Bank of England Banking Act report for 1993/94

Banking Act 1987

Annual report under the Banking Act for 1993/94

This report on the exercise of the Bank's functions under the Banking Act 1987 during the year to 28 February 1994 is presented to the Chancellor of the Exchequer, and by him to Parliament, pursuant to section 1(3) of the Act.

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Overview

The more stable economic and financial conditions prevailing in 1993 made it a year of recovery for the large British banks. The much-improved economic environment in both the United Kingdom and the United States led to falls in the overall bad debt charge for the sector. Combined with the third year of improvement at the operating profit level, this led to a marked recovery in overall profitability. The level of bad debts nevertheless remained high by historical standards, and the sector's performance in traditional banking was still weak. The growth in operating profits was driven in particular by trading activities, which flourished in favourable market conditions.

A return to positive retained earnings and the continued low growth in weighted risk assets helped the sector's capital adequacy reach its strongest position under the current system of measurement, which dates from the introduction of the Basle capital convergence regime in 1989. The banks therefore remain comfortably placed to accommodate any increased demand for lending that may accompany the economic upturn. The challenge for the banks in the coming years is to find alternative sources of profit growth to replace the strong market trading profits of 1993, given that market conditions as favourable as 1993's are unlikely to be repeated. At the pre-tax level, further falls in the bad debt charge should help in the short run, and the banks are taking steps in loan pricing and credit monitoring which aim to reduce the scale of renewed bad debt problems in the longer run. At the operating level, cost containment remains an important line of attack, but one where further improvements become ever harder to achieve. The banks will also have to examine further the case for diversifying out of traditional banking into the provision of other financial services.

The financial pressures on the smaller UK banks have eased thanks to the greater stability in the wholesale funding markets, the lower level of short-term interest rates and the fact that property prices have now stopped falling. Indeed, a number of institutions, principally those owned by financially-sound parents with a rating from one of the credit agencies, have found the wholesale markets willing to provide them with increased funding to finance expansion. Last year's Banking Act Report outlined the supervisory action taken by the Bank during 1991 and 1992 to ensure that the financial pressures on the smaller banks did not develop into a wider systemic disturbance. The Bank continued during 1993 to monitor closely the ability of these smaller institutions to raise and retain funding, and their ability to maintain adequate capital to withstand further provisions against doubtful loans and the diminution of security values.

Despite this easing of pressure on the small banks, their number has continued to decrease, falling by a further 11 (net) during 1993/94. However, whereas in previous years this was more closely linked to the difficulties outlined above, and in 1992 was owing to the onset of the minimum capital provisions of the Second Banking Co-ordination Directive (2BCD), the causes for the continued decrease over the last year have been more varied. While some institutions have ceased trading because of an inability to raise adequate funding or to withstand the requirement of further provisions, others have decided to surrender their authorisation for reasons such as: a wish to finance their activities from sources other than deposits; the costs of meeting supervisory requirements outweighing the benefits from authorisation; and an inability to reorganise the structure of a banking group which was impeding effective consolidated supervision by the Bank. Some of the banks that have ceased trading catered primarily for the needs of a particular minority, and the Bank has endeavoured to assist the communities served by such institutions to look to other banks to obtain their banking services.

Most foreign banks in London had a successful year, with increased profits on the back of strong dealing income. More traditional lending business was subdued, but bad debt charges generally fell. London remains a key centre for many major foreign banking groups, and continues to attract new entrants (see part III B).

The Bank held a series of bilateral discussions between June and November 1993 involving the major banks, the Confederation of British Industry and small business representative organisations on the subject of the financing of small firms. The Bank issued a paper[(1)] in January this year summarising the points that emerged. On the one hand, banks made it clear that they are committed to the finance of the small firm sector, and to enhancing the training of their staff responsible for originating and monitoring loans to small businesses. The small business representatives for their part recognised the need for banks to price risk realistically, and the

(1) 'Finance for small firms', note by the Bank of England, January 1994.

fact that the risks and administrative costs of providing financial services to small firms are high relative to those for larger companies. Various ways were identified for banks and their small business customers to contain those risks and costs: the current low inflation environment provides a promising background (see box on page 17) for suggestions such as a greater role for term loans in small firm finance.

Media interest focused also on banks' relations with their personal customers and, in February 1994, the banks issued a revised edition of the voluntary Code of Banking Practice which first came into force in March 1992. It sets out minimum standards of good banking practice for dealings with personal customers and the revisions include a commitment to provide advance notification of changes to charges and interest rates. The revised Code received a mixed reception from customer representative bodies.

The Bank of England continues to hear from both personal and corporate customers of banks who feel unhappy with the way they have been treated by their bank. The Bank, however, has neither the powers under the Banking Act 1987, nor the responsibility, to act as arbitrator or mediator in any individual dispute.(1) In many cases the complainant's best course of action is to follow the bank's own internal complaints procedure or, if this route has already been fully exhausted, to contact the Banking Ombudsman. Failing this, the complainant would need to take legal advice on whether it would be worthwhile pursuing the matter through the courts: the Bank cannot step in at any point and act as a quasi-court. The Bank's concern would solely arise where a dispute raised issues relating to the institution's compliance with the criteria in Schedule 3 to the Banking Act, or otherwise threatened the interests of depositors.(2) Typically, though, complaints, while important to the individual concerned, do not raise wider concerns about the control environment, skill or integrity of the institution taken as a whole. The Bank takes care to satisfy itself that these broader concerns do not arise, and where appropriate will submit its judgment in these cases to the members of the Board of Banking Supervision for their independent view.

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(1) However, under paragraph 22 of the London Code of Conduct the Bank is required to investigate complaints arising from transactions in the wholesale markets; and the Bank is prepared to arbitrate in disputes arising from transactions in the wholesale markets, on the basis set out in paragraph 91 of the Code.

(2) In the case of 'European authorised institutions' (see box on page 32), the Bank itself is no longer responsible for ensuring compliance with the Schedule 3 criteria other than the one relating to liquidity, but it would pass on any concerns it might have to the relevant home supervisor.

Table I
Large British banks: earnings

£ billions	1989	1990	1991	1992	1993
Operating profits before bad debts	7.72	7.29	8.28	9.30	10.41
Pre-tax profits	0.86	2.81	1.62	1.56	4.75
Post-tax profits	0.50	1.36	0.97	0.77	3.18
Pre-tax return on equity (%)	*3.80*	*11.70*	*7.18*	*6.83*	*19.29*
Post-tax return on equity (%)	*2.20*	*5.70*	*4.27*	*3.39*	*12.90*
Return on total assets (%)	*0.19*	*0.60*	*0.34*	*0.29*	*0.80*

Table II
Large British banks: sources of income

£ billions	1989	1990	1991	1992	1993
Net interest	13.92	13.97	14.45	14.82	15.06
Non interest	8.44	8.95	10.42	11.54	13.02
Total income	**22.36**	**22.92**	**24.87**	**26.36**	**28.08**
Non-interest income as percentage of total income	*37.7*	*39.0*	*41.9*	*43.8*	*46.4*

Table III
Four large banks: interest margins[(a)]

Percentages	1989	1990	1991	1992	1993
Domestic	4.7	4.3	4.0	3.8	3.6
International	1.8	1.9	2.1	2.3	2.0
Overall	**3.4**	**3.3**	**3.3**	**3.3**	**2.9**

(a) Net interest income/average interest-earning assets.

Bank earnings

The banking sector's operating profit exhibited strong growth over the year, due to the continued buoyancy of non-interest income (Tables I and II). The main source of non-interest income is fees and commissions from traditional banking business, but this element fell slightly over the year, reflecting both revisions of tariff structures by the banks and low levels of new business of this type. The growth in non-interest income in 1993 was driven rather by dealing profits: the large British banks benefited from increased customer volumes arising from periods of volatility in the foreign exchange markets and favourable conditions in the money markets.

The major domestic banks' net interest income remained depressed throughout the year, despite a reduction in the amount of suspended interest in respect of non-performing loans. The lack of growth in lending and the shift of some of the banks' balance sheets into lower risk and lower margin business—such as securities and mortgage lending—kept downward pressure on interest income and the lending margin. On the liabilities side of the balance sheet, lower interest rates in the United Kingdom throughout the year led to a further erosion of the 'endowment profit' earned from the banks' interest-free funds (which is in long-term decline as depositors switch out of non-interest-bearing deposits). In addition, increasing competition for funds in the retail deposit market led to a narrowing of the spread between the cost of retail funding and base rate. There was thus downward pressure on the margin from both sides of the balance sheet, leading to a further fall in the four large banks' overall margin on domestic business, from 3.8% to 3.6% (Table III).

The management of many small banks are facing new challenges as they seek to ensure the continuing profitability of their institutions. A number have endeavoured to lessen their reliance on wholesale funding by offering interest rates to retail depositors above those offered by the clearing banks and building societies. This has further increased the pressure on them to identify profitable business opportunities.

One approach has been to differentiate themselves from the large banks by offering products tailored to the needs of particular customer groups in order to obtain an adequate return: an example is the provision of credit cards, at competitive rates, to well defined 'affinity' groups. Those smaller banks which have been successful in identifying such opportunities are often those that have also taken a conscious decision to focus on a particular regional market about which they are knowledgeable.

Merchant banks had a good year in 1993, with profits generally well ahead of 1992. Although UK public takeover activity reached its lowest level in seven years, corporate finance earnings were supported by a level of new issue activity roughly double that of 1992. Securities trading and fund management were strongly ahead on the back of buoyant bond, equity and sovereign debt markets. Treasury departments generated high profits, thanks to continued favourable market conditions and increased client demand for various hedging products. Finally, problem loans had less of an impact than in recent years.

Although they are not immune to credit risk and the other risks inherent in banking, the merchant banks' particular role as advisers in major takeovers, new issues and corporate restructurings makes them especially vulnerable to litigation and loss of reputation in cases where clients or investors turn out to have been given bad advice. It is obviously essential for merchant banks to be alert to these risks and to ensure that safeguards against them are in place. This is a subject of supervisory discussion with the banks.

Lending

Bank lending remained very subdued during the year, especially to corporate customers (Chart 1 and Table IV). The company sector was in fact a net repayer of lending to banks over the year. This was partly a continuing adjustment to earlier high levels of indebtedness, but it also reflects a switch by companies to non-bank sources of finance: companies' net sterling capital issues in 1993 reached their highest level since 1987, and were 70% higher than the annual average for 1988–92. The strong growth in lending to the non-bank financial sector was almost entirely accounted for by lending to securities firms, which borrowed to take advantage of booming markets.

There were signs that individuals' borrowing for consumption started to recover towards the end of the year. The residential housing market also showed hesitant signs of recovery in 1993: generally, affordability is no longer a significant constraint, as the ratio of initial mortgage payments to average earnings is now the lowest for 15 years, but negative equity remains a problem. Within a broadly unchanged total for net new mortgage advances, the large banks managed significantly to increase their share at the expense of the building societies

Table IV
UK banks: lending to UK residents[a]

Annual growth rates for year to end-November (%)

	1989	1990	1991	1992	1993(b)
Lending to UK residents	23.8	12.4	5.3	3.6	3.2
of which:					
Lending to the company sector	*29.1*	*13.9*	*0.3*	*2.0*	*-7.2*
Lending to the personal sector	*15.1*	*9.2*	*6.2*	*4.9*	*7.8*
Lending to the non-bank financial sector	*22.7*	*13.1*	*14.0*	*5.0*	*17.3*

(a) Loans, advances, acceptances and sterling commercial paper in both sterling and other currencies, the latter adjusted to remove the estimated effects of exchange rate movements. No account is taken of changes in either reporting population or reporting dates.

(b) Year to end-December.

Chart 1
UK banks: lending to UK residents

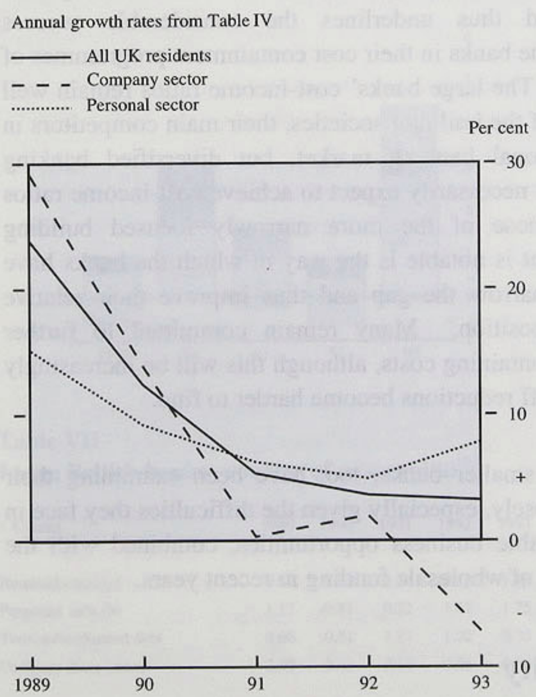


Chart 2
Bank lending by sector to UK residents

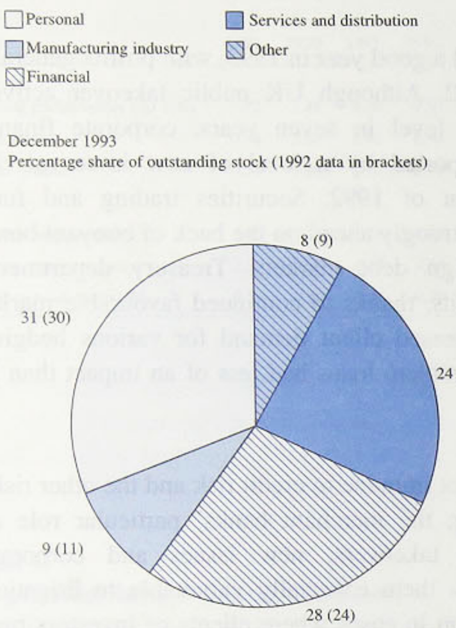
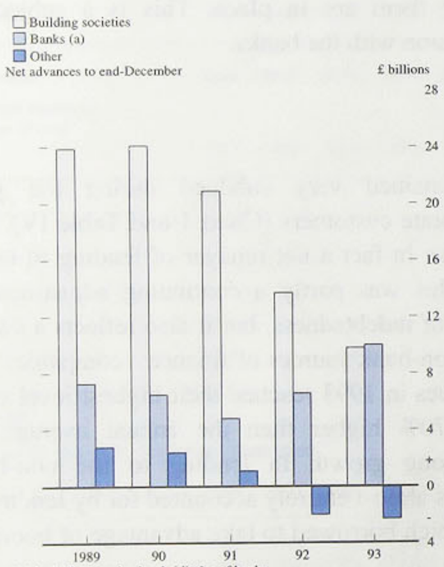


Chart 3
Loans for house purchase



(a) Including non-bank subsidiaries of banks.

Table V
Large British banks: costs

£ billions	1989	1990	1991	1992	1993
Staff	8.50	8.92	9.26	9.55	9.86
Premises and equipment	2.56	2.95	3.36	3.52	3.08
Other	3.93	3.71	3.98	3.99	4.20
Total operating costs	**14.99**	**15.58**	**16.60**	**17.06**	**17.14**
As percentage of total income	*67.0*	*68.0*	*66.7*	*64.7*	*61.0*

(Chart 3). Fixed-rate mortgages proved popular with borrowers wishing to lock in to current interest rates, and banks are in a stronger position than the building societies to provide such products, having better access to wholesale funds, and greater expertise than many of the smaller building societies in hedging the associated interest rate mismatch.

Costs

The containment of costs (Table V) continued to be one of the major objectives of banks' management. The largest component of total costs (comprising 58% of total) is that in respect of staff, and it is in this area that the large banks have concentrated most of their efforts to reduce costs. The year saw further reductions in both staff numbers and branch networks, although not on the scale of recent years. These measures were sufficient to contain the total growth in costs to just 1/2%: the underlying movement in recurrent costs was in fact downwards, but this was masked by exceptional restructuring costs and redundancy payments.

The figure of 61% for the sector's aggregate cost-income ratio compares with an average of some 68% over the period 1980–90, and thus underlines the considerable success achieved by the banks in their cost containment programmes of recent years. The large banks' cost-income ratios remain well above those of the building societies, their main competitors in the UK personal banking market, but diversified banking groups cannot necessarily expect to achieve cost-income ratios as low as those of the more narrowly focused building societies. What is notable is the way in which the banks have managed to narrow the gap and thus improve their relative competitive position. Many remain committed to further progress on containing costs, although this will be increasingly difficult as staff reductions become harder to find.

Many of the smaller banks, too, have been examining their costs more closely, especially given the difficulties they face in finding profitable business opportunities, combined with the increased cost of wholesale funding in recent years.

