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Secretary of State for Trade and Industry

16 February 1987

Ian Stewart Esq MP
Economic Secretary to the Treasury
Treasury Chambers
Parliament Street
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Price Printer²

Mr Chairman is in the end
prepared to give to the Treasury
proposal.

DLW
16/2

Dear Ian.

BANKING BILL - FOREIGN TAKEOVERS

Since I wrote to you on 13 February I have had the opportunity of considering the text of the amendment which you propose tabling. I have also seen the letter of 12 February from David Norgrove to your Private Secretary. *will request if required*

I remain very troubled about this whole matter. A readiness to make any move towards those who are pressing us to introduce new powers to control foreign take-overs of banks risks leading us into very difficult territory.

I acknowledge that the present text of your draft amendment is designed to do little more than enhance the reciprocity powers which we took in the Financial Services Act.

Those powers were designed - and we said so publicly on many occasions - to give us a lever to help us persuade overseas Governments to grant authorisations to UK banking, insurance and other financial services firms. They were most certainly not designed as a pretext for blocking foreign take-overs which a British target might find unattractive. They have no effect on any EC member state because the Treaty obligations prevent Member States from denying such access to each other. They were not

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designed to secure reciprocity of take-over facilities and, of course, one of the main take-over "threats" to UK banks comes from the USA where I believe there are no barriers to take-overs by British banks.

As I understand the thinking behind the amendment, the intention is not to transform the Financial Services Act reciprocity provisions. It is to extend the mechanism through which the leverage can be brought to bear - but only in respect of banks (presumably any class of bank, since another effect of the Bill is to treat all deposit-takers alike with the result that this clause would "bite" on some 300 institutions, varying from a large clearer like Lloyds to a credit institution like St Michael Financial Services Ltd). If the amendment is passed Government would have the right not only to threaten to have a banking authorisation withdrawn but also, as an alternative, to object to a new owner (on other than prudential grounds).

As it stands this is an ingenious piece of damage limitation but I see some major drawbacks.

First, we have no credible arguments for limiting it to deposit taking institutions and denying it to other financial services firms such as insurance companies. There is no lack of protectionist sentiment in the insurance industry and long term investors in life funds are arguably as much, if not more, likely to feel anxious about a foreign take-over as deposit holders in a bank.

Secondly, it will not be easy to use against the USA because there is reciprocity on take-overs. I have no particular wish to see us blocking US take-overs of UK banks but those who are pressing for an amendment will be among those pressing us to use the power. In order to make the power "bite" on a US take-over we would have to identify some other area where reciprocity is not available (eg the Glass/Steagall Act prohibition on securities dealing by banks) but where we would otherwise not be seeking to exercise leverage on the Americans.

Thirdly, as regards countries such as Japan, Canada and Australia where UK firms cannot take companies over and where a change of attitude is unlikely, it will be obvious that our policy intention is to block the UK market rather than to open the foreign market.

Fourthly, if we seek to minimise some of these risks by assurances of our intentions, we shall fail to win the support of those whose pressures are leading us to contemplate this device in the first place.

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I have to say that my preferred course would be to head off back bench pressure with a firm statement that the question of foreign take-overs is being addressed in our review of competition and mergers policy and that for the present our policy in applying the Fair Trading Act powers takes full account of the public interest. The statement could go on to say that there is no reason whatever to think that the review will result in any weakening of the broad public interest criterion in the Fair Trading Act. However, if you judge that you cannot hold the line with that, then I would reluctantly go along with your proposed amendment. Because of my concerns and responsibilities I would want to be consulted about the terms in which it is presented both to Parliament and the Press and I would want your assurance that you would not concede more ground on this matter.

I am sending copies of this letter to the Prime Minister, Geoffrey Howe, Nigel Lawson, Malcolm Rifkind and the Governor of the Bank of England.

Paul
Channon

PAUL CHANNON

ECON POL: Domestic Monetary Policy PE 16

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