 'two year rule' preventing members from receiving a payout until they had been members for two years. The Minister defended that decision in the following terms:

It would be seen as unfair and incomprehensible by a society's members . . .

and as such concluded that.

the government of the day, would be under unstoppable pressure to re-instate the current law.

A predictable response? Certainly understandable in the context of the election atmosphere at that time.

What of the prospects post-election? And of the intentions of a new government and one committed to the concept of 'stakeholding' and thought by many to be more sympathetic to the ideals of the mutual movement. Before turning to that let me say a little about the All Party Group, and my role in it as Chairman.

The All Party Building Society Group

The rules of Parliament insist that membership of an All Party Group must be open to all members of the House, and that its aims and constitution must be parliamentary in character. It must be composed of a minimum of ten members of the government party together with ten members from the parties in opposition.

Its numbers may include members from the House of Lords. The Group must meet at least annually and the elections must be announced in advance and publicised by approved means. The All Party Building Society Group was set up in 1996 in the context of the failure of the Government to bring forward legislation following two years of consultation and numerous draft bills. It played a prominent though perhaps not starring role in getting the Bill on the Statute Book and its chairman, Douglas French, piloted a separate measure through Parliament at the same time. The Group works closely with the Building Societies Association.

Following the general election, the Group reformed on the basis of what it believed to be urgent unfinished business. Within three months, and without any real effort on our part the All Party Group already has 60 members, which is double that in the previous Parliament. All Party Groups are often accused of being talking shops and many are. The best contain active and committed members who are experts in their field and recognised as such in the House. And it is that recognition that gives a group whatever influence it can exert on the government.

My own personal involvement with the All Party Group is as a result of co-operation between different sectors of the social economy. Prior to the General Election, I worked as the Parliamentary Officer of the Co-operative Party supporting a group of 19 members in the Lords and Commons. That group met with representatives of the building societies and gave its support in ensuring the passage of the 1997 Act. At the General Election I stood as a representative of both the Labour Party and the Co-operative Party. The British Co-operative Party is a political party of members of consumer co-operative societies and is organised as a department of the Co-operative Union. The Party issued a manifesto at the General Election, outlining a programme based on its co-operative and consumer philosophy. Included is a commitment of:

Support for building societies and greater accountability for their members so that their long term interests can be secured against the pressures to convert to a bank.

The Co-operative Party believes in the need to promote the social economy, which would include amongst others mutual building

societies, friendly societies and, of course, co-operatives. But it is not only in defence of our ideals that we need to act together. With the Government currently reviewing much of the provision of the welfare state, and indicating that it will be looking to alternative providers, there is vast scope for organisations in the mutual and 'self-help' movement to fill that gap as an ethical alternative to the private sector.

Of course support in Parliament for the retention of a viable mutual movement is not restricted only to members of the All Party Group or the Co-operative Group. A recent poll carried out by Harris showed that 87 per cent of MPs believe that it is important for the UK to maintain a viable mutual sector and three out of four said that societies wanting to remain mutual should be shielded by legislation. Not only is this a strong endorsement of mutuality but also provides another lever to influence the Government to reflect that support in its actions.

The Future of Building Societies

I now want to comment briefly on the conclusions of the study commissioned by the Building Societies Association on 'The Economics of Mutuality and the Future of Building Societies'.

First, the report talks about two schools of thought regarding mutuality - the philosophical and commercial. Each lie at the polar end of a spectrum of views. It will be on its ability to compete that the future of the mutual society will depend. I say that as someone whose sympathies lie much closer to the philosophical end of that spectrum, but also as an advocate of consumer choice. Retail co-operatives have to compete in an intensely competitive market which, on current form, they do rather less successfully than building societies. But as consumer advocates we would not argue for a lessening of those competitive pressures - only for a level playing field. That is the essence of the Co-operatives Act which the UK Co-operative Council is preparing.