Asset quality

The total bad debt charge of the large banks fell considerably over the year, reflecting the improving economic conditions in both the United Kingdom and United States. A marked feature of the results in 1992 was the high charge resulting from a number of large corporate collapses. This was not repeated in 1993, but the level of small company failures, as well as

Table VI
Large British banks: domestic bad debt provisions and charges

£ billions	1989	1990	1991	1992	1993
Stock of domestic commercial provisions (a)	2.7	4.1	6.8	7.9	7.2
As percentage of total lending	*1.3*	*1.9*	*3.4*	*4.2*	*3.7*
Charges to domestic commercial provisions	1.1	3.5	5.7	6.5	4.6
As percentage of total lending	*0.5*	*1.6*	*2.9*	*3.5*	*2.4*

(a) All figures for stocks are year-end; charges are gross charges during the year.

Chart 4
Large British banks' retained earnings

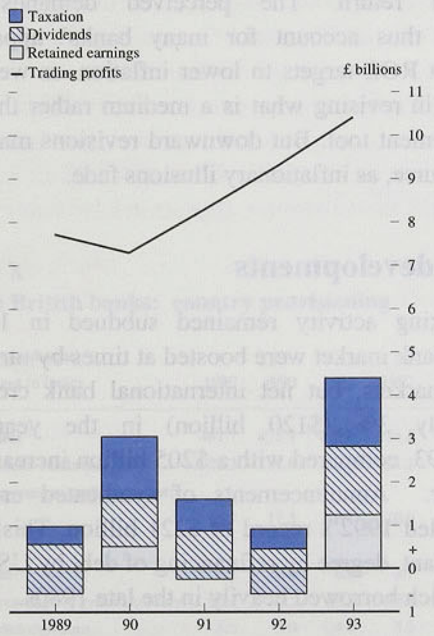


Table VII
Large British banks: sources of new capital[(a)]

£ billions	1989	1990	1991	1992	1993
Retained earnings	-0.57	0.52	-0.24	-0.58	1.24
Perpetual debt (b)	1.52	-0.81	0.22	1.47	1.75
Term subordinated debt	0.66	-0.51	1.17	1.02	0.35
Ordinary share issues	2.39	0.52	0.14	0.06	0.03
Total	**4.00**	**-0.28**	**1.29**	**1.97**	**3.37**

(a) Excludes certain items affecting reserves, such as surpluses on property revaluations.
(b) Includes preference shares.

problems in the personal sector, nevertheless kept provisions high by historical standards. Encouragingly, the present recovery from recession appears to be following a different pattern from previous recoveries, in that the end of recession has not been accompanied by an upsurge in bad debts.

The marked revival of investment activity at the prime end of the commercial property market during 1993 has eased the problem of loan security falling below the size of the loan. While the lower tiers of the property market have yet to see any appreciable revival, with prices no longer falling, there has been less need for banks to make further provisions to cover shortfalls of security. There are signs that the banks have had no choice but to accept longer-term holdings of property assets (acquired through enforcing security), in anticipation of further recovery of value.

Capital and risk management

For the first time in two years, the large banks added to capital from positive retained earnings, and were also able to increase dividends significantly. In addition, the banks continued with their large programme of capital issuance. Table VII shows the sources of new capital and demonstrates the important contribution of both retained earnings and new capital issues in 1993 to the overall growth (of 10%) in capital resources. At the same time the continued slow growth in weighted risk assets, caused by a combination of weak loan demand and some banks switching to lower risk-weighted assets, led to a further significant boost to the banks' combined risk asset ratio.

Although by historic standards capital may seem to be in ready supply, banks have pressed ahead with two related developments designed to make them more capital efficient. First, investment has continued in systems improvements designed to allocate costs and income more precisely and thus allow more accurate measurement of the profitability of different lines of business and individual transactions; and, secondly, further research has been taking place into risk measurement techniques to improve the allocation of capital to transactions according to the risk of loss, and hence to determine the appropriate capital charge to be included in the cost. Taken together, these will allow banks to obtain a truer picture of the risk-adjusted profitability, both of individual products and of their business as a whole. The Bank welcomes these developments and has been monitoring them carefully.

One component of risk-adjusted profitability is the rate which banks charge their different operating sectors for the capital

Table VIII
Large British banks: capital constituents

Convergence basis

£ billions	1989	1990	1991	1992	1993
Tier 1					
Ordinary shares	6.58	7.10	7.24	7.30	7.36
Preference shares	0.10	0.10	0.47	0.50	0.78
Reserves	13.48	13.25	13.08	12.81	14.17
Minorities	0.90	1.01	1.11	1.22	1.66
Deductions	—	—	—	-0.05	-0.05
Total Tier 1	**21.06**	**21.45**	**21.90**	**21.79**	**23.90**
Tier 2					
Property revaluation reserves	2.13	1.47	0.64	0.21	0.16
Hybrid capital	6.90	5.89	6.11	7.33	8.89
General provisions	1.17	1.48	1.68	2.00	2.15
Tier 2 minorities	0.08	—	—	0.01	0.01
Qualifying subordinated loan stocks	7.69	7.14	8.31	9.33	9.42
Headroom deduction	-1.06	-0.49	-0.57	-0.49	-0.19
Total net Tier 2	**16.92**	**15.50**	**16.18**	**18.39**	**20.44**
Other deductions	-2.99	-2.48	-2.64	-2.76	-3.07
Total net capital	**34.99**	**34.47**	**35.44**	**37.43**	**41.27**

Table IX
Large British banks: capital ratios

Convergence basis

£ billions	1989	1990	1991	1992	1993
Total assets	461.7	471.1	476.8	535.6	593.0
Weighted assets	377.1	374.2	365.0	378.9	381.2
Total net capital	35.0	34.5	35.4	37.4	41.3
Risk asset ratio (per cent)	**9.3**	**9.2**	**9.7**	**9.9**	**10.8**

which is allocated to them. This is ultimately determined by the target which banks set themselves for post-tax return on equity (ROE), which is driven by the return required by banks' shareholders. With lower inflation, the component of the nominal ROE that reflects risk-free return should also be lower, so there is a prima facie case for banks to revise downwards their target ROEs, which in some cases have been at the same level for several years. However, one argument against this is the possibility that banks' profits have become more variable over economic cycles: investors will thus demand a higher risk premium to hold bank shares, at least partly counteracting the lower risk-free element (see box on page 18). But it may also be true that investors are suffering from 'reverse money illusion' (see box on page 17), which prevents them from recognising the appropriate downward adjustment to their required nominal return. The perceived demands of shareholders may thus account for many banks' apparent reluctance to adapt ROE targets to lower inflation, as well as their own caution in revising what is a medium rather than a short-term management tool. But downward revisions may be expected in due course, as inflationary illusions fade.

International developments

International banking activity remained subdued in 1993. Flows in the interbank market were boosted at times by turmoil in the currency markets, but net international bank credit[1] increased by only 3% ($120 billion) in the year to end-September 1993, compared with a $205 billion increase in the previous year. Announcements of syndicated credits during 1993 equalled 1992's record of $221 billion. This was driven to a significant degree by refinancing of debt by US and UK companies which borrowed heavily in the late 1980s.

The major economies are at different stages of the economic cycle. Recovery has been under way in the United States for longer than in the United Kingdom, and this was reflected in the fact that US banks established another earnings record in 1993. As the economy gathered pace, loan demand began to rise and many US banks experienced an improvement in asset quality, which enabled them to reduce their loan loss provisions. Buoyant trading profits and efficiency gains also contributed.

The recession in the major continental European economies on the other hand appears only to have bottomed out during 1993, and only very gradual recovery is forecast for 1994. Market

(1) BIS estimate of cross-border lending to end-users by BIS reporting banks.

conditions in these economies therefore continued to deteriorate during the year, with asset quality suffering, particularly where property values declined. European banks are thus tending to concentrate on domestic problems and are giving a low priority to international expansion.

The prolonged recession in the Japanese economy continued to impact on the country's banking sector, with a further deterioration in asset quality during 1993. Retrenchment from international markets seems to have come to an end, although the increased interest in international activity may to a certain degree be a reaction to the marked slowdown in domestic lending. The aggregate balance sheet of the Japanese banks in London contracted more slowly in 1993, and now appears to have broadly stabilised: they are seeking to achieve a greater return on assets rather than growth through high-volume, low-margin business. The opening of new branches by Japanese banks seems to have been largely aimed towards other East Asian economies, which continue to enjoy robust growth and are seen to offer greater opportunities to increase profitability.

Table X
Large British banks: country provisioning

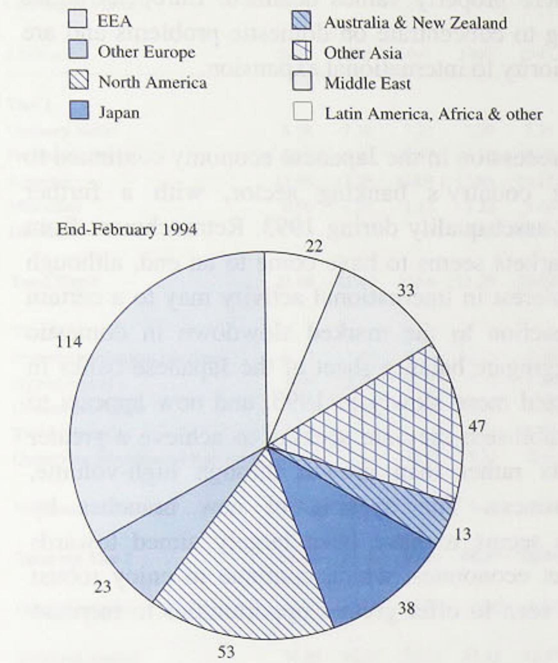
£ billions (end-year) Percentages in italics	1989	1990	1991	1992	1993
Total assets	461.7	471.1	476.8	535.6	593.0
Shareholders' funds (a)	22.3	21.9	20.3	21.1	24.7
Gross exposure to problem country debtors	15.2	11.5	10.1	10.9	8.3
Provisions	9.2	6.5	6.0	5.7	4.2
as a percentage of gross exposure	*60.3*	*56.5*	*59.6*	*52.8*	*51.2*
Unprovided exposure	6.0	5.0	4.0	5.1	4.0
as a percentage of total assets	*1.3*	*1.1*	*0.8*	*1.0*	*0.7*
as a percentage of shareholders' funds	*27.1*	*22.8*	*19.9*	*24.4*	*16.4*

(a) As published in the banks' annual accounts: differs from the definition of shareholders' funds for regulatory purposes (shown in Table VIII).

The experience of the UK banks abroad has continued to be mixed. The improving economic conditions in the United States led to a fall in bad debts for the sector as a whole, but in some individual cases restructuring costs outweighed this advantage. In contrast, the worsening economic environment in Europe during 1993 led to increasing bad debts and the decision by some banks to withdraw from certain markets, which in turn added to the losses in those markets.

Most foreign banks in the United Kingdom experienced increased profits in 1993. For many of the banks, treasury activities were a key component in strong profit growth. Such business benefited from the mostly one-way movement of interest rates in major European money markets over the year, and the performance of several foreign banks in London was boosted by their leading positions in rapidly-growing derivatives markets. The periods of turbulence in the ERM contributed to profits in foreign exchange markets, although to a lesser extent than in 1992. Those banks that rely more on traditional lending business continued to be affected by the economic climate, with balance sheets static and limited prospects for new business. But the worst of their bad debt problems now appears to be past: some banks benefited from refocusing on areas where they have a comparative advantage, for instance business connected with their home region.

Chart 5
Geographical representation of overseas institutions



Branch and subsidiary operations, together with controlling stakes in consortium banks.

London continues to be a vital component in many banks' global networks. For many non-European banks it remains the focus of their European operations, and major European banks increasingly use the London markets to co-ordinate European (and often global) foreign exchange, capital market and derivatives activities. Given the prevailing economic climate, few new banks from the major economies established in London during 1993, but increasing interest in a UK presence has become apparent from banks in other parts of the world where liberalisation and economic growth is encouraging international expansion, notably East Asia.

The impact of the Second Banking Co-ordination Directive (2BCD) continued to be felt: further subsidiaries of banks from other countries in the European Economic Area (EEA) surrendered their Banking Act authorisation to concentrate their UK operations through branches. Conversely, a number of US banks are taking advantage of the 2BCD to convert operations in other EEA countries into branches of their UK subsidiaries. US banks have continued to restructure their UK operations, but overall the decline in US authorisations in the United Kingdom seen in recent years appears to have halted.

Glossary of terms for Part 1

Sources of data	Audited financial statements for the large British banks; tables on capital ratios, lending to UK residents and mortgage lending are from Bank of England statistical returns. The tables relating to loan portfolios adopt the sectoral classifications used in the *Bank of England Quarterly Bulletin* and in the Central Statistical Office's *Financial Statistics*. Because of rounding, the columns in the tables may not balance.
Large British banks	Barclays, Lloyds, Midland and National Westminster together with Bank of Scotland, The Royal Bank of Scotland, Standard Chartered and the TSB. All data for these banks are consolidated. Calendar year-end information except for Bank of Scotland (1993 data are based on interim figures), The Royal Bank of Scotland (end-September) and the TSB (end-October). Figures for Abbey National are excluded from the Tables and Charts, as it switched from building society to bank status during the period covered by the historical data.
Four large banks	Barclays, Lloyds, Midland and National Westminster.
Consortium banks	Institutions majority-owned by two or more banks but none individually holding over 50% of the equity.
Trading profits	Profit before taxation and bad debt provisions (including the exceptional problem country charges in 1989).
Pre-tax profits	Profit after bad debt provisions but before taxation.
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 are defined as paid-up share capital and reserves.
Return on total assets	Percentage of pre-tax profits to average total assets.
Retained earnings	Current year's post-tax profits after extraordinary items and distributions.
Term subordinated debt	Subordinated debt with a fixed maturity and satisfying the Bank of England's conditions for Tier 2 capital.
Hybrid (debt/equity) capital	Perpetual cumulative preferred shares, including such shares redeemable at the option of the issuer and with the prior consent of the Bank, and such shares convertible into ordinary shares; and perpetual subordinated debt meeting the qualifying criteria, which require that the debt can only be converted into equity, is available at all times to absorb losses, and provides for the deferment of interest payments in certain circumstances. (Perpetual **non**-cumulative preferred shares are included in Tier 1 capital.)

Weighted assets	Total assets adjusted in accordance with the risk weightings as set out in the supervisory notices: for 1989, *Implementation of the Basle Convergence Agreement in the United Kingdom* (BSD/1988/3); and for 1990 onwards, *Implementation in the United Kingdom of the Solvency Ratio Directive* (BSD/1990/3) (as amended).
Adjusted capital base	Total capital (Tier 1 and Tier 2) less goodwill, connected lending of a capital nature, investments in subsidiaries and associates, and holdings of bank paper in excess of market-making concession.
Risk asset ratio	Percentage ratio of adjusted capital base to weighted assets.
Tier 1 and Tier 2 capital	As defined in the Bank's notice to institutions *Implementation in the United Kingdom of the Directive on Own Funds of Credit Institutions* (BSD/1990/2) (as amended).
Headroom deduction	Tier 2 capital which cannot count towards capital because of insufficient Tier 1 or upper Tier 2 on an institution's books.
Net interest income	Gross interest income less interest paid on borrowings.
Other income	Includes investment income.
Interest margin	Net interest income/average interest-earning assets.
Endowment effect	Net interest income earned by employing interest-free deposits.

Banking with low inflation

Given current economic trends in the United Kingdom and in many of the world's major economies, banks' strategic planning now has to address the implications of a sustained period with low inflation, with interest rates and asset prices also less volatile. The markets in which banks operate have changed dramatically since the last period of persistent low inflation, with deregulation and the increasing financial sophistication of their customers helping to produce a much more competitive environment. The patterns of customer behaviour to which banks may now have to adapt are therefore hard to predict from past experience.

The benefits of stable prices in reducing the uncertainty in economic decision-making are well known, but a stable environment may nevertheless present new challenges to the banks. For instance, the evidence suggests that some bank depositors are now seeking higher returns than those the banks are able to offer, whether by investing directly in equities and bonds or indirectly through PEPs, unit trusts and the like.

What is not clear is whether some of these phenomena are merely features of a transitional phase, during which long experience of inflation still influences economic behaviour, or whether they will persist in the longer run. Such phenomena may be the result of an effect that one can label 'reverse money illusion'—the effect that, at a time of falling inflation, although real rates of return may be no different, individuals or firms pay regard only to the money return on their assets, and find this inadequate by comparison with recent memory of higher nominal rates.

Reverse money illusion may explain the current tendency for bank depositors to seek higher (but riskier) returns from non-deposit investments: in real terms the trade-off between higher risk and higher real return should not be changed when nominal returns are lower across the spectrum. On the other hand, the fall in nominal returns may have led customers to raise their awareness of other opportunities they had not previously contemplated, accelerating the trend towards greater financial sophistication.

