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PREM 19/2111

CONFIDENTIAL FILE

Takeover Bid for Royal
Bank of Scotland
Bank Takeovers and Mergers

Economic

Policy

APRIL 1981

Referred to	Date	Referred to	Date	Referred to	Date	Referred to	Date
2.7.81							
14.7.81							
17.9.81							
12.10.81							
15.10.81							
23.10.81							
3.11.81							
24.11.81							
15.1.82							
20.1.82							
16.8.82							
6.7.82							

PREM 19/2111



DEPARTMENT OF TRADE AND INDUSTRY
1-19 VICTORIA STREET
LONDON SW1H 0ET

TELEPHONE DIRECT LINE 01-215 5422
SWITCHBOARD 01-215 7877

Secretary of State for Trade and Industry

PS/

**CONFIDENTIAL
MARKET SENSITIVE**

6 July 1987

Alex Allan Esq
Private Secretary to the
Chancellor of the Exchequer
HM Treasury
Parliament Street
LONDON
SW1

Price Rinker²

DWS
6/7. L MT

Dear Alex

MIDLAND BANK

We spoke about the expected announcement (tomorrow) by Midland of the disposal of one of their subsidiaries to the National Australian Bank. I thought it might be helpful to circulate the line we propose to draw on when asked about my Secretary of State's position in this disposal.

This would be as follows:

" This proposal qualifies for investigation under the merger control provisions of the Fair Trading Act 1973. Our policy is to make references primarily on competition grounds. In evaluating the competitive situation in each case, the Secretary of State has regard to the international context - that is, to the extent of competition in the home market from non-UK sources and to the competitive position of UK companies in overseas markets.

Before the Secretary of State takes his decision whether or not to refer he takes advice from the Director General of Fair Trading. The Director General will examine this proposal and advise the Secretary of State in due course. It would not



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be appropriate to prejudge the Director General's advice by commenting further at this point. Any persons who wish to make representations should contact the

Director General of Fair Trading
Office of Fair Trading
Field House
Bream's Buildings
London
EC4A 1PR Tel: 01 242 2858

Clearly not all of this might be needed in answer to every question. My Secretary of State has a quasi judicial role in matters of this kind and I very much hope that statements about this role will be confined to the points in our line to take.

I am copying this to David Norgrove (No 10), Robert Gordon (Scottish Office) and David Watkins (Northern Ireland Office).

Yours

T Walker

TIMOTHY WALKER
Private Secretary

DW1DDB

R 16/8

FROM: F CASSELL

16 August 1983

PRINCIPAL PRIVATE SECRETARY

cc PS/Financial Secretary
PS/Economic Secretary
Mr Middleton o.r.
Mr Monck "
Mr Hall
Mr Pirie or.
Mr Ilett

- Mr Scholar, 10 D St

GRINDLAYS BANK: REARRANGEMENT OF SHAREHOLDINGS

The Bank of England have informed us that a rearrangement of shareholdings in Grindlays Group (under discussion for some time) has been agreed. This will give Citibank effective control of Grindlays Bank. If approved by Grindlays Board, an announcement is likely this afternoon.

Under the present two-tier capital structure 49 per cent of the issued capital of Grindlays Bank is owned by Citibank and 51 per cent by Grindlays Holdings, in which Lloyds Bank has a 40 per cent stake. This structure gives Lloyds - at least in theory - a greater degree of control than Citibank (which has a much bigger financial stake) and has made the strategic direction of the bank unwieldy.

The group has for some time been trying to get a more rational capital structure and to strengthen its management - which, among other things, will need to look afresh at the bank's commitments in Latin America.

Several approaches to other banks have come to nothing. The scheme now agreed is a rather complicated share exchange. It will give Citibank 49 per cent of the share capital of Grindlays Holdings, and reduce Lloyds Bank's share to about 21 per cent. Grindlays Bank will become a wholly owned subsidiary of Grindlays Holdings.

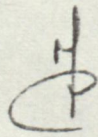
COMMERCIAL IN CONFIDENCE

Citibank will support the development of Grindlays as an independent international bank; it does not intend to treat it as part of Citibank's global banking operations. Lloyds Bank supports the proposals, but in time will probably withdraw altogether from Grindlays.