Second, there is a prospect of a systemic failure, as members vote for a windfall in their narrow self interest, and ignore the wider consequences that may lead to the disappearance of the mutual sector in the marketplace. If the Government is to be consistent, then it must view this as a public policy issue to which they should have a response. The All Party Group is

attempting to address the concerns of Government to ensure that decisions are taken in the light of continuing changes in the market and the need to sustain competition for the benefit of consumers. In this regard societies have already taken action to benefit consumers. This was done partly to respond to the obvious attraction to members of the "windfall" profit, but also at the urging of Government who were anxious that societies should show the benefits to consumers of remaining as a mutual.

Whilst reaffirming its commitment to the principles of mutuality, the Government has resisted all pressures to take action. I believe there are a number of reasons for this: The General Election on May 1 brought more than a change of Government. Many think that it has brought a sea change in the political climate and exposed the bankruptcy of the Thatcher years. Some interpret the Nationwide Building Society vote in this context. (Members of the society voted against demutualisation.) There are those who believe that public sentiment alone will safeguard the future of the mutual movement. The Government also points to the permissive regime introduced by the 1997 Act and the additional protection against takeover. It is only reasonable, they claim, to give the new legislation an opportunity to bed down and allow the inherent strengths of mutuality to come to the fore.

Of course, the one thing the 1997 Act did not do was to address the confusion that currently exists over the two year rule (the principle that members should not be eligible for a payout until they have been members for two years). This was an opportunity missed. The new Government complains that to revisit this or to introduce a moratorium on conversions would require primary legislation and precious Parliamentary time. The Government already has a crowded 18 months Parliamentary agenda with a number of prominent manifesto pledges having to be delayed because of a shortage of time. Whether or not we sympathise with the Government's predicament or simply view it as a convenient excuse, I think that it will take a considerable change of circumstances to shift them from this view. In an effort to respond to this concern, the All Party Group in partnership with the Building Societies Association has brought forward a number of legislative changes that can be dealt with through a delegated procedure that does not take up the time of Parliament. These

have been criticised by Government spokesmen as being contrary to the spirit of the '86 and '97 Acts.

Responding to a debate in the House of Lords, Lord McIntosh of Haringey, on behalf of the Government said:

we would like proposals from the building societies which will protect mutuality without reducing the rights of members.

Helen Liddell reflected this view in her meeting with the All Party Group when she expressed concern that the Government did not want to be accused of running a 'Nanny State'. Additionally the Government appears to believe that societies can convert without having to pay the price. In a recent adjournment debate on building societies the Postmaster General, Geoffrey Robinson MP, starting from the commitment given by the Halifax and Woolwich that they would not depart from the principles and practice of business that has served them so well in the past, concluded, and I quote:

the purpose of the Debate is to stress how important it is for the inherent advantages and principles of mutual societies to be continued even after conversion.

We have a lot of work to do.

But we already have the arguments and the evidence to counter all of these propositions. The All Party Group will in the near future be bringing them to the attention of Helen Liddell. One of the many ironies of this situation is that the advantages and principles of mutuals and the rights of members are under far greater threat from the carpetbagger than from any of the suggested options put forward by the Movement. Looking on the brighter side, it may also turn out to be ironical that the very success of the de-mutualisation process will lead to its demise. Recent estimates suggest that of the total windfall this year of around £36 billion, some £6 to £8 billion will be added to consumer expenditure. Uncertainty over the short run effects on domestic demand and ultimately on the level of interest rates is the result. With interest rates already high the Government may not wish to take the risk of further substantial injections of windfall profits in the near future.

Whatever happens, the All Party Group will be engaging with the Government in an effort to persuade them of the strength of the case. There is a great deal at stake. This is about the future of the building society movement, a movement that by any measure has had a significant impact on British life - both in terms of the unique extent of owner occupation in the UK for which the movement can lay some claim and for the high standard of prudential supervision exercised over members' deposits. It is a record not matched by either the banks or for that matter any other financial institution. And it is that legacy in a modern context that we seek to maintain.

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