In brief, the control of inflation will bring a large number of conflicting influences to bear on the make-up and size of banks' balance sheets, making any conclusions on their shape at the end of the transition period highly speculative. Such influences include shifts in corporate demand for funding between equity, bond and loan finance; shifts in personal loan demand between fixed and floating-rate finance; and shifts in the relative willingness to supply these various forms of funding, as between banks and direct investors. It is nevertheless possible that the signs of disintermediation already observed in the United Kingdom in the short term might continue in the longer term. If so, this would mean a further trend away from traditional branch banking, but with increased opportunities for banks to earn non-interest income, for instance by selling higher return investment products to depositors.

A range of other possible features of low inflation banking may be identified. For instance, below a certain point, the interest which banks earn on non-interest-bearing current accounts no longer covers the cost of providing the standard money transmission services on such accounts. Low nominal interest rates may therefore increase the pressures on banks to end cross-subsidisation of products, by targeting cost recovery accurately at each service provided. Such pressures already exist, with the steady drift towards interest-bearing current accounts, as well as the current impetus to offer more transparent pricing.

Another area where more accurate pricing becomes possible, to the clear advantage of both bank and customer, is corporate lending. Low inflation and the attendant less volatile nominal interest rates take some of the guesswork out of banks' assessment of corporate borrowers' future cashflows, and hence their creditworthiness—making longer-term and even fixed-rate finance more feasible for both parties, by reducing the risk premia on such borrowing.

In summary, banks will have to adapt their longer-term planning to allow for possibly significant changes in their business profile which may emerge in a post-inflationary world. The task for monetary policy is to persuade banks (and others) in the United Kingdom that price stability is now a permanent feature of the economy.

Excess banking capacity?

During the year, an internal working group in the Bank considered whether there is excess capacity in UK banking markets. Broadly, excess capacity can be said to exist in a sector whenever a reduction in capacity would increase aggregate profitability. If banks are using capacity to produce banking services which they can only sell unprofitably, or if they have capacity lying idle, their profitability will be lower than it could be.

But why should banks retain excess capacity? To put the question another way, why should a bank retain more branches, more staff, more capital than it would choose if it were entering a market afresh? Even assuming the bank is well managed, it might still do so for three reasons. First, banking (in its traditional form at least) is a long term business. A bank may not know that a loan it makes today is bad business until five or ten years from now. Because of these long time lags, banks may react relatively slowly to changing market conditions. Secondly, strategic interaction between banks can make an individual bank unwilling to shed capacity lest it yield a competitive advantage to its rivals. If all banks behave this way, the overall result is that excess capacity persists throughout the industry. Finally, some forms of capacity are easier to shed than others. Modern office buildings in prime locations, for example, can be readily adapted for new uses; high street branches, by contrast, are less flexible and may also be difficult to sell. In general, where there are high 'exit costs', excess capacity is more likely to persist.

It is often argued that excess capacity has emerged in UK domestic banking markets over the past ten or twenty years. Possible reasons include the entry of new players such as building societies and foreign banks into traditional banking markets, and technological changes which enable banks to deliver services more cheaply and make existing capacity redundant: for example, automatic teller machines and telephone banking may be turning branches into 'excess capacity'.

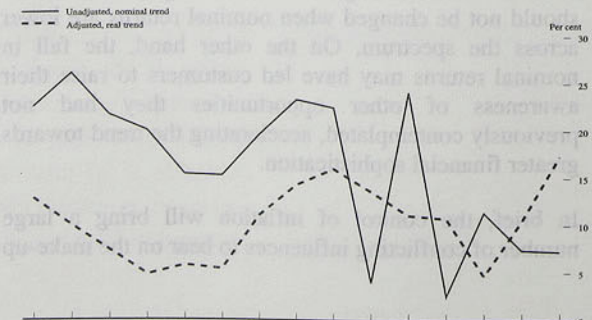
If excess capacity had developed, this should be reflected in declining profitability. The unbroken line in the chart shows the reported return on equity of the largest six UK banks between 1978 and 1992. Within the cyclical pattern, there is indeed a definite downward trend. Using reported profitability is misleading, however, for at least three reasons. First, in periods of higher inflation, banks will earn a higher nominal return on the proportion of their shareholders' funds which is invested in banking assets when, in fact, they are no more profitable in real terms. Secondly, there are always time lags between the years in which banks recognise the income and operating expenses associated with a portfolio of loans and the years in which they recognise provisions against any bad debts. The high provisions against loans to less developed countries in the late 1980s, for example, were made against loans booked five, ten or even fifteen years previously. To get a truer picture of bank profitability, therefore, it is advisable to 'smooth back' provisions over the life of the loans to which they relate. Thirdly, the nature of banking (in particular the range of markets entered and products offered) has changed markedly over time.

The broken line in the chart shows the pre-tax return on equity of six large UK banks between 1973 and 1992 after adjustments have been made for the first two distortions described above. Although various simplifying assumptions have to be made, this line should be a better representation of the banks' underlying profitability. The trend, although still significantly distorted by the cycle, is flat or slightly upwards.

This is not conclusive evidence that excess capacity has **not** developed in UK banking markets as a whole. It may be, for example, that the riskiness of the banking sector has increased: investors in bank shares therefore require greater profitability than previously, which on the above evidence banks have not been able to achieve, and excess capacity provides a possible explanation for this. Nor does the evidence mean that excess capacity has not existed for periods of time in particular areas: such as, perhaps, the syndicated loan market in the late 1980s.

But the profitability trends do not on the other hand provide clear evidence that excess capacity **has** developed to any significant degree. This suggests that most banking capacity is adaptable and that banks have been able to find new, profitable uses for their resources. For example, although deregulation has made some banking markets more crowded, it has also opened up new markets to the banks, such as insurance, into which capacity can be transferred. What this means is that banking markets have become more prone to change. More than ever, the onus is on management to have the systems to enable them to monitor closely how profitable their various businesses are, and to anticipate, or adapt quickly to, change as it occurs.

Six large UK banks: published, nominal and adjusted, real returns on equity 1978-1992



Part II
Policy developments

(i) Changes implemented in the United Kingdom[1]

Large Exposures Directive

In October 1993, the Bank issued a notice (BSD/1993/2) concerning the implementation of the EC Directive on the monitoring and control of credit institutions' large exposures, adopted in December 1992. This notice replaced three earlier notices.

Although the terms of the Large Exposures Directive are broadly in line with the Bank's existing large exposures policy, implementation of the Directive has led to several changes. In compliance with the Directive, the new policy introduces explicit limits on the size of exposures that may be undertaken by UK-incorporated authorised institutions at the consolidated level:

- in aggregate, exposures which individually exceed 10% of capital base should not exceed 800% of capital base;
- no exposure to an individual counterparty should exceed 25% of capital base; and
- the total of exposures to unconsolidated connected counterparties should not exceed 25% of capital base.

These limits operate in parallel with the notification requirements of the Banking Act. Certain types of exposure (exposures to banks and building societies under one year in maturity; exposures to central governments and central banks; exposures secured by cash or government securities) are exempted from the limits. The definition of an exposure is also extended to include exposures on interest rate and foreign exchange related contracts.

While the Directive applies formally only at a consolidated level, the notice places the same limits and requirements on authorised institutions at an unconsolidated level.

On-balance-sheet netting and cash collateralisation

In December 1993, the Bank of England issued a notice (BSD/1993/3) revising its capital adequacy reporting rules in the area of on-balance-sheet netting and cash collateralisation. The **on-balance-sheet netting rules** give guidance on the circumstances in which banks may report debit and credit balances with a single customer (or customers in the same company group) as a single net item. This reduces the amount of the reported asset against which capital must be held. The **cash collateralisation rules** give guidance on when banks may weight assets at 0% in recognition of the existence of cash security.

The main changes to the previous rules are:

- there is no longer a requirement for the customer(s) and bank offices involved in the transaction to have the same residency. Banks may now report on a net or cash-collateralised basis where the customer is located in a different country from the office of the bank which holds the deposit or advances the credit;
- there is no longer a requirement in the netting rules that balances reported on a net basis must be denominated in the same currency;
- for both netting and cash collateralisation, banks must have an opinion from their legal advisers confirming the legal enforceability of the arrangement in all relevant jurisdictions. Group facilities being reported on a net basis must be supported by cross-guarantees; and
- in order to report balances on a net basis, banks must be managing the relevant accounts on a net basis.

At the same time as the issue of the supervisory notice, the Bank's Financial Statistics Division published a notice which set out revised guidelines for net reporting on forms other than the capital adequacy form.

(1) A list of policy and practice notices issued by Banking Supervision Division which are currently in force is contained in Appendix 2.

Notice on subordinated loan capital

In May 1994 the Bank issued a new notice (BSD/1994/3) setting out its requirements for perpetual and dated subordinated loan capital to qualify for inclusion in an institution's tier two capital. The notice adopted the proposals of a consultative paper issued in July 1992. It applies only to subordinated loan capital issued after May 1994.

The notice requires subordination provisions to be fully effective in a winding-up of the issuer (and of the institution, where different): the Bank now seeks confirmation from the institution that its legal advisers are satisfied that the subordination provisions are effective. The notice also restricts the events which can put subordinated loan capital into default, and stipulates that a lender's only remedy following such a default should be to petition for the winding up of the institution.

Money laundering

The EC Money Laundering Directive has been implemented by new measures in the Criminal Justice Act 1993 and Money Laundering Regulations 1993 ('the Regulations'), which became effective early in 1994. The main practical changes are:

- the Criminal Justice Act 1993 covers the proceeds of all serious crime, in addition to drug and terrorist related activities;
- the Regulations make it a criminal offence for a bank, building society or other financial institution not to have in place procedures to combat money laundering; and
- the Regulations recognise Guidance Notes issued by a supervisory authority or trade association. A court may take account of such guidance in deciding whether a person or institution has complied with the requirements of the Regulations.

Revised editions of the Joint Money Laundering Steering Group's Guidance Notes were published in October 1993 to reflect the requirements of this new legislation. As a result, the Bank wrote to all authorised institutions drawing attention to the revised editions and confirming them as the new criteria against which the adequacy of their systems and controls to counter money laundering would be assessed. The Bank continues to carry out such assessment by means of reporting accountants' reports (under section 39 of the Banking Act 1987).

The Regulations also require supervisory authorities themselves to report to the National Criminal Intelligence Service any information they obtain which in their opinion indicates that any person has or may have engaged in money laundering. The Bank has thus established and implemented procedures to meet this duty.

Statutory duty on auditors in the regulated sector

Sir Thomas Bingham's Report on the supervision of Bank of Credit and Commerce International SA (BCCI) recommended that auditors should have a statutory duty to report relevant information to the Bank. This recommendation was accepted by both the Bank and the Government, and statutory instruments implementing the recommendation across most of the financial sector were approved early in 1994 and, with one exception, came into force on 1 May 1994: the statutory instrument relating to the insurance industry comes into effect on 1 June 1994. In March 1994, the Bank issued a notice (BSD/1994/1) setting out the relationship between the Bank, auditors and reporting accountants which replaced the previous guidance issued in 1987 (BSD/1987/4).

Guidance note for reporting accountants

During 1993/94 the Bank undertook a review of the way in which it utilises reporting accountants' reports, commissioned under section 39 of the Banking Act. Following this review, several changes have been made to the required format of reporting accountants' reports on accounting and other records and internal control systems. Accordingly the Bank issued a new notice in March 1994 (BSD/1994/2) providing revised guidance to reporting accountants on the format of such reports, which replaced the earlier notice on the same subject (BSD/1987/2).

In addition to the existing requirements to list any material weaknesses found, reporting accountants are now required to provide in their report a summary of the main risks faced by the institution, the key controls in place and an overall assessment of the control environment, together with a brief description of the nature of transactions entered into by the institution. The other main changes to the guidance note include the introduction of a section on audit committees, and the strengthening of the section on internal audit.

Work of other bodies

Accounting developments

In December 1993, the Accounting Standards Board issued Financial Reporting Standard 4 on Capital Instruments, which was developed from the proposals of Financial Reporting Exposure Draft 3 with little change. The standard requires all financing transactions to be classified according to their form as either liabilities, equity or non-equity, and on the face of the balance sheet companies must identify shareholders' funds and minority interests as being equity or non-equity, and liabilities as either convertible or non-convertible.

In April 1994, the Accounting Standards Board issued Financial Reporting Standard 5 on Reporting the Substance of Transactions. The Standard incorporates a number of changes from the proposals of Financial Reporting Exposure Draft 4. In particular, offsets between debit and credit balances can now be allowed where there is a foreign exchange or interest rate risk.

In response to the auditors' new statutory duty to report relevant information to the Bank, the Auditing Practices Board published in March 1994 Statement of Auditing Standards 620 and a Practice Note, 'Direct reports to the Bank', which establish standards and give guidance to the accounting profession on the situations in which auditors and reporting accountants should report matters to the regulators.

Treasury and Civil Service Committee report on the role of the Bank of England

In March 1993, the Treasury and Civil Service Committee announced an inquiry into the role of the Bank of England. The Governor and other Bank officials were among those who gave evidence to the Committee during the year, and the Committee published its First Report on 'The Role of the Bank of England' on 8 December 1993.

Among the terms of reference of the inquiry was consideration of the role of the Bank of England as supervisor of banking institutions in the United Kingdom, and three of the Report's fifteen conclusions and recommendations related to supervision. The Committee first noted that, in the light of their previous criticisms, they greatly welcomed evidence of a shift in the Bank's attitude and approach to supervision. The Committee's main conclusion was that, although it is possible for prudential supervision to be undertaken by a body separate from the central bank, there is no overwhelming case for such a separation to be implemented in the United Kingdom, and that the balance of the argument would probably remain this way even if the Bank gained greater autonomy in the area of monetary policy. They noted nevertheless that they would need to review this position if there were to be a complete reorganisation of banking and financial services regulation and supervision.

(ii) Implementation in progress

The Capital Adequacy Directive

The Capital Adequacy Directive (CAD) sets minimum capital requirements for market risks in the trading books of banks and non-bank investment firms. It was adopted by the European Community during the first half of 1993, and will become part of the prevailing supervisory regime for banks and securities firms from 1 January 1996. The European Commission has recently begun to hold meetings to discuss issues raised by implementation of the directive. The Bank meanwhile continues to work on the implementation of the CAD in the United Kingdom, in discussion with other UK supervisors and market practitioners.

At the heart of the CAD lies the allocation of positions between the trading book and the non-trading book, also known as the banking book. The banking book will continue to be covered by the credit risk requirements set out in the Solvency Ratio Directive. The instruments that can be held in the trading book are prescribed in the Investment Services Directive (see below).

The Bank hopes to publish details of the revised supervisory regime in the second half of 1994, to enable banks to amend their systems as necessary by the implementation date of 31 December 1995.

Revision will also be needed to those aspects of the Bank's implementation of existing directives such as the Large Exposures, Own Funds, and Solvency Ratio Directives which apply to trading book positions.

Investment Services Directive

The European Community reached agreement during the year on an Investment Services Directive. This is intended to give non-bank investment firms in the EEA a 'passport' which will allow them to offer services throughout the EEA on the basis of a single authorisation in their home Member State.

The Directive's impact on banks' operations will be limited, since the freedom to passport has already been conferred on banks by the Second Banking Co-ordination Directive. The Investment Services Directive will, however, result in common minimum EEA-wide standards for the supervision of banks' investment business, including the broad principles governing conduct of business rules. It will also give UK banks the right to apply for membership of Stock Exchanges and other regulated markets in other Member States.

The implementation of those of the Directive's provisions which affect banks (including those institutions which are listed under section 43 of the Financial Services Act as wholesale money-market principals) is being co-ordinated with the FSA regulators. The Directive will come into force at the beginning of 1996, at the same time as the Capital Adequacy Directive.

Post-BCCI Directive

Provisional agreement has been reached among Member States on a directive to reinforce prudential supervision within the European Community following the collapse of BCCI (the 'Post-BCCI Directive'). It covers not only credit institutions but also investment firms and insurance companies. The Directive has four main provisions: first, it requires supervisors to refuse authorisation where group and ownership links preclude effective prudential supervision; second, member states must require that a financial undertaking has its head office in the same member state as the registered office; third, it allows member states to widen the range of disclosure gateways, to allow supervisors to provide confidential information to, amongst others, those supervising the accountancy profession, and to bodies responsible for the detection and investigation of breaches of company law (including external Inspectors); and, fourth, member states are required to place a duty on auditors, and experts (such as reporting accountants) appointed by supervisory authorities, to report material breaches of law and certain other concerns to the supervisory authorities. The date for implementation, and the nature of any changes that may be needed to UK legislation, will become clear once the directive has been finalised and adopted by the European Community.

Deposit protection

It is expected that the Directive on Deposit Guarantee Schemes will be adopted in May 1994 and will have to be implemented in Member States by 1st July 1995. The UK Government intends to enact Regulations to amend the relevant sections of the Banking Act 1987, following a short consultative period.

Under the changes proposed to the current UK scheme, qualifying deposits placed with the UK branch of a bank from another EEA country will be covered by the bank's home country deposit protection arrangements, rather than by the UK scheme as at present. The cover of the UK scheme will, conversely, be widened to branches of UK-incorporated institutions throughout the EEA. The other main changes proposed are the extension of the UK scheme to include deposits in other EEA currencies as well as sterling, and the increase in the level of cover offered by the UK scheme from 75% to 90%.