The announcement - which would say, among other things, that the Bank of England has been consulted and supports the proposals - is likely to attract some press interest. It may be presented as a US bank effectively taking over a British bank; however, since Citibank already has a 49 per cent stake in Grindlays Bank, the change is not a dramatic one - though as noted above it will lead to greater involvement by Citibank in the management of Grindlays.

The press may point to a contrast between the Bank of England's blessing of this change of ownership and its opposition to the HongShai's bid for the Royal Bank of Scotland. The two cases, however, are hardly parallel. The Royal Bank is essentially a retail bank, doing business in the UK; Grindlay's business is almost entirely overseas.

What is clear from the recent history of Grindlays - but cannot be said by us - is that the bank has serious problems and that no other UK bank showed any willingness to sort these out. In the circumstances, Citibank's increased involvement is no doubt the best solution - indeed, it seems to be the only one available.



F CASSELL

file *JH*
Econ Pol

10 DOWNING STREET

please to me
AG 201
THE PRIME MINISTER

20 January 1982

Dear Sir William,

Thank you for your confidential memorandum of 12 January about the MMC report on bids for the Royal Bank of Scotland. As you will by now know, the Commission found against both bids; and the Secretary of State has decided not to allow either bid. I enclose a copy of the press notice setting out his decision.

The Commission's report dealt at some length with a number of issues which you raised in your memorandum; I hope that you will consider that it gave them sympathetic treatment, and that you will find yourself in a substantial measure of agreement with its conclusions.

Yours sincerely,

(sgd)

MT

Sir William Lithgow

SIC

Sir William Lithgow
Telephone Langbank (0475-54) 692
(after hours Langbank 389)
Telex 779801

P.O. Box 2,
Port Glasgow,
Renfrewshire.
PA14 5JH

19th January, 1982.

Miss Caroline Stephens,
Personal Assistant,
No. 10 Downing Street,
London S.W.1.

CFpps

21/1

Dear Miss Stephens,

I confirm that I shall report at No. 10 Downing Street for a meeting at 5.30 p.m. on Monday 25th January.

Yours sincerely
William Lithgow



10 DOWNING STREET

Arranged for
Tuesday 25th
January at 1730
at N.W.10.

No briefing
required —
just a meeting
folder for the
preceding w/e.
cf.

15/1



From the Secretary of State

Michael Scholar Esq
Private Secretary
10 Downing Street
London, SW1

15th January 1982

Dear Michael,

Thank you for your letter of 15 January.

... I enclose a draft reply for the Prime Minister to send to Sir William Lithgow following the announcement of the Government's decision on the proposed takeover of the Royal Bank of Scotland Limited.

Yours Ever,

Jonathan Rees

J N REES
Private Secretary



*Please type for PM
MUS 15/1*

DRAFT REPLY FOR THE PRIME MINISTER TO SEND TO:

Sir William Lithgow Bt CEng FRINA FBIM MInstPL DL LLD
Drums
Langbank
Renfrewshire
SCOTLAND

Thank you for your confidential memorandum of 12 January about the MMC report on bids for the Royal Bank of Scotland. As you will by now know the Commission found against both bids; and the Secretary of State has decided not to allow either bid. I enclose a copy of the press notice setting out his decision.

The Commission's report dealt at some length with a number of issues which you raised in your memorandum; I hope that you will consider that ~~they~~ gave them sympathetic treatment, and that you will find yourself in a substantial measure of agreement with ~~their~~ ^{its} conclusions.



Tyre M
cc I.G.

✓
MAP

MAP

From the Secretary of State

Mike Pattison
Private Secretary
10 Downing Street
London, SW1

15th January 1982

Dear Mike,

... Thank you for your letter of 11 January. As requested, I enclose a draft reply for the Prime Minister to send to Anthony Nelson MP about the take-over bid for the Royal Bank of Scotland Group Ltd.

Yours Ever,

Jonathan Rees

J N Rees
Private Secretary



DRAFT REPLY FOR THE PRIME MINISTER TO SEND TO:

A. Nelson MP
House of Commons
SW1A 0AA

112
Thank you for your letter of 6 January about the Monopolies and Mergers Commission's report on bids for the Royal Bank of Scotland.