No changes are planned to the structure of the Deposit Protection Scheme nor the way it is funded. However, the UK scheme will have to offer 'top up' cover to UK branches of EEA banks whose home state cover is less generous than that offered by the UK Scheme. This 'top up' cover will give depositors with those branches which choose to pay for this option the same total level of cover as that offered to depositors with UK authorised institutions.

Peer group review

In his report on the supervision of BCCI, Sir Thomas Bingham commented that if host country supervisors were increasingly to rely on the home country supervisor, they must be reassured by some form of independent verification that the home country supervisor is really doing his job. He suggested that a 'system of peer group review' might be one way of meeting this need. The Bank has now reached agreement with supervisors from certain other G10 and EC countries on the broad form that reviews should take: in particular, the review of each country's supervisory body will be carried out by experienced supervisors from two other countries. The primary objective of the exercise is to provide supervisors with more information about other countries' regimes, and to encourage the spread of 'best practice' supervision as a means of establishing acceptable minimum standards.

(iii) Areas under discussion

Basle consultative papers

In April 1993, the Basle Supervisors' Committee issued three consultative papers, inviting comments by 31 December 1993. The topics covered were off-balance-sheet netting, market risk and interest rate exposure measurement. The Bank received a number of comments from interested parties in the United Kingdom, and these have been collated and forwarded to the Basle Committee.

Off-balance-sheet netting

The paper on off-balance-sheet netting proposed changes to the current recognition of netting of off-balance-sheet items (such as swaps, forwards and options). Under the current wording of the 1988 Basle Capital Accord, banks may only report exposures arising from swaps and similar contracts on a net basis where the netting is in the form of bilateral novation of contracts which amalgamates amounts due in the same currency and for the same value date into a single net amount. The Basle Committee has proposed widening this recognition to any type of bilateral netting contract which has a sound legal basis. The Committee has also outlined its preliminary thinking on how recognition of multilateral netting arrangements (netting of transactions through a central clearing house) might be incorporated into the Capital Accord.

These proposals have been widely supported by the market—they represent what is potentially a significant easing in capital requirements. Before netting agreements can be recognised, however, supervisors will have to be satisfied that there is no doubt in law that risk has been genuinely reduced. With regard to the position under English law, the Financial Law Panel published a statement in November 1993 which confirmed that bilateral netting in principle applies to off-balance sheet instruments under English insolvency law. It is also the case that, in order for UK banks to take advantage of any wider recognition of netting agreed in Basle, the EC's Solvency Ratio Directive will have to be amended. The European Commission has held discussions at a working party level with a view to formulating proposals to amend the Solvency Ratio Directive.

Market risks

The Basle Committee's paper on market risks proposes capital requirements which are broadly similar to the requirements of the Capital Adequacy Directive; the differences between the CAD and these proposals tend to be in the detailed risk weightings rather than in the overall framework.

The Bank received detailed and thoughtful responses on this paper, with some respondents drawing attention to the remaining differences between the Basle paper and the CAD, while others argued that banks which have more sophisticated and accurate internal monitoring and measurement systems should be able to make use of these in calculating regulatory capital requirements. The Basle Committee is now assimilating these comments and identifying topics requiring further work. At present no date has been fixed for any revised proposals to be incorporated into the Basle Committee's supervisory guidelines.

Interest rate exposure measurement

This paper proposes techniques for the measurement of interest rate exposure across a bank's entire activities. The intention is to enable supervisors to identify which banks are outliers in terms of interest rate exposure on a national and international basis.

The proposals contain suggestions for the treatment of interest rate exposure for items with behavioural characteristics which differ from their contractual terms, such as retail deposits. Several banks commented on how these compared with their existing system for measuring interest rate risk.

Derivatives

Over the last year there has been a great deal of interest in the subject of derivatives, with many reports from regulatory agencies and central banks worldwide (including one prepared by the Bank of England in April 1993) and a study by the Group of 30, a private sector body, last July.

A theme common to most of the reports was the rapid growth of derivatives contracts in the last 10 years or so, the comparative complexity of the instruments traded compared with their cash market equivalents, and the need for understanding and control by senior management. The concerns raised fall into two broad categories:

- micro-prudential issues relating to the supervision of individual institutions; and
- macro-prudential issues involving consideration of the linkages within the financial system.

Derivatives do not in themselves create any new type of risk which is not already present in other financial activities, although the incidence and scale of the risk may vary substantially from the corresponding cash market activities. For example, the depth and liquidity of the derivatives and cash markets may differ substantially from one another, even for trading the same basic product.

It is therefore important to ensure that the controls, monitoring systems, and accounting techniques are capable of meeting the needs of not only a bank's dealers, but also its senior management. Given the complexity of some derivatives products which link different risks into a single product this can present a major challenge.

Although the nominal values of the underlying instruments traded on derivatives markets are very large—frequently a multiple of the balance sheet of a bank—the risk in terms of a bank's exposure is normally significantly less. For example, at end-December 1993 UK banks' credit exposure, measured by calculating the amount which would be owed by counterparties to banks if the contract were to be terminated, together with a supplementary factor for all outstanding contracts, amounted to approximately 12% of the total balance sheet in respect of interest rate derivatives and foreign exchange derivatives combined.

There remains a considerable amount of work to do in connection with derivatives. A group of practitioners is providing valuable comments on the Bank's proposal for implementing the Capital Adequacy Directive. The Basle Supervisors Committee is collating and considering the comments received on the proposals put forward last year for modifying the Accord to incorporate a capital requirement for market risks. The G10 Central Banks are also considering what data to collect on derivatives which would be capable of aggregation at an international level, with the aim of shedding light on macro-prudential and macroeconomic issues. One possibility being explored is to collect information in conjunction with existing data surveys, such as that for foreign exchange.

Meanwhile, within the Bank of England, a specialist group has been established in the Banking Supervision Division to focus the expertise of the Bank in this area. Much of their time will be spent visiting the trading operations of banks, assessing their trading strategies, considering the control environment in which they operate and the monitoring and support functions available to both the dealers and senior management. In this way, the group will be able to keep as close as possible to the 'leading edge' of market developments. High on its list of priorities will be the review of computer models to determine capital adequacy, for those banks which have chosen to use this option under the Capital Adequacy Directive.

Proposed new approach to review team visits

As part of its review of the way in which it uses reporting accountants' reports (see page 20), the Bank also reconsidered the method of operation of its own review team staff. The way in which the work of reporting accountants and the review teams interlink has been restructured, to ensure that the examination of accounting records and systems and controls is clearly targeted at any issues about which the Bank may have a concern. It is also envisaged that where these reports reveal difficulties, the review teams will undertake fuller reviews.

(iv) Liaison with overseas supervisors

The Basle Committee on Banking Supervision

The Committee met three times during the year.

Discussions through the year have focused on proposals for the supervision of market risk. As mentioned above, Consultative Papers were published in April 1993 on the supervision of market risk, interest rate exposure measurement and off-balance-sheet netting.

Further work was carried out on the supervision of financial conglomerates, on derivatives and, in the light of the collapse of BCCI, a comparative study on bank insolvency arrangements.

The Committee has continued to monitor the progress of implementation and the impact of the 1988 Convergence Agreement. Final implementation of the Agreement was formally completed in July 1993 at which time the Committee was able to report that all G10 banks met the 8% Basle minimum capital requirement.

A joint meeting was held in December 1993 with regional representatives of non-G10 supervisors to discuss arrangements for strengthening relations between supervisors.

EC supervisory bodies

The Banking Advisory Committee (BAC) and the Contact Committee of EC Supervisory Authorities ('Groupe de Contact') met regularly during 1993 to discuss a host of legislative and practical matters.

In addition to the exercise of its 'comitological' functions (ie approving technical amendments to existing EC legislation), the BAC continued to work alongside the Commission in the preparation of legislative proposals such as the Investor Compensation Directive. The BAC also paid particular attention to general issues affecting the functioning of the Single Market, such as the transposition of EC legislation into national law and the adoption by the Member States of measures in the 'general good'. The BAC was assisted in its work by a newly-constituted Technical Working Group, which focused on the interpretation of existing legislation.

The Groupe de Contact, similarly, devoted much of its time to the technical discussion of interpretational difficulties, and to the development of bilateral arrangements for supervision. Other subjects considered by the Groupe de Contact included national authorisation and licensing procedures, the treatment of fiduciary deposits and 'no-correspondence' accounts, difficulties arising in the co-ordination of cross-border liquidation procedures, and crisis management. Much of the work carried out by the Groupe de Contact was fed into the BAC and/or the Banking Supervisory Sub-Committee.

The EMI Banking Supervisory Sub-Committee

The Sub-Committee, which is chaired by the Bank's Executive Director of Banking Supervision, Mr Quinn, met three times in the last year and has primarily focused on three supervisory issues: the management of crises affecting EC banks, the co-operative oversight of cross-border participation in EC Payment Systems, and factors leading to financial fragility in the European banking sector.

The Sub-Committee has produced a set of basic principles for supervisory co-operation in the event of crises affecting banks in the EC. These take the form of recommendations for co-ordination of flows of information and supervisory action between home and host supervisors. The principles were presented to the Council of the EMI in March 1994, when a working group set up to address the perceived causes of financial fragility and resulting concerns for banking supervisors also submitted a summary of its work: this working group had reported to the Sub-Committee in October. Finally, the Council of the EMI considered a paper setting out the broad objectives of co-operative oversight and information sharing with regard to EC payment systems, which has been prepared in conjunction with the Working Group on EC Payment Systems.

Part III
The legal framework and operational supervision

A. Developments in the legal framework

The European Economic Area

The European Economic Area ('EEA') includes all EU member states and certain EFTA member states (ie Norway, Sweden, Austria, Finland and Iceland[1]) and was established on 1 January 1994. In consequence, HM Treasury made regulations in 1993 to implement the United Kingdom's obligations in this area; their implications for the legal framework of UK banking supervision are described below.

The Banking Co-ordination (Second Council Directive) (Amendment) Regulations 1993

These regulations[2] came into force on 1 January 1994. They amend the '2BCD Regulations'[3] to bring the non-EU EEA countries within the definition of 'Member State' (the 2BCD Regulations themselves having come into force on 1 January 1993 to implement the Second Banking Co-ordination Directive ('2BCD') in the United Kingdom).

The legal effect of the amending Regulations is as follows:-

- UK-incorporated credit institutions which wish to carry on activities listed in Schedule 1 to the 2BCD Regulations in any of the non-EU EEA countries, whether through the establishment of a branch in those countries or on a cross-border basis, are now required to follow the notification procedures set out in the 2BCD Regulations.

- Conversely, credit institutions incorporated in the non-EU EEA countries which wish to carry on Schedule 1 listed activities in the United Kingdom, whether through the establishment of a branch in the United Kingdom or on a cross-border basis, are also now required to follow the notification procedures set out in the 2BCD Regulations.

- Credit institutions incorporated in the non-EU EEA countries which were authorised under the Banking Act on 31 December 1993 became 'European authorised institutions' under the 2BCD Regulations with effect from 1 January 1994.

- Credit institutions from the non-EU EEA countries which are subsidiaries of undertakings incorporated in countries outside the EEA are prohibited from carrying on Schedule 1 activities in the UK in the case where the EU has decided to exercise its reciprocity powers under 2BCD.

Finally, with effect from 1 January 1994, all references to EU countries in Banking Act supervisory notices issued by the Bank are to be construed to include the non-EU EEA countries. This reflects the Bank's own practice, and is not a provision of the amending Regulations.

Statutory instruments

Made under the Banking Act 1987

Two statutory instruments have been made under the Act since last year's Report was published. The Banking Appeal Tribunal (Amendment) Regulations 1993[4] came into force on 30 April 1993. These regulations amend the Banking Appeal Tribunal Regulations 1987[5] to take account of changes introduced by 2BCD; they also make certain changes to the procedure governing appeals, including the time-limits for bringing an appeal, and provide increased protection for commercially sensitive information.

The Accountants (Banking Act 1987) Regulations 1994,[6] which came into force on 1 May 1994, implement the recommendations in the Report of the Bingham Inquiry into the supervision of BCCI that a statutory duty should be imposed on the auditors of banks to report to the Bank of England matters which

(1) Referred to hereafter as the 'non-EU EEA countries'. It is expected that Liechtenstein will be included at a later date.
(2) SI 1993 No 3225.
(3) More precisely, the Banking Co-ordination (Second Council Directive) Regulations 1992: SI 1992 No 3218.
(4) SI 1993 No 982.
(5) SI 1987 No 1299.
(6) SI 1994 No 524.

are relevant to the fulfilment by banks of the criteria for authorisation in Schedule 3 to the Banking Act 1987 (see page 20 above).

Made under the European Communities Act 1972

In the same period, one statutory instrument of relevance to the legal framework of UK banking supervision was made under this Act. This was The Banking Co-ordination (Second Council Directive) (Amendment) Regulations 1993, mentioned above.

Statements of Principles

A revised Statement of Principles, taking into account the amendments to the Act made by the 2BCD Regulations and changes in the Bank's supervisory approach resulting from various other EC directives, was published in May 1993 under section 16 of the Banking Act. The Bank also published Statements of Principles in relation to European institutions and UK subsidiaries respectively, as required by the 2BCD Regulations. The Statements of Principles are available separately on request.

The Statement of Principles published in May 1993 by the Bank under section 16 of the Act contains a number of references to money laundering in the context of the Bank's interpretation of the criteria in Schedule 3 to the Act. The Bank's interpretation of the criteria now takes into account the coming into force of the Money Laundering Regulations 1993[1] and the publication of revised editions of the Joint Money Laundering Steering Group's Guidance Notes. As noted on page 20, the Bank considers that the revised Guidance Notes are appropriate criteria against which to assess the adequacy of a bank's systems and controls to counter money laundering,[2] and compliance with them will consequently be taken into account in determining whether the requirement for a bank to maintain adequate accounting and other records and adequate systems of control of its business records (Schedule 3, paragraphs 4(7) and (8)) is met.[3]

Contravention of the Money Laundering Regulations will also call into question whether the integrity element of the requirement for the business of a bank to be carried on with integrity and skill (Schedule 3, paragraph 5) is fulfilled.[4] The Bank will also give particular weight to whether a person has contravened the requirements of the Regulations in considering whether the requirement for directors, controllers and managers to be fit and proper persons is met (Schedule 3, paragaph 1).[5]

The following papers are added to the table in paragraph 2.5 of the Statement of Principles published in May 1993 by the Bank under Section 16 of the Act:

(i) Implementation in the United Kingdom of the Directive on the Monitoring and Control of Large Exposures of Credit Institutions (BSD/1993/2, October 1993).

(ii) On-balance-sheet netting and cash collateral (BSD/1993/3, December 1993).

(iii) The Bank of England's relationship with auditors and reporting accountants (BSD/1994/1, March 1994).

(iv) Guidance note on reporting accountants' reports on accounting and other records and internal control systems (BSD/1994/2, March 1994) .

(v) Subordinated loan capital (BSD/1994/3, May 1994).

Recent rulings of the Banking Appeal Tribunal

In 1993/94 appeals were lodged in respect of the Bank's exercise of its powers in relation to two authorised institutions. For the first time, the Banking Appeal Tribunal authorised the publication of its decisions in relation to one set of appeals, and of its chairman's rulings on preliminary issues in respect of both appeals.

(1) 'Banks and Banking Financial Services: The Money Laundering Regulations' (SI 1993 No 1933).
(2) The references in the May 1993 Statement of Principles to the guidance notes on money laundering issued by the Joint Money Laundering Working Group are now therefore taken to refer to the Joint Money Laundering Steering Group's Guidance Notes published in October 1993.
(3) Paragraph 2.27 of the Statement of Principles May 1993.
(4) Paragraph 2.38 of the Statement of Principles May 1993.
(5) Paragraph 2.47 of the Statement of Principles May 1993.

Mount Banking Corporation Ltd (in administration)

The administrators of Mount Banking Corporation Ltd (in administration) appealed on behalf of the company against the Bank's decision to impose a time-limit of three months on its authorisation, and two individuals appealed against findings that they were not fit and proper to be directors or controllers. (An appeal was also lodged by a former director against a similar finding, but this was withdrawn.) Because these appeals were related, they were heard together on 7-14 September 1993. This was the first time that appeals brought under the Banking Act 1987 had been heard in full. The Banking Appeal Tribunal's decisions, and its chairman's ruling on a preliminary issue, were published on 14 October following certain modifications to the text of the decisions, made at the request of the appellants, to protect information given to the Bank in confidence.

The Banking Appeal Tribunal took the view that, in relation to findings on factual matters, its role was to evaluate the evidence which had been before the Bank and to decide whether the findings were justified. Where the point at issue was how the Bank had chosen to exercise its discretion, the Tribunal believed it should adopt an approach similar to that which a court would adopt on an appeal from a first instance judge.