As you will now know the report was published on 15 January, when John Biffen announced his decision to accept the Commission's findings against both bids, and not to allow either bid. I enclose a copy of his Department's press notice of 15 January, setting out his decision.

I need hardly say that there is room for more than one point of view on the very difficult issues raised by the two bids; you will have seen that the Commission's group responsible for investigating the bids was itself divided on some of ~~its~~ ~~their~~ conclusions. The Commission's report was however the product of a long and exhaustive investigation of this particular case taking account of a wide spectrum of Scottish opinion as well as of a range of other factors. As a mature and comprehensive examination of the issues it commands respect.

As ⁱⁿ all their investigations, the Commission's findings and recommendations relate to the particular circumstances of the case under examination. I would not wish the decision to endorse the Commission's conclusions in this case to be interpreted as a touchstone for future Government policy towards inward investment in the United Kingdom, or UK financial institutions in general, or towards the acquisition of Scottish assets (whether or not in the financial sector) in particular. Each case will need to be considered on its merits. Your letter raises issues which will remain important matters for discussion in future merger cases affecting Scotland, or indeed the country as a whole. I can assure you that where they arise on future occasions, they will be given the fresh and individual consideration which they received in this case.

cc. MR INGHAM

WFS

Econ. Pol.

RESTRICTED



10 DOWNING STREET

From the Private Secretary

15 January 1982

Royal Bank of Scotland Group:
MMC Report

The Prime Minister was grateful for your Secretary of State's minute of 14 January whose contents she has noted.

I am sending copies of this letter to John Kerr (HM Treasury), Brian Fall (Foreign and Commonwealth Office), Muir Russell (Scottish Office), John Rhodes (Department of Trade) and David Wright (Cabinet Office).

M.C. SCHOLAR

Jonathan Spencer Esq
Department of Industry

RESTRICTED

SW



10 DOWNING STREET

From the Private Secretary

15 January 1982

Dear Jonathan.

Royal Bank of Scotland Group:
MMC Report

The Prime Minister was grateful for your Secretary of State's minute of 14 January, whose contents she has noted.

I am sending copies of this letter to John Kerr (HM Treasury), Brian Fall (Foreign and Commonwealth Office), Muir Russell (Scottish Office), John Rhodes (Department of Trade) and David Wright (Cabinet Office).

Your sincerely,

Michael Scholar

Jonathan Spencer Esq
Department of Industry

JS



10 DOWNING STREET

PRIME MINISTER

The attached letter from
Sir William Lithgow is self-
explanatory.

Would you like to:

1. see him ?

*Yes. When he
is next in London
mf*

2. get Michael Scholar to
draft a reply?

es.

14 January 1982

HL

14 January 1982

I am writing to acknowledge your letter of 12 January. This is receiving attention and a reply will be sent to you as soon as possible.

CAROLINE STEPHENS

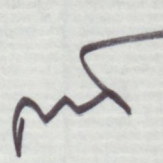
Sir William Lithgow

CS



PRIME MINISTER

Prime Minister



This accords closely
with your own view.

MCS 14/1

I have seen a copy of John Biffen's minute to you of 11 January stating his intention to accept the majority MMC report on the bids for the Royal Bank of Scotland Group. Like John I have reservations about some of the report's arguments and I feel some concern about the wider implications. I accept that there is a case for preserving Scottish control of the RBSG on regional policy grounds but this section of the report presents the arguments in a general and rather uncritical way. It could lead a wide range of companies based in Scotland and perhaps in other regions to feel less vulnerable to takeover and this may not help to stimulate efficiency.

2 There are implications too for inward investment. While the MMC's sensitivity to the question of national control is welcome, the report will unavoidably add to an impression of protectionism in investment matters and do some harm to the climate for both inward and outward investment.

3 Finally rejection of the bids will lose an opportunity to increase competition in retail banking which could have led to an improvement in the provision of financial services to industry.

4 Nevertheless, I share John Biffen's view that these reservations do not justify taking the exceptional step of rejecting the majority recommendations. If this is accepted we



must be particularly sensitive in handling questions about the implications for future foreign bids in general and for clearing banks in particular. It should be made clear that each case is considered on its merits and that there is no implication here of a change in attitude to foreign bids or that the door is closed on all foreign bids in this sector.

5 I am sending copies of this minute to Geoffrey Howe, Peter Carrington, George Younger, John Biffen and Sir Robert Armstrong.

PJ

P J

14 January 1982

Department of Industry



B.T.

①

Prime Minister

I think this has all the right points except that the MMC is there to enhance competition not to limit it. Agree that 14th January 1982 this be added? and that the briefing is otherwise satisfactory?

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From the Secretary of State

MARKET SENSITIVE

Michael Scholar Esq
Private Secretary
10 Downing Street
London, SW1

I will leave it on SFS with M.T.

Dear Michael,

Following my Secretary of State's minute to the Prime Minister of 11 January about the MMC Report on the bids for the Royal Bank of Scotland by the Hong Kong and Shanghai Banking Corporation and Standard Chartered, you said that the Prime Minister had agreed to an announcement on the lines he recommended at 4.30 pm on Friday 15 January.

MS 14/1

- ... I now attach drafts of the Press Release, which the Secretary of State intends to issue tomorrow on publication. He believes that this should be fairly clinical in its approach, and you will see that the attached draft is purely factual. However, there will almost certainly be press requests for fuller
- ... briefing, and I attach a copy of the background brief which is to be used in response to these requests. This will not be published, but will be for the use of Whitehall Press Offices. You will see that any questions on the Report should be directed to the Department of Trade Press Office. The background brief reflects my Secretary of State's view that the MMC Report should not be construed as setting a general policy. Rather any future take-over bids for United Kingdom companies, whether in the banking sector or not, will be treated on their merits at the time.

Clearly if you, or any other interested departments, have comments on the line we propose to take, it would be very helpful to receive them today.

I am copying this to the Private Secretaries of the Chancellor, the Foreign Secretary, Secretary of State for Scotland and the Secretary of State for Industry and to Sir Robert Armstrong.

Yours Sincerely,

Jonathan Rees

J N REES
Private Secretary

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CONFIDENTIAL

MARKET SENSITIVE

BACKGROUND BRIEF

MMC REPORT ON BIDS FOR ROYAL BANK OF SCOTLAND

General

The Department's press release summarises the report and the Secretary of State's decision on it. Any questions on the report should be directed to the Department of Trade Press Office.

The Commission's Decision

All take-over proposals, whether by United Kingdom or overseas companies, involving assets of over £15m are subject to scrutiny under the Fair Trading Act and may be referred to the MMC for investigation. The bids for the Royal Bank of Scotland Group Limited were treated on their merits like any other bids.

Implications for Scotland

The Commission's report drew particular attention to the possibility of either bid having adverse consequences for the Scottish economy and career opportunities in Scotland. As in the case of mergers generally, any future bid for a Scottish, or Scottish based, company would need to be considered on its merits. If such a bid were referred to the Monopolies and Mergers Commission, they would need to consider it on the case by case basis which they invariably follow.

Inward Investment

United Kingdom inward investment policy is liberal and will remain so. All exchange controls have been removed and overseas-owned companies in the United Kingdom are treated in the same way as domestic companies. But this does not detract from the need to examine all aspects of individual take-over proposals in relation to United Kingdom merger policy, just as they are examined in other countries. As far as the banking sector is concerned, the Commission's report points out that the United Kingdom authorities have operated a conspicuously liberal approach towards the influx of overseas-owned banks represented here.

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MARKET SENSITIVE

Implications for bids for other United Kingdom clearing banks

In accepting the report on the Royal Bank, the Secretary of State decided that given the Commission's arguments and conclusions in this case, neither bid should be allowed. The Commission's investigation considered the merits of this particular case; and their conclusions, and the Secretary of State's decision, were reached accordingly. Any other bid for a clearing bank, like any bid, would need to be considered on its merits. In particular the outcome of this case does not imply that all future overseas bids for clearing banks will be turned down whatever the circumstances.

Evidence of the Bank of England

The Bank of England gave evidence in the same way as other interested parties. The Commission reached its conclusions on the basis of its own objective study of the evidence. In any comparable future case the views of the Bank would again be assessed along with all the other relevant factors.