On this basis, the Tribunal held that the Bank's decision to place a time-limit on the authorisation and its findings in relation to the two individuals' fitness to be directors or controllers were lawful and reasonable. Costs were awarded in favour of the Bank. The individuals found not fit and proper subsequently appealed to the High Court on two points of law; one has now withdrawn his appeal.

Roxburghe Bank Ltd (in administration)

Appeals were lodged by the administrators of Roxburghe Bank Ltd (in administration) and several of its directors, but these were all withdrawn before a full hearing could take place. Costs were awarded in favour of the Bank, with those of the administrators being payable as an expense of the administration. The chairman of the Banking Appeal Tribunal also authorised the publication of certain orders for directions and rulings on preliminary issues which he had made during the early stages of these appeals. These included rulings that the Tribunal had no jurisdiction to hear an appeal made out of time, and that the conduct of an appeal by an institution in administration rested with the administrators, not with its directors, shareholders or their representatives.

B. Operational supervision

(i) The 'authorised population'

The 'authorised population' consists of institutions authorised under the Banking Act 1987 and European authorised institutions ('EAIs'). EAIs are authorised by the relevant home state authority and are recognised under the 2BCD Regulations. They are not authorised by the Bank. 14 credit institutions incorporated in the non-EU EEA countries ceased to be authorised under the Banking Act and became EAIs on 1 January 1994, joining existing EAIs from EU countries.

The authorised population rose for the first time in eight years (Table XI). However, the population total now includes a number of EAIs which are not entitled to accept deposits in the United Kingdom through UK branches: the number of institutions actually permitted to accept deposits in the United Kingdom fell once again, to 486.

Institutions authorised under the Banking Act

There were 389 institutions authorised under the Banking Act at the end of February 1994. 157 of these institutions were represented in the United Kingdom by branches of institutions incorporated outside the EEA and 232 were incorporated in the United Kingdom. Of the UK-incorporated institutions, 76 were subsidiaries of overseas companies and 8 were joint ventures involving overseas institutions.

European authorised institutions

As at end-February 1994, there were 129 institutions recognised under the 2BCD Regulations as European authorised institutions. Of these, 97 have branches in the United Kingdom which are entitled (among other things) to accept deposits in the United Kingdom, and 2 have branches in the United Kingdom which are entitled only to carry on other of the activities listed in Schedule 1 to the 2BCD Regulations. The remaining 30 EAIs offer services only on a cross-border basis into the United Kingdom.

Table XI
The 'authorised population'(1)

End-February	1987	1988	1989	1990	1991	1992	1993	1994
UK-incorporated	334	313	295	289	275	263	253	232
Incorporated outside the United Kingdom	254	254	256	259	255	255	255	286
Total	**588**	**567**	**551**	**548**	**530**	**518**	**508**	**518**
of which:								
EAIs with UK branches entitled to accept deposits in the United Kingdom							*79*	*97*
Other EAIs							*—*	*32*

(1) Includes European authorised institutions, which are not authorised under the Banking Act - see above

New authorisations

In the year to end-February 1994 ('1993/94') five applications for authorisation under the Banking Act were granted by the Bank—two to UK-incorporated institutions and three to institutions incorporated overseas wishing to open branches in the United Kingdom.

New European authorised institutions

During 1993/94, five new European authorised institutions became entitled to establish branches in the United Kingdom for the purpose of accepting deposits in the United Kingdom. Two other EAIs also established branches in the United Kingdom: one of these is not entitled to accept deposits, while the other is only entitled to accept deposits by the provision of services on a cross-border basis. A further 30 EAIs became entitled to carry on, by the provision of cross-border services only, various listed activities.

Table XII
New authorisations under the Banking Act and new EAIs

Year to end-February	1987	1988	1989	1990	1991	1992	1993	1994
Banking Act Authorisations	37	21	12	15	15	25	26	5
New EAIs with UK branches entitled to accept deposits in the United Kingdom								5
Other new EAIs								32

Surrenders

Thirty authorisations were surrendered in the year 1993/94, compared with thirty-three in 1992/93. Eighteen of these were accounted for by mergers and acquisitions of banking institutions, and restructurings and rationalisations of banking groups—including surrenders by four UK subsidiaries of banks incorporated in other EEA countries which still maintain UK presences in the form of branches recognised under the 2BCD Regulations. Two other overseas-incorporated institutions surrendered following changes of legal entity in their home countries, and the new entities both subsequently obtained authorisation. One institution surrendered after the Bank had imposed restrictions on its authorisation and it had subsequently been placed into administration. In another case, the institution surrendered after the Bank had imposed restrictions on its authorisation. Eight other institutions surrendered their authorisations because, for a variety of other reasons, they no longer wished to accept deposits in the United Kingdom.

In cases where an institution surrenders its authorisation but retains deposits, the Bank's supervisory role continues until such time as all depositors are repaid—such institutions are 'former authorised institutions' within the meaning of Section 106 of the Banking Act. The Bank has the power to give such directions to former authorised institutions as it considers necessary in the interests of depositors. Directions were given to two former authorised institutions in 1993/94.

One institution ceased to be a European authorised institution during the year.

Revocations, prohibitions and restrictions

Sections 11 to 14 of the Banking Act provide the Bank with powers to take action against an authorised institution on a number of grounds. These powers may in particular be exercisable if it appears to the Bank that any of the minimum criteria for authorisation set down in Schedule 3 to the Act is not or has not been fulfilled, or may not be or may not have been fulfilled, in respect of the institution. In the year 1993/94, one institution had its authorisation revoked. Another notice of intention to revoke was issued by the Bank. The Bank restricted the authorisations of seven institutions by imposing conditions on their businesses. No formal action was taken against any European authorised institution during the year.

Table XIII
Revocations and restrictions [(a)]

Year to end-February	1989	1990	1991	1992	1993	1994
Revocation of authorisation (b)	–	–	3	1	3	1
Restriction of authorisation	2	2	4	4	12	7
Revocation of restricted authorisation	–	–	–	–	2	–

(a) The table only relates to institutions authorised under the Banking Act. It records cases in the year that the Bank's formal notice of revocation or restriction was given. In some cases the revocation did not take effect until the following year and in a few cases the institution surrendered its authorisation or a conditional authorisation expired, before the revocation took effect. It is not therefore a record of authorisations revoked or restricted but of the use of the Bank's powers.

(b) Including the expiry of a time limited authorisation.

Appeals

A total of seven appeals were lodged against the Bank's decisions to exercise its powers in 1993/94, relating to two authorised institutions. The details are given in the 'Legal Framework' section above.

Administration orders and liquidations

Two authorised institutions were placed into administration during 1993/94, in both cases on the application of the directors. The authorisation of one was subsequently surrendered. Two other authorised institutions continued in administration: in one case a Scheme of Arrangement was reached during the year, in the other a Company Voluntary Arrangement (CVA) was agreed with creditors. CVAs were also agreed in two other cases, one an institution which has not so far been subject to formal insolvency procedures, the other a former authorised institution which remains in administration.

(ii) Supervision of the 'authorised population'

Interviews, visits and prudential/statistical returns

The number of meetings was slightly below the level of recent years, although there were still over 3,000 meetings held during 1993/94. The majority—nearly 2,000—were non-routine meetings held to discuss specific issues. The Bank's routine meetings are of two main types: the prudential interview to discuss the institution's performance and attendant supervisory issues; and the trilateral meeting attended by the Bank, the institution and its reporting accountants, at which the main item for discussion is reports produced by the reporting accountants under Section 39 of the Act. In 1993/94, there were 401 interviews with institutions incorporated in the United Kingdom, 283 routine interviews with branches and 357 trilateral meetings.

The Bank continues to operate its review team system, whereby Bank staff, together with bankers and accountants seconded to the Bank, visit the premises of authorised institutions to assess the quality of their lending and the adequacy of their systems and controls. Such visits are made to a wide range of institutions of varying size and complexity. Some visits will be able to cover the full range of a bank's activities; others will concentrate on particular business streams. Occasionally so-called 'special' review team visits are carried out which focus on a specific issue. Short visits may take two days at one location, but complex visits may extend into weeks and cover multiple locations throughout the country. Each review team typically includes two or three people. During the year, 112 full review team visits were carried out, along with a further 11 'special' visits.

In addition, visits are conducted to review the foreign exchange operations of institutions and assess them in terms of the guidelines set by the Bank for foreign exchange positions. The total number of such visits during the year was 41. Both the review team and the foreign exchange visits are conducted with the co-operation of the institution and do not involve the use of the Bank's statutory powers.

Bank officials regularly undertake visits to the head offices of institutions, overseas branches and subsidiaries of UK institutions, and for discussions with overseas supervisors. Such visits extended to 22 countries during 1993/94, and 81 meetings were held at home and abroad with overseas supervisors.

Use of powers to obtain information

Section 39 of the Act gives the Bank powers to require an institution to commission reports from reporting accountants, to establish among other things the adequacy of its systems and controls and the accuracy of its prudential returns. In addition to routine section 39 reports, special reports may be commissioned if a specific area of concern is identified. Section 39 also allows the Bank to require an institution or former authorised institution, or other persons (for example, an institution's controllers), to provide documents and information to the Bank.

Experience with the Second Banking Co-ordination Directive

The Second Banking Co-ordination Directive (2BCD) came into effect for countries in the European Union on 1 January 1993, and for those EFTA countries who have chosen to participate in the European Economic Area (EEA)(1) on 1 January 1994. As a consequence, a total of 99 branches of European banks(2) in London are now designated as 'European authorised institutions' and are supervised solely by their home country supervisor for all purposes except liquidity, which is a shared responsibility with the host supervisor.(3) A bank incorporated in any EEA country is free to branch out elsewhere in the EEA, subject to satisfying its home supervisor that it is equipped to do so - often referred to as obtaining a 2BCD 'passport'. The host supervisor has no power of veto. European banks also now have a passport to provide services on a cross-border basis within Europe, but they must first notify their intention to supply such services unless they benefit from grandfathering rights.

Use of the passport

Banks have so far made little use of the new passport arrangements. This is not surprising, as the market for banking services in Europe has always been reasonably free—and particularly so in London. Furthermore, few banks were in an expansionary phase at the time that 2BCD came into effect. Nevertheless, there has been some movement into and out of the United Kingdom. Six UK banks have established a total of 19 branches elsewhere in Europe since the beginning of 1993, bringing the total of such branch presences to 48. In a number of cases this has involved the conversion of existing subsidiaries in other European countries into branches, thus economising on the use of capital and reducing the regulatory burden. On the inward passport, seven banks(2) have established new branches in the UK in the last year.

Effect on the Bank's supervision

The reallocation of supervisory responsibilities between home and host supervisor has been a significant change, and the details have therefore needed clarification. Accordingly, European supervisory authorities have been negotiating a series of bilateral memoranda of understanding to deal with a range of practical issues. These mostly concern formalising contact between home and host supervisors, which has become a more important part of the supervisory process.

Broadly speaking, there have been only limited changes to the Bank's role as **home supervisor**. Supervision of British banks with European (and indeed non-European) operations has always been conducted on a consolidated basis. This continues, with the principal supervisory focus being on the effectiveness with which the head office controls its European operations. However, the Bank **is** developing its supervisory approach to European branches in a variety of ways, including: more emphasis on European operations in the course of routine supervision, such as prudential interviews; more travel to visit the branches; and more contact with host supervisors. This is being done on a case-by-case basis, with an important consideration being the scale of the European operations relative to the size of the whole institution.

The supervisory changes for the Bank as **host supervisor** are more marked, because the Bank is now responsible, in co-operation with the home state, only for local liquidity. In the short run, the change in responsibilities has involved a good deal of work: in completing unfinished business arising from the previous regime, in passing over relevant information to home supervisors, and in putting the appropriate arrangements in place for the supervision of local liquidity. Nevertheless, the Bank has already achieved significant resource savings in this area. A total staff saving of 9 has been achieved so far, with further savings likely over the next year or so. The Bank is, however, continuing to keep in contact with European branches in London, partly because of its role in relation to liquidity, partly because of its obligations to the home supervisor, and partly out of a wish to follow developments in the markets in which these branches operate.

(1) Austria, Finland, Iceland, Norway and Sweden.
(2) Of which 2 are not entitled to accept deposits through their UK branches.
(3) The Money Laundering Directive also imposes obligations on member states in relation to all banking business carried on within their jurisdictions.

During 1993/94, 620 section 39 reports were commissioned (244 of them on foreign branches), including special reports on two institutions.

Section 41 of the Act empowers the Bank to commission reports from competent persons on authorised institutions or former authorised institutions where areas of concern have been identified and where it is in the interests of depositors to do so. Three such reports were commissioned during 1993/94.

The Bank did not exercise its formal investigatory powers under the Act in relation to European authorised institutions during the course of the year.

Shareholder controllers of authorised institutions

The Banking Act provides that persons must notify the Bank of their intention to become a shareholder controller of an authorised institution which is incorporated in the United Kingdom, or to increase their level of control through any of the threshold points defined in the Act. The Bank assesses, among other things, their fitness and properness to become shareholder controllers at the proposed threshold. 35 notifications for new or increased control were received in 1993/94. 30 were passed without objection and five were withdrawn.

Representative offices of overseas institutions

In 1993/94, 22 overseas institutions notified the Bank of their intention to establish representative offices in the United Kingdom, and six institutions notified the Bank of their intention to change the name used by them in the United Kingdom.

The Bank remained alert to, and investigated, suggestions that overseas institutions had established UK representative offices without giving the Bank prior notification, in contravention of section 75 of the Act. In almost all cases, investigation found that, if such offices existed, they briefly used UK accommodation address/mail drop facilities arranged by entities incorporated in, and with bank licences purchased from, centres where there is little or no banking supervision.

Banking names and descriptions

Eighteen institutions changed their registered names during the year after giving notice to the Bank under section 70 of the Act. No notices of objection to the proposed name changes were issued.

The Bank also examined 123 names submitted during the year by persons who were not authorised under the Banking Act or European authorised institutions, in order to consider whether such names would be likely to breach the prohibition on the use of banking names as set out in section 67 of the Act. The Bank indicated that 26 of the proposed names would, or might be likely to, breach the Act.

During the year, the Bank also became aware of, and pursued, a number of cases where names and descriptions were being used in a manner that appeared to breach the prohibitions in sections 67 and 69 of the Act. In most instances either no physical presence of the entities or their representatives could be identified, or the case was resolved without formal action being required.

Discount houses

There have been no changes in the names or number of discount houses over the year. The Bank continues to have a direct dealing relationship in the sterling money markets with seven discount houses authorised under the Banking Act and one gilt-edged market-maker.

The discount houses are supervised by the Wholesale Markets Supervision Division of the Bank. Supervisory arrangements are broadly unchanged from those set out in the Bank's paper of October 1988, *Bank of England operations in the sterling money markets*, although some refinements have been made. The Bank has continued to monitor the houses' positions under the terms of the EC Second Banking Co-ordination Directive and the Consolidated Supervision Directive; and to monitor their compliance with the terms of the exemption from the Solvency Ratio Directive.

During the course of the year, the Bank has also continued to pay particularly close attention to credit issues, the management of liquidity, and systems and controls. In order to ensure compliance with EC Directives and with the recommendations made by

Sir Thomas Bingham in his Report on the supervision of BCCI, the Bank is in the process of requesting routine reports under section 39 of the Banking Act on all of the houses.

(iii) Prohibition on unauthorised deposit-taking

Last year it was reported that a defendant had pleaded guilty to charges under section 3 of the Banking Act (unauthorised deposit-taking). This defendant was subsequently sentenced to 12 months' imprisonment. During the year, another individual who pleaded guilty to a number of charges under section 35 of the Banking Act 1987 (fraudulent inducement to make a deposit) was given a custodial sentence of nine months.

There has been no slackening in the activity in investigating and prosecuting suspected offences under sections 3 and 35 of the Banking Act. There are two further cases that have been committed for trial at Crown Courts in the near future; one of them is for suspected offences under section 3 and the other for suspected offences under section 35. A number of other cases are being investigated which may give rise to further prosecutions.

In one other case under investigation, the Bank successfully applied to the High Court for the appointment of a Provisional Liquidator to protect assets pending hearing of a creditor's petition for a company's winding up. In another case, the Bank gave support to a petition from a creditor to wind up a company.

The Bank has been concerned at the steady flow of cases of unauthorised deposit-taking coming to its attention. These tend to result in significant losses, and consequent hardship, to the depositors who often receive little or no repayment from the deposit-taker. As a result of this, the Bank took the initiative to issue a leaflet warning the public of the dangers of placing money with people who are not authorised to accept it. This leaflet, entitled 'Money in the Bank', was distributed to banks, building societies, post offices and a number of other outlets and received considerable publicity in the press. The leaflet explains how people can check whether those soliciting deposits are properly authorised and stresses that there are no deposit protection arrangements for funds placed with unauthorised deposit-takers. Copies of the leaflet can be obtained from the Public Liaison Group of the Bank of England.