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DRAFT PRESS NOTICE

THE ROYAL BANK OF SCOTLAND GROUP LIMITED/HONGKONG AND SHANGHAI
BANKING CORPORATION/STANDARD CHARTERED BANK LIMITED

REPORT ON THE MONOPOLIES AND MERGERS COMMISSION

The proposed mergers between the Royal Bank of Scotland Group Limited and the Hongkong and Shanghai Banking Corporation and between the Royal Bank of Scotland Group Limited and Standard Chartered Bank would be against the public interest and should not go ahead. These are the conclusions of the Monopolies and Mergers Commission in their report on the proposed mergers, publication of which was announced today by Mr John Biffen, Secretary of State for Trade.

Mr Biffen said: "The Monopolies and Mergers Commission concluded by a majority that both the proposed mergers might be expected to operate against the public interest, and recommended therefore that they should not be allowed.

"In accordance with the advice of the Director General of Fair Trading I am accepting the Commission's majority recommendations and I am requesting the Director General to consult the Hongkong and Shanghai Banking Corporation and Standard Chartered Bank with a view to obtaining undertakings not to proceed with their proposals to acquire the Royal Bank of Scotland Group Limited".

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The Commission concluded by a majority of four to two of the investigatory team that both the proposed mergers would have adverse effects on career prospects, initiative and business enterprise in Scotland which would be damaging to the public interest in the United Kingdom as a whole. The Commission made clear while they saw value in preserving independent local centres of business initiative and opinion it was not their intention to imply that leading Scottish financial institutions in general, or clearing banks in particular, should in no circumstances be taken over by companies based outside Scotland.

In the case of the proposed merger between the Royal Bank of Scotland Group Limited and the Hongkong and Shanghai Banking Corporation, in addition to the effect in Scotland, the Commission concluded by a majority of five to one that the transfer of ultimate control of a significant part of the clearing bank system outside the United Kingdom would have the adverse effect of opening up possibilities of divergence of interest which would not otherwise arise. In reaching this conclusion, the Commission noted that consideration of this question did not in any sense imply hostility to the competition provided by overseas banks in the United Kingdom.

In neither case did the majority foresee benefits which might outweigh the adverse effects identified. Nor could they devise effective safeguards which might prevent the adverse effects. They therefore recommended that neither of the proposed mergers should be allowed.

In a note of dissent, one member of the investigatory group did not accept that the proposed mergers might be expected to have adverse effects on Scotland sufficient to constitute a detriment

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to the public interest in the United Kingdom.

In a separate note of dissent, another member of the group gave less weight to the detriments arising from the effects of both the proposed mergers in Scotland and found no detriment in the proposed transfer of control to a bank based in Hong Kong. He gave greater weight to the potential benefits of the proposed mergers, in particular the promotion of competition in retail banking in the United Kingdom. He therefore concluded that both bids should be allowed to proceed.

Notes for Editors

1 The Secretary of State for Trade referred the proposed mergers between the Royal Bank of Scotland Group Limited and the Hongkong and Shanghai Banking Corporation and between the Royal Bank of Scotland Group Limited and Standard Chartered Bank to the Monopolies and Mergers Commission for investigation and report on 1 May 1981. The Commission was required to report within six months. However, on 8 September 1981 the Secretary of State announced that he was satisfied that there were special reasons why the report could not be made within the time specified in the original reference. Accordingly, he decided to allow a further period to 31 January 1982 for the making of the report, and it was submitted to him on 22 December 1981.

2 Under section 88 of the Fair Trading Act 1973, where a report from the Commission concludes that a merger may be expected to operate against the public interest, the Secretary of State may request the Director General of Fair Trading to consult the relevant parties in order to obtain undertakings with a view to

remedying or preventing the adverse effects specified in the report.

3 Part II of Schedule 3 to the Fair Trading Act 1973 deals with the performance of the functions of the Commission. Paragraph 16 of that Schedule has the effect that a two-thirds majority of an investigatory group finding against a merger is sufficient to enable the Secretary of State to prevent it.

4 Copies of the report (hoc) (ISBN) are available price from HM Stationery Office, 49 High Holborn, London WC1v 6HB and branches, or by post from HMSO, PO Box 569, London SE1.

No - but thanks.

1. Michael - Are you aware of Mike Pattison's actions below?

2. Mike - Are you aware of Michael's request to D/T below?

Kay

13/1/82

Alan

He spoke. The file is now with Mike Schlar.

Kay

14/1



cc: HMT
FCO
SO
IND
CO
hcc: B. Ingham
A. Walters

10 DOWNING STREET

From the Private Secretary

13 January 1982

Royal Bank of Scotland
Monopolies and Mergers Commission Report

As I told you earlier today, the Prime Minister concurs, reluctantly, with the course of action proposed in your Secretary of State's minute of 11 January about the MMC's report on the Royal Bank of Scotland.

The Prime Minister concurs, too, that your Secretary of State's decision should be announced on Friday 15 January. She would be grateful to be consulted about the terms of the announcement, and of the associated press briefing.

I am sending copies of this letter to John Kerr (Chancellor of the Exchequer's Office), Brian Fall (Foreign and Commonwealth Office), Muir Russell (Scottish Office), Jonathan Spencer (Department of Industry) and David Wright (Cabinet Office).

M. C. SCHOLAR

Jonathan Rees, Esq.,
Department of Trade

Prime Minister

(2)

TO: MISS CAROLINE STEPHENS
FROM: SIR WILLIAM LITHGOW

I will put forward a
draft reply when the
announcement is imminent
(planned for Friday 15th)

As advised by telephone, here

MCS 12/1

is the text of a memorandum I have posted
today.

12th January 1982.

CONFIDENTIAL MEMORANDUM

PROPOSED TAKEOVER OF THE ROYAL BANK OF SCOTLAND LIMITED

It is my strong belief as an industrialist, that the concentration of commercial decision-making and wisdom remote from industrial communities over the last 50 years, has been a major factor in our industrial decline. In the Scottish economy, the base of Scottish headquartered activities has to be broadened, not narrowed. Earlier bank rationalisation encouraged by the Bank of England, has made the Royal Bank of Scotland non-expendable, and a successful bid would permanently weaken the highly successful Scottish financial community and encourage further predation. It could only be bad for the chemistry of industrial development. The extension of a branch factory/branch office economy must have serious economic, social and political consequences.

My experience in 20 years as a Bank of Scotland Director, is that a smaller bank can be very effective and agile; the Scottish headquartered banks have been major innovators over these years. I would anticipate continuing and very significant development, particularly because of the new freedoms introduced under the present Government. Sufficient heat has now been generated to ensure new initiatives within the Royal Bank if the bid is dropped. Whilst greater overseas involvement in the London based banking community may not be undesirable, and whilst, as a general principle, I favour a diplomatic climate in which British banks are themselves able to take over banks overseas, in the special circumstances, I believe that this takeover would be contrary to the public interest. I believe that having thought through the implications of such a takeover, informed opinion in Scotland accords with my own.

12th January 1982

FILE

R M

Sir Wm. LITHGLOW

15/1

12 January, 1982

I attach a copy of a memorandum which Sir William Lithgow has addressed to the Prime Minister about the proposed takeover of the Royal Bank of Scotland Limited.

The Prime Minister wishes to reply to this herself. I would be grateful if you could let me have a draft by Friday, 15 January; or by whenever the Government's decision is announced.

M. C. SCHOLAR

J Rees, Esq
Department of Trade

12 January, 1982

I am writing on the Prime Minister's behalf to thank you for your confidential memorandum on the proposed takeover of the Royal Bank of Scotland Limited.

I shall place this before the Prime Minister at the earliest opportunity and a reply will be sent to you as soon as possible.

M. C. SCHOLAR

Sir William Lithgow

(sent to:- P O Box 2,
Port Glasgow
Renfrewshire, PA14 5JH)

Sir William Lithgow
Telephone Langbank (0475-54) 692
(after hours Langbank 389)
Telex 779801

P.O. Box 2,
Port Glasgow,
Renfrewshire.
PA14 5JH

12th January, 1982.

Miss C.M. Stephens,
Prime Minister's Office,
10 Downing Street,
London S.W.1.