Overall, the number of investigations of unauthorised deposit-taking carried out during the year rose to 43 (30 in 1992/1993). As in recent years, the bulk of resources was committed to a relatively small number of major cases, particularly those which have, or will, come before the courts. The Bank's powers under section 42 of the Banking Act 1987, which require the person on whom such a notice is served to provide relevant documents, information and answers to the investigators were exercised in 12 new investigations (one more than in 1992/1993) with a total of 71 individual notices being served (41 in 1992/1993). Two cases involved a total of 27 notices, reflecting both the extent and the complexity of the enquiries sometimes involved.

Where the Bank's investigators identify serious non Banking Act offences, information is passed to the Crown Prosecution Service or Serious Fraud Office as appropriate. During the year, one case was passed to the Serious Fraud Office, with the Bank continuing to liaise and assist on it. There have also been two cases during the year which have been prosecuted by other bodies, but where the Bank had an earlier involvement which resulted in investigators from the Bank giving evidence at the trials. At any one time the Bank normally has an interest in around 40 cases, some of which it is actively investigating or prosecuting, and others where different investigators or prosecutors are in the lead. It is estimated that the value of possible deposits involved in all current cases, both where the Bank is the lead investigator and where other prosecuting authorities are now taking cases forward, is around £35 million.

The Special Investigations Unit and the Legal Unit

It was reported last year that two new units had been set up in the Bank, as part of the response to Sir Thomas Bingham's Report on the Bank's supervision of BCCI. These are the Special Investigations Unit (SIU) and the Legal Unit.

The Special Investigations Unit

The primary role of the SIU is to advise the line supervisors on appropriate action to take in pursuing suspicions and warnings of fraud and other criminal activity involving authorised institutions, and, wherever appropriate, to undertake investigations of such cases. It also has a general responsibility to assist in formulating relevant training for the supervisors to help develop their alertness to fraud in the banking system. In a wider context the SIU maintains close liaison with other investigating and law enforcement agencies, and it is represented on the Financial Fraud Information Network, of which Ian Watt, the head of the SIU, is currently the chairman.

The intention has been to maintain the SIU as a small, but flexible, unit. It has two sections, one dealing primarily with the investigations work, the other fulfilling an 'intelligence desk' function through its liaison with agencies in the United Kingdom and overseas. The current staff complement is 11 in total, including both experienced banking supervisors and specialist forensic accountants recruited from major international accountancy firms. The investigations section is to be expanded modestly in the course of 1994 with the appointment particularly of additional accountants.

The SIU now acts as the focal point for all cases where there are concerns about possible criminal activity involving institutions for which the Bank has supervisory responsibility. This includes cases where the institution is the victim. The SIU is required to evaluate each case referred to it, and determine whether further enquiry or action is justified by the Bank. This may range from providing advice to the supervisor on an appropriate line to take, through to conducting an on-site investigation at the premises of an authorised institution, either independently or in conjunction with staff of Banking Supervision Division. 170 cases have been referred to the SIU since its inception. Some 50% of these have required further action by the SIU, although such action may only amount to the provision of advice. In addition, the SIU has instituted a programme of reviews of individual supervisory files to help identify any indicators of fraud, or of the potential for fraud, that might exist within the information routinely available to the Bank.

To assist in its work, the SIU has installed an advanced database and text retrieval system. Development work continues in conjunction with BSD, with the objective of ensuring that the Unit will, at all times, have on-screen access to a fast, comprehensive information base.

The Legal Unit

The Legal Unit provides advice to the Bank's supervisory areas on legal questions arising in the course of their work. The Unit's prime objective is to ensure that the Bank, in its supervisory role, takes full account of the powers available to it under the law. One of the Unit's key functions is to provide the supervisors with a legal focus on day-to-day issues arising in the course of their work. It is also involved with the legal dimension of policy issues, including proposals for new and amending legislation affecting the supervisory areas and questions relating to the implementation and interpretation of EC Directives. Members of the Unit also contribute to internal training courses on legal issues affecting the work of Banking Supervision Division.

The Unit at present comprises ten lawyers, a number of whom are on short-term secondments to the Bank, together with three Bank Officials and the necessary support staff. Recourse is also had to external legal advice, where appropriate.

Part IV
Organisation and staffing of Banking Supervision Division

Staff

Staff numbers at end February 1994 were identical to those of a year previously, when allowance is made for two categories of staff not previously included: namely secretarial and Information and Records support staff (for which the Division took over responsibility from the Bank's central services during 1993), and staff involved in Deposit Protection Fund distributions. For the year to end-February 1995 the budgeted number is 256, an increase on a like-for-like basis of seven staff. The Division has again found invaluable the contribution of its eight inward secondees, of whom three are from clearing banks and five from the main accounting firms. They join some of the Division's own staff in visiting institutions to carry out review team visits.

Michael Foot succeeded Roger Barnes as Head of Banking Supervision Division on 31 August 1993, upon Mr Barnes' retirement from the Bank. Richard Farrant, Deputy Head responsible for policy matters, resigned from the Bank to become the chief executive of the Securities and Futures Association, and was succeeded on 21 September 1993 by Clifford Smout.

Table XIV
Allocation of Banking Supervision Division Staff

End-February	1990	1991	1992	1993(a)	1994
Managers	35	34	32	30	29
Analysts and assistants	147	149	147	146	152
Inward Secondees/Review Teams	10	11	10	10	11
Support services (b)					57
Total	**192**	**194**	**189**	**186**	**249**

(a) Figures include 3 managers, 7 analysts and assistants, and 2 secondees who subsequently transferred to the Legal Unit or the Special Investigations Unit.

(b) Until May 1993, Support Services Staff were budgeted for centrally in the Bank.

	Staff		Institutions	
	1993	1994	1993	1994
UK retail and merchant banks (a)	25	27	73	71
Small & medium-sized UK institutions (b)	37	41	96	80
UK branches and subsidiaries of overseas banks, European authorised institutions (c)	65	64	332	360
Policy and other matters (d)	42	39	—	—
Administration and Review Teams	17	21	—	—
Support services		57	—	—
Total	**186**	**249**	**501[(e)]**	**511[(e)]**

(a) Groups 3-5 on the organogram at Appendix 1.
(b) Groups 6-9.
(c) Groups 11-18.
(d) Groups 1-2, 10, Information Technology, Deposit Protection Board.
(e) Excluding the 7 discount houses, which are supervised by Wholesale Markets Supervision Division.

Training of staff

The Division's extensive programme of external courses in accountancy, banking and legal issues has now been supplemented by one aimed at alerting staff to signs of financial fraud and malpractice. All new entrants to the Division receive an introductory course on banking supervision, and new graduates also participate in a Bank-wide graduate training programme.

Several staff of the Division have continued to benefit from secondments. Overseas, staff are working in Hong Kong, the Cayman Islands and at the Bank for International Settlements and at the European Commission. Within the United Kingdom, secondments to banks for staff to gain experience of derivative products have continued.

Training provided by Banking Supervision Division

The growing demand from overseas supervisory authorities for advice and training has continued, and led to the creation from 1 March 1993 of a second full-time managerial 'secondment' to the Bank's own Centre for Central Banking Studies. In 1993/94, 23 formal training programmes were provided, nine in the United Kingdom and the remainder overseas; as before, the Former Soviet Union and other former centrally planned economies have been a prime focus, but more traditional contacts in the developing world have also been important recipients of both training and technical assistance.

In addition, overseas visitors, mainly from central banks and governments, come to the Bank on mostly short-term visits to familiarise themselves with the Bank's supervisory work. The number of such visitors to the Division during 1993/94 was some 40 people, a small increase over the previous year.

Information technology

The major project to transfer the Division's information systems from a mainframe to a local area network environment of personal computers, which began in the summer of 1992, was successfully completed during the summer of 1993.

Statistical data from reporting institutions is held on a new statistical database developed in conjunction with the Bank's Financial Statistics Division. The analysis and presentation of both statistical and non-statistical data is achieved using flexible personal computing software tools. The project also involved the upgrade of the Division's office automation facilities.

A project to automate the Division's ability to access textual information has started, linked closely to work proceeding in the SIU and Legal Unit. The results of a pilot exercise will be evaluated before a decision is taken to proceed with implementation of the system across the whole Division.

In addition to the support of the Division's internal systems, the division's IT Group also provides IT consultancy to line supervisors and participates in review team visits. The increase in the Division's interest in IT supervision may lead to greater demands for this service in 1994/95.

Banking Supervision Division organogram

As at 1 May 1994

The Governors — **Board of Banking Supervision**

Brian Quinn
Executive Director

M D K W Foot
Head of Banking Supervision

- P A C Smout — *Deputy Head, Policy, Statistical reporting*
  - R A Allen — *Manager, Group 1, Market Trading*
  - D Holt, J C W Osborn — *Managers, Group 2, General policy, Statistical reporting*
  - W D R Swanney — *Manager, Accountancy & special issues, Secretary of Board of Banking Supervision, Secretary of Deposit Protection Board*
- C F Sergeant — *Deputy Head, United Kingdom retail and merchant banks*
  - J Fischel — *Manager, Group 3, Major English clearers*
  - W M Hyde — *Manager, Group 4, Scottish and other UK clearers*
  - C J Thompson — *Manager, Group 5, Major UK merchant banks*
- D W Green — *Deputy Head, Medium and smaller UK banks, Investigations*
  - C M Miles — *Manager, Group 6, A-B & T-Z*
  - D A Reeves — *Manager, Group 7, C-E*
  - A E Pack — *Manager, Group 8, F-L*
  - J R Cooper — *Manager, Group 9, M-S*
  - P W Filmer — *Manager, Group 10, Investigations*
- J Bartlett — *Deputy Head, Overseas banks, North America & West Europe*
  - J C Cleland (a) — *Manager, Group 11, Austria, Belgium, France, Germany, Luxembourg, Switzerland*
  - J G Ellis — *Manager, Group 12, Canada, USA*
  - K S Pooley — *Manager, Group 14, Denmark, Finland, Gibraltar, Greece, Ireland, Italy, Malta, Netherlands, Norway, Portugal, Spain, Sweden*
- D J Reid — *Deputy Head, Overseas banks, Rest of world*
  - R E P Diggory — *Manager, Group 15, Japan*
  - J A Hoskins — *Manager, Group 16, Afghanistan, Australasia, Eastern Europe, Indian sub-Continent, Israel, South Africa*
  - P L Fox — *Manager, Group 17, Cyprus, Middle East, Turkey*
  - M J Fuggle — *Manager, Group 18, Bermuda, Caribbean, Far East, Latin America, Other Africa*
  - C M D Bird (b) — *Manager, Administration, Staff training*
  - P J Marr — *Manager, Review team visits*
  - R J MacDonald, D A Ware — *Managers, Technical Assistance*

(a) J Bulloch takes over from J C Cleland on 16 May.
(b) E M Ainley takes over from C M D Bird later in the year.

Appendix 2

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
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
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
Large exposures in relation to mergers and acquisitions (BSD/1986/1)	February 1986
Subordinated loan capital (BSD/1986/2)	March 1986
Statistical notice to monetary sector institutions	June 1986
Guidance note on reporting accountants' reports on Bank of England returns used for prudential purposes (BSD/1987/3)	October 1987
Large underwriting exposures (BSD/1987/1.1) (to be read in conjunction with the large exposures paper)	February 1988
Advertising for deposits (BSD/1988/1)	April 1988
Supervisory treatment of ECU Treasury bills (BSD/1988/2)	October 1988
Letter to authorised institutions concerning money laundering	January 1989
Loan transfers and securitisation (BSD/1989/1)	February 1989
Further letter to authorised institutions concerning money laundering	November 1989
Letter to authorised institutions concerning advertising of interest bearing accounts	December 1990
Letter to authorised institutions concerning guidance notes issued by the Joint Money Laundering Working Group	December 1990
Code of conduct for the advertising of savings and deposit accounts and money-market accounts	December 1990

Implementation in the United Kingdom of the directive on own funds of credit institutions (BSD/1990/2)	December 1990
Implementation in the United Kingdom of the solvency ratio directive (BSD/1990/3)	December 1990
Statistical notice to reporting banks on capital adequacy treatment of deferred tax assets	December 1990
Implementation in the United Kingdom of the directive on own funds of credit institutions (BSD/1992/1) (amendment to the 1990 paper)	January 1992
Loan transfers and securitisation (BSD/1992/3) (amendment to the 1989 paper)	April 1992
Verification of interim profits in the context of the own funds directive (BSD/1992/5)	August 1992
Implementation in the United Kingdom of the solvency ratio directive (BSD/1992/6) (amendment to the 1990 paper)	November 1992
Letter to authorised institutions concerning debt provisioning (the new matrix)	February 1993
Implementation in the United Kingdom of the directive on the consolidated supervision of credit institutions (BSD/1993/1)	March 1993
Statements of Principles (Banking Act 1987 Section 16; The Banking Co-ordination (Second Council Directive) Regulations 1992)	May 1993
Implementation in the United Kingdom of the directive on the monitoring and control of large exposures of credit institutions (BSD/1993/2)	October 1993
Letter to authorised institutions concerning revised editions of the guidance notes issued by the Joint Money Laundering Steering Group	October 1993
On-balance-sheet netting and cash collateral (BSD/1993/3)	December 1993
The Bank of England's relationship with auditors and reporting accountants (BSD/1994/1)	March 1994
Guidance note on reporting accountants' reports on accounting and other records and internal control systems (BSD/1994/2)	March 1994
Subordinated loan capital (BSD/1994/3)	May 1994

Geographical representation of overseas institutions

The following table shows the geographical origins and status of foreign institutions represented in the United Kingdom at end-February 1994.

Geographical origin of ownership	Branch of an overseas bank(1)	UK incorporated subsidiary of an overseas Bank(1)	UK incorporated subsidiary of an overseas Non-Bank	Controlling (15% or more) stake in a consortium bank	Representative offices(2)	Total
Afghanistan	—	1	—	—	—	1
Argentina	1	—	—	—	1	2
Australia	7	5	—	—	1	13
Austria	4	—	—	—	1	5
Bahamas	—	—	—	—	2	2
Bahrain	2	1	—	—	2	5
Bangladesh	1	—	—	—	1	2
Belgium	6	—	—	—	—	6
Bermuda	1	—	—	—	1	2
Brazil	4	—	—	—	5	9
Bulgaria	—	—	—	—	1	1
Canada	6	5	—	—	—	11
China	1	—	—	—	4	5
Croatia	—	—	—	—	1	1
Cuba	—	1	—	—	—	1
Cyprus	2	2	—	—	—	4
Czech Republic	1	—	—	—	2	3
Denmark	4	1	—	—	—	5
Ecuador	—	—	—	—	2	2
Egypt	1	1	—	—	—	2
Finland	3	1	—	—	2	6
France	14	6	1	—	7	28
Germany	16	1	—	—	3	20
Ghana	1	—	—	—	—	1
Greece	3	—	—	—	2	5
Hong Kong	4	3	—	—	1	8
Hungary	—	1	—	—	—	1
India	6	1	—	—	—	7
Indonesia	2	—	—	—	3	5
Iran	5	—	—	1	—	6
Iraq	1	—	—	—	—	1
Ireland	9	2	—	—	2	13
Israel	2	2	—	—	3	7
Italy	15	1	—	—	27	43
Jamaica	—	—	—	—	2	2
Japan	28	6	4	—	15	53
Jordan	1	—	—	1	—	2
Kenya	—	—	—	—	1	1
Kuwait	—	1	—	1	5	7
Lebanon	1	—	—	—	2	3
Libya	—	—	—	1	—	1
Luxembourg	1	—	—	—	2	3
Former Yugoslav Republic of Macedonia	—	—	—	—	1	1
Malaysia	2	—	—	—	2	4
Mexico	4	—	—	1	3	8
Montenegro	—	—	—	—	1	1
Netherlands	6	—	—	—	1	7
New Zealand	1	—	—	—	1	2
Nigeria	2	—	—	—	4	6
Norway	2	—	—	—	—	2
Pakistan	4	—	—	—	1	5
Panama	—	—	—	—	2	2

Geographical origin of ownership	Branch of an overseas bank(1)	UK incorporated subsidiary of an overseas Bank(1)	Non-Bank	Controlling (15% or more) stake in a consortium bank	Representative offices(2)	Total
Philippines	1	1	—	—	1	3
Poland	1	—	—	—	—	1
Portugal	4	—	—	—	1	5
Qatar	1	—	—	—	—	1
Romania	—	—	—	1	—	1
Russia	—	1	—	—	2	3
Saudi Arabia	3	2	—	1	3	9
Serbia	—	—	—	1	3	4
Singapore	4	—	—	—	—	4
Slovenia	—	—	—	—	2	2
South Africa	3	3	—	—	2	8
South Korea	7	3	—	—	8	18
Spain	7	1	—	—	6	14
Sri Lanka	1	—	—	—	—	1
Sweden	5	1	—	—	—	6
Switzerland	9	1	—	—	14	24
Taiwan	2	—	—	—	3	5
Thailand	3	—	—	—	1	4
Turkey	2	1	—	—	5	8
Uganda	—	—	—	—	1	1
UAE	4	—	—	—	—	4
USA	24	11	4	3	9	51
Venezuela	—	—	—	—	2	2
Zambia	1	—	—	—	—	1
Totals	**256**	**67**	**9**	**11** (3)	**180**	**523** (4)
of which						
EEA countries (5)	99	14	1	—	54	168
Other Europe	15	6	—	2	32	55
North America	30	16	4	3	9	62
Japan	28	6	4	—	15	53
Australia & New Zealand	8	5	—	—	2	15
Other Asia	38	9	—	—	25	72
Middle East	21	7	—	5	15	48
Other	17	4	—	1	28	50

(1) Includes institutions authorised to conduct banking business in the country of origin.
(2) This covers only those representative offices included in the list published at the end of January 1994.
(3) Representing 8 institutions.
(4) Representing 520 institutions.
(5) Other than the United Kingdom.