Dear Miss Stephens,

In her letter to me of 2nd January, 1981, the Prime Minister suggested that I contacted you with a view to a meeting with her in about six months' time, which would have been last July. In the event, I have not done so because I had felt inadequately briefed to be able to develop new thinking in a satisfactory manner. Although I have been actively concerned with the questions posed by the bids for the Royal Bank of Scotland since their announcement, it was only this morning that I appreciated the probability of a Cabinet decision being involved. Inevitably I am afraid that advice relating to industrial matters also has to relate to the context within which industry functions, and since the Scottish banking community is at a focal point of considerable commercial and intellectual significance in the Scottish economy, I have prepared the enclosed paper, a transcript of which has already been sent to you by messenger.

A year ago, I drafted out some ideas that had been touched on in discussion with the Prime Minister, which related most specifically to economics, finance and taxation. Again, these are areas that are not central to my experience, though in reality, they are the ones in which Government policy can have the most influence on industry. I do not know whether the Prime Minister would like a further meeting now, and whether there are specific points she would wish pursued.

I believe that the combination of Government policies and the world recession has led to a significant improvement in industrial performance. I believe it to be important now that industry should begin to be stretched again to take up slack capacity, force the pace and tempo of production and through improved profit expectations, investment be stimulated, particularly in new technologies. I continue to believe that apart from inflation, the most serious economic problem which must be solved is the correction of the distortions induced by the petro pound. I believe conventional City wisdom is in error in supposing that nothing can be done and that the loss of manufacturing capacity and jobs is the price that has to be paid for North Sea oil.

The continuance of Capital Gains Tax is resulting in increasing frustration/

Miss C.M. Stephens.

12th January, 1982.

frustration of potential investment, particularly in new ventures. The Inland Revenue are already frustrating the declared objectives of this Government's demerger legislation. It should also be possible to roll over Capital Gains liabilities where the proceeds of a realisation are reinvested by an individual in suitable productive businesses, particularly where the individual is actively engaged in them. Companies should have the ability to make a Reverse Rights Issue resulting in the payment of capital sums which would enjoy some rollover options. Generally the balance of tax advantage should move in favour of equity rather than debt funding, individual rather than corporate, or pension fund, investment.

I share the widely held view in industry that both Central and Local Government have a long way to go in the streamlining of administration, the elimination of unnecessary tasks and personnel, and in particular, a logical allocation of resources between capital and revenue.

Clearly, some Ministers have been more effective than others in instilling a more disciplined sense of resource management into their Departments. I am bluntly appalled at some aspects of the working of Departments with which I have first hand experience.

One cannot solve unemployment by seeking to employ the unemployed, rather the economy must grow under the influence of those best able to make it do so. Unfortunately, current rates of unemployment do represent an unacceptably high overhead, particularly in the form of National Insurance Surcharge, and I believe that those at the sharp end of the economy must be relieved of some of this burden if they are to advance as fast as is necessary.

It is my intention to go to Australia for about three weeks on the 22nd of February, otherwise I am available at this place if my presence should be required, or a note on any specific subject.

Yours sincerely

William J. H. J.

12th January, 1982.

CONFIDENTIAL MEMORANDUM.

PROPOSED TAKEOVER OF ROYAL BANK OF SCOTLAND.

It is my strong belief as an Industrialist, that the concentration of commercial decision making and wisdom remote from industrial communities over the last fifty years, has been a major factor in our industrial decline. In the Scottish economy, the base of Scottish headquartered activities has to be broadened, not narrowed. Earlier Bank rationalisation, encouraged by the Bank of England, has made the Royal Bank of Scotland non expendable, and a successful bid would permanently weaken the highly successful Scottish financial community and encourage further predation. It could only be bad for the chemistry of industrial development. The extension of a branch factory/branch office economy must have serious economic, social and political consequences.

My experience in twenty years as a Bank of Scotland Director, is that a smaller Bank can be very effective and agile; the Scottish headquartered Banks have been major innovators over these years. I would anticipate continuing and very significant development, particularly because of the new freedoms introduced under the present Government. Sufficient heat has now been generated to ensure new initiatives within the Royal Bank if the bid is dropped. Whilst greater overseas involvement in the London based banking community may not be undesirable, and whilst, as a general principle, I favour a diplomatic climate in which British Banks are themselves able to take over Banks overseas, in the special circumstances, I believe that this takeover would be contrary to the public interest. I believe that having thought through the implications of such a takeover, informed opinion in Scotland accords with my own.