List of institutions authorised at 28 February 1994

Appendix 4

This list is made available pursuant to section 17 (2) of the Banking Act 1987 as amended by The Banking Co-ordination (Second Council Directive) Regulations. The inclusion of an institution does not mean that the Bank of England in any way guarantees its obligations. The list includes institutions authorised by the Bank of England under the Banking Act 1987 and European authorised institutions.

(i) Institutions authorised by the Bank of England

The following institutions are authorised by the Bank of England under the Banking Act 1987 to accept deposits in the UK. Qualifying sterling deposits made with the UK offices of these institutions are covered by the UK's Deposit Protection Scheme.

1 UK-incorporated [1]

ABC International Bank plc
ANZ Grindlays Bank plc
AY Bank Ltd[2]
Abbey National plc
Abbey National Treasury Services plc
Adam & Company plc
Afghan National Credit & Finance Ltd
Airdrie Savings Bank
Aitken Hume Bank plc
Alexanders Discount plc
Alliance Trust (Finance) Ltd
Allied Bank Philippines (UK) plc
Allied Trust Bank Ltd
Anglo-Romanian Bank Ltd[2]
Henry Ansbacher & Co Ltd
Assemblies of God Property Trust
Associates Capital Corporation Ltd
Avco Trust plc

Bank Leumi (UK) plc
Bank of America International Ltd
Bank of Boston Ltd
Bank of Cyprus (London) Ltd
Bank of Montreal Europe Ltd
Bank of Scotland
Bank of Scotland Treasury Services plc
Bank of Tokyo International Ltd
Bank of Wales plc
Bankers Trust International plc
Banque Nationale de Paris plc
The Baptist Union Corporation Ltd
Barclays Bank plc
Barclays de Zoete Wedd Ltd
Barclays Bank Trust Company Ltd
Baring Brothers & Co Ltd
Belmont Bank Ltd
Beneficial Bank plc
British & Commonwealth Merchant Bank plc (in administration)
The British Bank of the Middle East
The British Linen Bank Ltd
British Railways Savings Company Ltd
Brown, Shipley & Co Ltd

CIBC Bank plc
CLF Municipal Bank plc
Caledonian Bank plc
Cater Allen Ltd
Central Hispano Bank (UK) Ltd
The Charities Aid Foundation Money Management Company Ltd
Chartered Trust plc
Charterhouse Bank Ltd
Chase Investment Bank Ltd
Chemical Investment Bank Ltd
Chesterfield Street Trust Ltd
Citibank International plc
City Merchants Bank Ltd
City Trust Ltd
Clive Discount Company Ltd
Close Brothers Ltd
Clydesdale Bank plc
Commercial Bank Trust plc
Commercial Bank of London plc
Confederation Bank Ltd
Consolidated Credits Bank Ltd
The Co-operative Bank plc
County NatWest Ltd
Coutts & Co
Credit Suisse Financial Products

Daiwa Europe Bank plc
Dalbeattie Finance Co Ltd
Dao Heng Bank (London) plc
Davenham Trust plc
The Dorset, Somerset & Wilts Investment Society Ltd
Dryfield Finance Ltd
Dunbar Bank plc
Duncan Lawrie Ltd

Eccles Savings and Loans Ltd
Exeter Bank Ltd

FIBI Bank (UK) plc
Fairmount Trust Ltd
FennoScandia Bank Ltd
Financial & General Bank plc
James Finlay Bank Ltd
First National Bank plc
First National Commercial Bank plc
The First Personal Bank plc
First Trust Bank (AIB Group Northern Ireland plc)
Robert Fleming & Co Ltd
Ford Credit Europe plc
Foreign & Colonial Management Ltd
Forward Trust Ltd
Forward Trust Personal Finance Ltd
Frizzell Banking Services Ltd

Gartmore Money Management Ltd
Gerrard & National Ltd
Girobank plc
Goldman Sachs Ltd
Granville Trust Ltd
Gresham Trust plc
Guinness Mahon & Co Ltd

HFC Bank plc
HSBC Investment Banking Ltd
Habibsons Bank Ltd
Hambros Bank Ltd
Hampshire Trust plc
The Hardware Federation Finance Co Ltd
Harrods Bank Ltd
Harton Securities Ltd

(1) Including partnerships formed under the law of any part of the United Kingdom.
(2) Consortium banks.

Havana International Bank Ltd
The Heritable & General Investment Bank Ltd
Hill Samuel Bank Ltd
C Hoare & Co
Julian Hodge Bank Ltd
Humberclyde Finance Group Ltd
Hungarian International Bank Ltd

3i plc
3i Group plc
IBJ International plc
International Mexican Bank Ltd[(2)]
Iran Overseas Investment Bank Ltd[(2)]
Italian International Bank plc

Jordan International Bank plc [(2)]
Leopold Joseph & Sons Ltd

KDB Bank (UK) Ltd
KEXIM Bank (UK) Ltd
King & Shaxson Ltd
Kleinwort Benson Ltd
Kleinwort Benson Investment Management Ltd
Korea Long Term Credit Bank International Ltd

LTCB International Ltd
Lazard Brothers & Co Ltd
Lloyds Bank plc
Lloyds Bank (BLSA) Ltd
Lloyds Bowmaker Ltd
Lloyds Private Banking Ltd
Lombard Bank Ltd
Lombard & Ulster Ltd
Lombard North Central plc
London Scottish Bank plc
London Trust Bank plc
Lordsvale Finance plc

MBNA International Bank Ltd
McNeill Pearson Ltd
W M Mann & Co (Investments) Ltd
Marks and Spencer Financial Services Ltd
Matheson Bank Ltd
Matlock Bank Ltd
Meghraj Bank Ltd
Mellon Europe Ltd
Mercury Provident plc
Merrill Lynch International Bank Ltd
The Methodist Chapel Aid Association Ltd
Midland Bank plc
Midland Bank Trust Company Ltd
Minories Finance Ltd
Minster Trust Ltd
Samuel Montagu & Co Ltd
Morgan Grenfell & Co Ltd
Moscow Narodny Bank Ltd
Mount Banking Corporation Ltd (in administration)
Mutual Trust & Savings Ltd

NIIB Group Ltd
NWS Bank plc
National Bank of Egypt International Ltd
National Bank of Kuwait (International) plc
The National Mortgage Bank plc
National Westminster Bank plc
NationsBank Europe Ltd
The Nikko Bank (UK) plc
Noble Grossart Ltd
Nomura Bank International plc
Northern Bank Ltd
Northern Bank Executor & Trustee Company Ltd
Nykredit Mortgage Bank plc

Omega Trust Co Ltd

PaineWebber International Bank Ltd
Peoples Bank plc
Pointon York Ltd
The Private Bank & Trust Company Ltd
Provincial Bank plc

Ralli Investment Company Ltd
R Raphael & Sons plc
Rathbone Bros & Co Ltd
Rea Brothers Ltd
Reliance Bank Ltd
Republic Mase Bank Ltd
Riggs A P Bank Ltd
Riyad Bank Europe Ltd
N M Rothschild & Sons Ltd
Royal Bank of Canada Europe Ltd
The Royal Bank of Scotland plc
RoyScot Trust plc

SBI European Bank Ltd
Sabanci Bank plc
Sanwa International plc
Saudi American Bank (UK) Ltd
Saudi International Bank (Al-Bank Al-Saudi Al-Alami Ltd)[(2)]
Schroder Leasing Ltd
J Henry Schroder Wagg & Co Ltd
Scotiabank (UK) Ltd
Scottish Amicable Money Managers Ltd
Seccombe Marshall & Campion plc
Secure Homes Ltd
Singer & Friedlander Ltd
Smith & Williamson Securities
Southsea Mortgage & Investment Co Ltd
Standard Bank London Ltd
Standard Chartered Bank
Svenska International plc

TSB Bank plc
TSB Bank Scotland plc
Tokai Bank Europe Ltd
Toronto Dominion Bank Europe Ltd
Turkish Bank (UK) Ltd
Tyndall Bank plc

UBAF Bank Ltd[(2)]
UCB Bank plc
ULC Trust Ltd
Ulster Bank Ltd
Union Discount Company Ltd
The United Bank of Kuwait plc[(2)]
United Dominions Trust Ltd
Unity Trust Bank plc

Wagon Finance Ltd
S G Warburg & Co Ltd
Wesleyan Savings Bank Ltd
West Merchant Bank Ltd
Western Trust & Savings Ltd
Whiteaway Laidlaw Bank Ltd
Wimbledon & South West Finance plc (in administration)
Wintrust Securities Ltd
Woodchester Credit Lyonnais plc

Yamaichi Bank (UK) plc
Yorkshire Bank plc

2 Incorporated outside the European Economic Area

ABSA Bank Ltd
Allied Bank of Pakistan Ltd
American Express Bank Ltd(3)
Arab African International Bank
Arab Bank plc
Arab Banking Corporation BSC
Arab National Bank
The Asahi Bank, Ltd(3)
The Ashikaga Bank Ltd(3)
Australia & New Zealand Banking Group Ltd(3)

BSI-Banca della Svizzera Italiana(3)
Banca Serfin SA
Banco de la Nación Argentina
Banco do Brasil SA
Banco do Estado de São Paulo SA
Banco Mercantil de São Paulo SA
Banco Nacional de Mexico SNC
Banco Real SA
Bancomer SA
Bangkok Bank Public Company Ltd
Bank Julius Baer & Co Ltd(3)
Bank Bumiputra Malaysia Berhad
PT Bank Ekspor Impor Indonesia (Persero)
Bank Handlowy w Warszawie SA
Bank Hapoalim BM
Bank Mellat
Bank Melli Iran
PT Bank Negara Indonesia (Persero)
Bank of America NT & SA(3)
Bank of Baroda
The Bank of NT Butterfield & Son Ltd
Bank of Ceylon
Bank of China
The Bank of East Asia Ltd
The Bank of Fukuoka Ltd(3)
Bank of India
Bank of Montreal(3)
The Bank of New York(3)
Bank of New Zealand(3)
The Bank of Nova Scotia(3)
Bank of Seoul
The Bank of Tokyo, Ltd(3)
The Bank of Yokohama, Ltd(3)
Bank Saderat Iran
Bank Sepah-Iran
Bank Tejarat
Bank von Ernst & Co Ltd(3)
Bankers Trust Company(3)
Beirut Riyad Bank SAL
Boston Safe Deposit and Trust Company(3)

Canadian Imperial Bank of Commerce(3)
Canara Bank
Chang Hwa Commercial Bank Ltd
The Chase Manhattan Bank, NA(3)
Chemical Bank(3)
The Chiba Bank Ltd(3)
Cho Hung Bank
The Chuo Trust & Banking Co, Ltd(3)
Citibank NA(3)
Commercial Bank of Korea Ltd
Commonwealth Bank of Australia(3)
Continental Bank, National Association(3)
CoreStates Bank NA(3)
Crédit Suisse(3)
Cyprus Credit Bank Ltd
The Cyprus Popular Bank Ltd

The Dai-Ichi Kangyo Bank, Ltd(3)
The Daiwa Bank, Ltd(3)
The Development Bank of Singapore Ltd
Discount Bank and Trust Company(3)

Emirates Bank International Ltd

First Bank of Nigeria plc
First Commercial Bank
First Fidelity Bank NA Pennsylvania(3)
The First National Bank of Boston(3)
The First National Bank of Chicago(3)
Fleet Bank of Massachusetts, NA(3)
French Bank of Southern Africa Ltd
The Fuji Bank, Ltd(3)

Ghana Commercial Bank
Gulf International Bank BSC

Habib Bank AG Zurich(3)
Habib Bank Ltd
Hanil Bank
Harris Trust and Savings Bank(3)
The Hiroshima Bank, Ltd(3)
The Hokkaido Takushoku Bank, Ltd(3)
The Hokuriku Bank Ltd(3)
The Hongkong and Shanghai Banking Corporation Ltd

The Industrial Bank of Japan, Ltd(3)

The Joyo Bank Ltd(3)

Korea Exchange Bank
Korea First Bank

The Long-Term Credit Bank of Japan, Ltd (3)

Malayan Banking Berhad
MashreqBank PSC
Mellon Bank, NA(3)
Merchants National Bank & Trust Company of Indianapolis (National City Bank, Indiana)(3)
The Mitsubishi Bank, Ltd(3)
The Mitsubishi Trust and Banking Corporation(3)
The Mitsui Trust & Banking Co Ltd(3)
Morgan Guaranty Trust Company of New York(3)
Multibanco Comermex SA

NBD Bank, NA(3)
National Australia Bank Ltd(3)
National Bank of Abu Dhabi
National Bank of Canada(3)
The National Bank of Dubai Ltd
National Bank of Pakistan
NationsBank of North Carolina, NA(3)
Nedcor Bank Ltd
The Nippon Credit Bank, Ltd(3)
The Norinchukin Bank(3)
The Northern Trust Company(3)

Oversea-Chinese Banking Corporation Ltd
Overseas Trust Bank Ltd
Overseas Union Bank Ltd

Philippine National Bank

Qatar National Bank SAQ

R&I Bank of Western Australia Ltd(3)
Rafidain Bank (provisional liquidator appointed)
Republic National Bank of New York(3)
The Riggs National Bank of Washington, DC(3)

(3) Non-EEA OECD institutions.

Riyad Bank
Royal Bank of Canada[3]

The Sakura Bank, Ltd[3]
The Sanwa Bank, Ltd[3]
Saudi American Bank
Shanghai Commercial Bank Ltd
Shinhan Bank
The Siam Commercial Bank Public Company Ltd
Sonali Bank
State Bank of India
State Bank of New South Wales Ltd[3]
State Bank of South Australia[3]
State Street Bank and Trust Company[3]
The Sumitomo Bank, Ltd[3]
The Sumitomo Trust & Banking Co Ltd[3]
Swiss Bank Corporation[3]
Syndicate Bank

TC Ziraat Bankasi[3]
The Thai Farmers Bank Public Company Ltd
The Tokai Bank, Ltd[3]

The Toronto-Dominion Bank[3]
The Toyo Trust & Banking Company, Ltd[3]
Türkiye Iş Bankasi AŞ[3]

Uco Bank
Union Bancaire Privée, CBI-TDB[3]
Union Bank of Nigeria plc
Union Bank of Switzerland[3]
United Bank Ltd
United Mizrahi Bank Ltd
United Overseas Bank Ltd[3]

Westpac Banking Corporation[3]

The Yasuda Trust & Banking Co, Ltd[3]

Zambia National Commercial Bank Ltd
Zivnostenská Banka AS

(ii) European authorised institutions

1 European authorised institutions entitled to establish UK branches for the purpose of accepting deposits in the United Kingdom

Name of institution	Country of home state supervisory authority
ABN AMRO Bank NV	Netherlands
AIB Capital Markets plc	Republic of Ireland
AIB Finance Ltd	Republic of Ireland
ASLK-CGER Bank NV-SA	Belgium
Allied Irish Banks plc	Republic of Ireland
Anglo Irish Bank Corporation plc	Republic of Ireland
BfG Bank AG	Germany
Banca Cassa di Risparmio di Torino SpA	Italy
Banca Commerciale Italiana	Italy
Banca di Roma SpA	Italy
Banca Nazionale dell'Agricoltura SpA	Italy
Banca Nazionale del Lavoro SpA	Italy
Banca Popolare di Milano	Italy
Banca Popolare di Novara	Italy
Banco Ambrosiano Veneto SpA	Italy
Banco Bilbao-Vizcaya	Spain
Banco Central Hispanoamericano SA	Spain
Banco de Sabadell	Spain
Banco di Napoli SpA	Italy
Banco di Sicilia SpA	Italy
Banco Español de Crédito SA	Spain
Banco Espirito Santo e Comercial de Lisboa	Portugal
Banco Exterior de España SA	Spain
Banco Nacional Ultramarino SA	Portugal
Banco Portugês do Atlântico	Portugal
Banco Santander	Spain
Banco Totta & Açores SA	Portugal
Bank Austria AG	Austria
Bank Brussels Lambert	Belgium
The Bank of Ireland	Republic of Ireland
Banque Arabe et Internationale d'Investissement	France
Banque Banorabe	France
Banque Française de l'Orient	France
Banque Française du Commerce Extérieur	France
Banque Indosuez	France
Banque Internationale à Luxembourg SA	Luxembourg
Banque Nationale de Paris	France
Banque Paribas	France
Bayerische Hypotheken-und Wechsel-Bank AG	Germany
Bayerische Landesbank Girozentrale	Germany
Bayerische Vereinsbank AG	Germany
Belgolaise SA	Belgium
Berliner Bank AG	Germany

Berliner Handels-und Frankfurter Bank	Germany
Byblos Bank Belgium SA	Belguim
CARIPLO - Cassa di Risparmio delle Provincie Lombarde SpA	Italy
Caisse Nationale de Crédit Agricole	France
Cassa di Risparmio di Verona Vicenza Belluno e Ancona SpA	Italy
Christiania Bank og Kreditkasse	Norway
Commerzbank AG	Germany
Compagnie Financière de CIC et de l'Union Européenne	France
Confederacion Espanola de Cajas de Ahorros	Spain
Crédit Commercial de France	France
Crédit du Nord	France
Crédit Lyonnais	France
Crédit Lyonnais Bank Nederland NV	Netherlands
Creditanstalt - Bankverein	Austria
Credito Italiano	Italy
Den Danske Bank Aktieselskab	Denmark
Den norske Bank A/S	Norway
Deutsche Bank AG	Germany
Deutsche Genossenschaftsbank	Germany
Dresdner Bank AG	Germany
Ergobank SA	Greece
First National Building Society	Republic of Ireland
Generale Bank	Belgium
GiroCredit Bank Aktiengesellschaft der Sparkassen	Austria
Gota Bank	Sweden
Hamburgische Landesbank Girozentrale	Germany
ICS Building Society	Republic of Ireland
Internationale Nederlanden Bank NV	Netherlands
Ionian and Popular Bank of Greece SA	Greece
Irish Permanent Building Society	Republic of Ireland
Istituto Bancario San Paolo di Torino SpA	Italy
Jyske Bank	Denmark
Kansallis-Osake-Pankki	Finland
Kas-Associatie NV	Netherlands
Kredietbank NV	Belgium
Landesbank Berlin Girozentrale	Germany
Landesbank Hessen-Thüringen Girozentrale	Germany
MeesPierson NV	Netherlands
Monte dei Paschi di Siena	Italy
National Bank of Greece SA	Greece
Nordbanken	Sweden
Norddeutsche Landesbank Girozentrale	Germany
Postipankki Ltd	Finland
Rabobank Nederland (Coöperatieve Centrale Raiffeisen-Boerenleenbank BA)	Netherlands
Raiffeisen Zentralbank Osterreich AG	Austria
Skandinaviska Enskilda Banken	Sweden
Société Générale	France
Südwestdeutsche Landesbank Girozentrale	Germany
Svenska Handelsbanken	Sweden
SwedBank	Sweden
Ulster Investment Bank Ltd	Republic of Ireland
Unibank A/S	Denmark
Union Bank of Finland Ltd	Finland
Westdeutsche Landesbank Girozentrale	Germany

2 European authorised institutions entitled to accept deposits in the United Kingdom which are not covered by the UK deposit protection scheme

A European authorised institution may be entitled to accept deposits in the United Kingdom without establishing a branch in the United Kingdom (ie by the provision of services on a cross border basis). These deposits are not covered by the UK Deposit Protection Scheme. Where an institution's name appears in both sections 1 and 2 of this list this is because it is entitled to accept deposits in the United Kingdom both by establishing a branch and by accepting deposits on a cross border basis. Only qualifying sterling deposits made with the UK offices of these institutions are covered by the UK Deposit Protection Scheme.

Name of institution	Country of home state supervisory authority
BNP Finance	France
Banco Borges & Irmão SA	Portugal
Banco Chemical (Portugal) SA	Portugal
Banque Arabe et Internationale d'Investissement	France
Banque de Bretagne	France
Banque de la Cité	France
Banque et Caisse d'Epargne de l'Etat	Luxembourg
Banque Nationale de Paris	France
Banque Nationale de Paris Guyane	France
Banque Nationale de Paris Intercontinentale	France
Banque pour l'Expansion Industrielle	France
Banque Scalbert Dupont	France
Caja de Ahorros de Galicia	Spain
Chang Hwa Commercial Bank (Europe) NV	Netherlands
Chiao Tung Bank Europe NV	Netherlands
Compagnie du Crédit Universel	France
Compagnie Financière de CIC et de L'Union Européenne	France
Crédit Universel	France
DePfa-Bank Europe plc	Republic of Ireland
Deutsche Hypothekenbank AG	Germany
Internationale Nederlanden Bank NV	Netherlands
Irish Permanent Building Society	Republic of Ireland
SNVB Financements	France
Société Nancienne Varin-Bernier	France
Sparekassen Bikuben A/S *	Denmark
Sydbank Luxembourg SA	Luxembourg

* This institution has also established a branch in the United Kingdom entitled to provide certain listed activities which do not, however, include the acceptance of deposits in the United Kingdom.

3 European authorised institutions which are not entitled to accept deposits in the United Kingdom

The following European authorised institutions are entitled to carry on in the United Kingdom by the provision of services certain listed[1] activities other than the acceptance of deposits:

(a) European authorised institutions entitled to establish a branch in the United Kingdom

Name of institution	Country of home state supervisory authority
Crédit Agricole Futures	France

(b) European authorised institutions not entitled to establish a branch in the United Kingdom

Name of institution	Country of home state supervisory authority
Caja Bilbao Bizkaia Kutxa	Spain
Crédit Européen SA	Luxembourg
Deutsche Hypothekenbank Frankfurt AG	Germany
Europäische Hypothekenbank SA	Luxembourg
Frankfurter Hypothekenbank AG	Germany
Hypothekenbank in Hamburg AG	Germany

(1) Ie one or more of the activities listed in Schedule 1 to The Banking Coordination (Second Council Directive) Regulations 1992.

Irish Nationwide Building Society	Republic of Ireland
Realkredit Danmark A/S	Denmark
Rheinboden Hypothekenbank AG	Germany
Rheinische Hypothekenbank AG	Germany

Changes to the list of institutions

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

(i) Institutions authorised by the Bank of England

1 UK-incorporated

Additions

MBNA International Bank Ltd
Wesleyan Savings Bank Ltd

Deletions

Albaraka International Bank Ltd
BNL Investment Bank plc
The Bank of Edinburgh plc
Bunge Finance Ltd
Citibank Trust Ltd
Clydesdale Bank Finance Corporation Ltd
Combined Capital Ltd
Darlington Merchant Credits Ltd
Den norske Bank plc
Enskilda Securities-Skandinaviska Enskilda Ltd
Equatorial Bank plc (in administration)
Family Finance Ltd
Greyhound Bank plc
Holdenhurst Securities plc
LMB Services Ltd
McDonnell Douglas Bank Ltd
Manchester Exchange and Investment Bank Ltd
Roxburghe Bank Ltd (in administration)
Royal Trust Bank
Security Pacific Trust Ltd
Société Générale Merchant Bank plc
Standard Chartered Bank Africa plc
Unibank plc

Name Changes

Ak International Bank Ltd to Sabanci Bank plc
Chartered WestLB Ltd to West Merchant Bank Ltd
Citicorp Investment Bank Ltd to Citibank International plc
FIBI Bank (UK) Ltd to FIBI Bank (UK) plc
Ford Credit plc to Ford Credit Europe plc
HongkongBank London Ltd to HSBC Investment Banking Ltd
Lloyds Merchant Bank Ltd to LMB Services Ltd
Mase Westpac Ltd to Republic Mase Bank Ltd
Peoples Bank Ltd to Peoples Bank plc
Tyndall & Co Ltd to Tyndall Bank plc

2 Incorporated outside the EC (EEA from 1994)

Additions

BSI-Banca della Svizzera Italiana[1]
Bank von Ernst & Co Ltd[2]
Emirates Bank International Ltd

Deletions

BSI-Banca della Svizzera Italiana[1]
First Interstate Bank of California
Middle East Bank Ltd
National Bank of Egypt
National Bank of Kuwait SAK
Reserve Bank of Australia
Wirtschafts- und Privatbank[2]
Swiss Volksbank

Bank Austria AG[3]
Christiania Bank og Kreditkasse[3]
Creditanstalt-Bankverein[3]
Den norske Bank A/S[3]
GiroCredit Bank Aktiengesellschaft der Sparkassen[3]
Gota Bank[3]
Kansallis-Osake-Pankki[3]
Nordbanken[3]
Postipankki Ltd[3]
Raiffeisen Zentralbank Osterreich AG[3]
Skandinaviska Enskilda Banken[3]
Svenska Handelsbanken [3]
Swedbank[3]
Union Bank of Finland Ltd[3]

Name Changes

Bangkok Bank Ltd to Bangkok Bank Public Company Ltd
Bank Ekspor Impor Indonesia to PT Bank Ekspor Impor Indonesia (Persero)
Bank of Oman Ltd to MashreqBank PSC
CBI-TDB Union Bancaire Privée to Union Bancaire Privée, CBI-TDB
Fidelity Bank NA to First Fidelity Bank NA Pennsylvania
The Siam Commercial Bank, Ltd to The Siam Commercial Bank Public Company Ltd
The Thai Farmers Bank Ltd to The Thai Farmers Bank Public Company Ltd
Z-Länderbank Bank Austria AG to Bank Austria AG

(ii) European authorised institutions

1 European authorised institutions entitled to establish UK branches for the purpose of accepting deposits in the United Kingdom

Additions

Name of institution	Country of home state supervisory authority
First National Building Society	Republic of Ireland
ICS Building Society	Republic of Ireland
Ionian and Popular Bank of Greece SA	Greece
Landesbank Berlin Girozentrale	Germany
Unibank A/S	Denmark
Bank Austria AG	Austria[3]
Christiania Bank og Kreditkasse	Norway[3]
Creditanstalt-Bankverein	Austria[3]
Den norske Bank A/S	Norway[3]
GiroCredit Bank Aktiengesellschaft der Sparkassen	Austria[3]
Gota Bank	Sweden[3]
Kansallis-Osake-Pankki	Finland[3]
Nordbanken	Sweden[3]
Postipankki Ltd	Finland[3]
Raiffeisen Zentralbank Osterreich AG	Austria[3]
Skandinaviska Enskilda Banken	Sweden[3]
Svenska Handelsbanken	Sweden[3]
SwedBank	Sweden[3]
Union Bank of Finland Ltd	Finland[3]

(1) Reauthorisation was necessary due to a change in legal entity in Switzerland.
(2) Wirtschafts- und Privatbank acquired Bank von Ernst in April 1993. The two institutions subsequently merged and the name of Bank von Ernst & Co Ltd was retained for the merged entity.
(3) These institutions were authorised under the Banking Act 1987 until the creation of the European Economic Area on 1 January 1994. As from that date they became institutions recognised under the Banking Coordination (Second Council Directive) Regulations 1992.

Deletion

Banque Worms	France

Name Changes

Bank Mees & Hope NV to MeesPierson NV	Netherlands
Banque Bruxelles Lambert SA to Bank Brussels Lambert	Belgium

2 European authorised institutions entitled to accept deposits in the United Kingdom which are not covered by the UK deposit protection scheme

Additions

Name of institution	Country of home state supervisory authority
BNP Finance	France
Banco Borges & Irmão SA	Portugal
Banco Chemical (Portugal) SA	Portugal
Banque Arabe et Internationale d'Investissement	France[4]
Banque de Bretagne	France
Banque de la Cité	France
Banque et Caisse d'Epargne de l'Etat	Luxembourg
Banque Nationale de Paris	France[4]
Banque Nationale de Paris Guyane	France
Banque Nationale de Paris Intercontinentale	France
Banque pour l'Expansion Industrielle	France
Banque Scalbert Dupont	France
Caja de Ahorros de Galicia	Spain
Chang Hwa Commercial Bank (Europe) NV	Netherlands
Chiao Tung Bank Europe NV	Netherlands
Compagnie du Crédit Universel	France
Compagnie Financière de CIC et de l'Union Européenne	France[4]
Crédit Universel	France
DePfa-Bank Europe plc	Republic of Ireland
Deutsche Hypothekenbank AG	Germany
Internationale Nederlanden Bank NV	Netherlands[4]
Irish Permanent Building Society	Republic of Ireland[4]
SNVB Financements	France
Société Nancienne Varin-Bernier	France
Sparekassen Bikuben A/S	Denmark
Sydbank Luxembourg SA	Luxembourg

(4) These banks' names now appear in both sections 1 and 2 of the list because they are entitled to accept deposits in the United Kingdom both through their UK branches and by accepting deposits on a cross border basis. Only qualifying sterling deposits made with the UK branches of these institutions are covered by the UK Deposit Protection Scheme.

3 European authorised institutions which are not entitled to accept deposits in the United Kingdom

(a) European authorised institutions entitled to establish a branch in the the United Kingdom

Addition

Crédit Agricole Futures	France

(b) European authorised institutions not entitled to establish a branch in the United Kingdom

Additions

Caja Bilbao Bizkaia Kutxa	Spain
Crédit Européen SA	Luxembourg
Deutsche Hypothekenbank Frankfurt AG	Germany
Europäische Hypothekenbank SA	Luxembourg
Frankfurter Hypothekenbank AG	Germany
Hypotheken Bank in Hamburg AG	Germany
Irish Nationwide Building Society	Republic of Ireland
Kreditforeningen Danmark	Denmark
Rheinboden Hypothekenbank AG	Germany
Rheinische Hypothekenbank AG	Germany

Name Change

Kreditforeningen Danmark to Realkredit Danmark A/S	Denmark

Annual report by the Board of Banking Supervision

Membership as at 28 February 1994

Chairman:	E A J George	Ex-officio
	R L Pennant-Rea	
	Brian Quinn	
	Jon Foulds	
	P N Gerrard	
	Sir Alan Hardcastle	
	Sir Peter Leslie	
	Lord Swaythling	
	Harry Taylor	

This is the Board's report for the year to 28 February 1994.

Membership

A number of changes in membership took place during the year. On 30 June 1993, the Right Hon. Robin Leigh-Pemberton retired as Governor and ex-officio chairman. Mr Leigh-Pemberton, who had been chairman of the Board since its inception, was replaced by Mr George, who was appointed Governor on 1 July 1993. The Board is indebted to Mr Leigh-Pemberton for his chairmanship over the past six years. Also on 1 July 1993 Mr Pennant-Rea was appointed Deputy Governor of the Bank and an ex-officio member of the Board in place of Mr George. Mr Foulds was appointed to the Board for a five year term from 1 September 1993, to replace Mr Robson, who died in February 1993.

Meetings

The Board met regularly each month during the year, except in June.

At each meeting the Board receives a report on the work of the Banking Supervision Division, setting out matters of general policy and matters relating to specific institutions. Some matters are reported to the Board for information and in some cases the Board's advice is sought on specific issues. In particular, cases in which formal action under the Banking Act might be required are reported to the Board, as are institutions where the Division has concerns or sees potential concerns. The independent members offered advice where they were invited to do so, and at other times where they thought it right to do so.

Matters considered

The Board maintained under review all aspects of the Bank's work relating to its responsibilities under the Banking Act. The Board also kept under review the changes in the Bank's supervisory arrangements which had been made following the publication of the Bingham Inquiry report into the supervision of Bank of Credit and Commerce International SA. The independent members gave advice to the ex-officio members on matters of supervisory policy and on the conduct of individual cases.

There were no instances of disagreement between the ex-officio members and the independent members requiring notification to the Chancellor of the Exchequer pursuant to Section 2(5) of the Banking Act 1987.

The Board was consulted by the Bank in preparing its further evidence which was submitted to the Treasury and Civil Service Select Committee. The Board also considered papers on a wide range of policy matters. These included the Statements of Principles issued consequent upon the implementation of the Banking Co-ordination (Second Council Directive) Regulations

1992, the role of non-executive directors, the Division's approach to the requirement of comfort letters from shareholder/controllers and the Bank's approach to the treatment of complaints against institutions.

The Board also received reports on a range of operational matters. As well as reports on particular institutions where the Division had concerns, the Board reviewed the papers on the impact of the Second Banking Co-ordination Directive on smaller UK-incorporated institutions, and on the Bank's approach to the supervision of branches of overseas banks. The Division's policy towards commissioning reports from reporting accountants and its use of inward secondees to carry out review team visits was also considered. The Board was consulted on the Division's approach to consolidated supervision following the EC Consolidated Supervision Directive.

Regular reports were received from the Special Investigations Unit on its activities. The Board also discussed four papers dealing with specific sectors of the banking industry and continued to review the staffing and information technology arrangements for Banking Supervision Division.

Secretary, by Order of the Board