William Johnston

COVERING CONFIDENTIAL AND MARKET SENSITIVE



DEPARTMENT OF TRADE CTS Division
Sanctuary Buildings 20 Great Smith Street London SW1P 3DB
Telex 8811074 DTHQ G
Telegrams Advantage London SW1
Telephone Direct Line 01-215 3700
Switchboard 01-215 7877

Alan Watkins

As requested

MUS 12/1

TO ALL RECIPIENTS OF
TYPESCRIPT COPIES

Your reference

Our reference

Date

12 January 1982

COPY NOS: *42 & 43*

75/SOS (for No 10 Downing Street)

*Report
attached to
back of file*

MMC REPORT ON PROPOSED MERGER

I attach a typescript copy of the Commission's report on this merger, number above.

We would like to remind all recipients that the contents of the report are confidential and must remain so until the report has been laid before Parliament and published in accordance with section 83 of the Fair Trading Act 1973. This is important not only because of the usual considerations applying to Parliamentary papers, but because of the immediate impact that prior disclosure of the Commission's conclusions on a merger report can have on share prices, and thus on future relations with the Stock Exchange, the parties and the City generally. To guard against the risk of leaks it is therefore important not only to avoid direct disclosure outside Government but to confine disclosure of the findings within Government strictly to those with a "need to know", and to ensure that they too are aware of the need for strict security.

Sam McCant

PS

H P N Steinitz

ENC

COVERING CONFIDENTIAL AND MARKET SENSITIVE



JP

10 DOWNING STREET

From the Private Secretary

11 January 1982

Mr. Anthony Nelson, MP, has copied to your Secretary of State his letter of 11 January to the Prime Minister, about press speculation on the contents of the MMC report on take-over bids for the Royal Bank of Scotland Group. I enclose a further copy for ease of reference.

I should be grateful for a draft reply for the Prime Minister's signature as soon as possible.

B/E

M. A. PATTISON

John Rhodes, Esq.,
Department of Trade.

JP



10 DOWNING STREET

From the Private Secretary

11 January 1982

I am writing on behalf of the Prime Minister to thank you for your letter of 22 January. I will place this before the Prime Minister and a reply will be sent to you as soon as possible.

M. A. PATTISON

Anthony Nelson, Esq., MP.

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MARKET SENSITIVE



PRIME MINISTER

I do not think we can overturn the result although the MMC was not set up to make subjective judgements. The lesson from

Several references to the name is that we must be careful what we refer to them. I

Prime Minister suspected they will fit another bid.
Do you wish

(i) Simply to note Mr Biffen's conclusion
(ii) would you like us to get the report and arrange a meeting with him?

I have received the report by the MMC on the bids for the Royal Bank of Scotland by the Hongkong and Shanghai Banking Corporation and Standard Chartered.

On the face of it the Commission's arguments appear misconceived.

The Commission have concluded by a majority of five to one of the investigatory team against the HSBC bid, and by a majority of four to two against the Standard Chartered bid. These majorities are sufficient to enable me to act to prevent both mergers, by order if the parties are unwilling to give voluntary undertakings not to proceed.

MLs 11/1

Four of the team identify adverse effects flowing from both bids on "career prospects, initiative and business enterprise in Scotland which would be damaging to the public interest of the United Kingdom as a whole". In the case of the HSBC bid, five members cite the additional adverse effect of a possible divergence of interest arising from overseas control of a United Kingdom clearing bank which would be contrary to the public interest. Mr Smethurst, (an economist fellow of Worcester College, Oxford), has entered a note of dissent rejecting both the Scottish argument and, in the circumstances of HSBC, the overseas control argument, and, placing greater weight on the potential benefits of fresh competition from a fifth force in United Kingdom retail banking. The other dissenter (Sir Alan Neale) rejects only the Scottish argument. It is inevitable that a disagreed report of this kind will, when published, give rise to debate, the more so since many of the issues discussed in the report are matters for subjective judgement. To my mind the Commission could have made more of a number of the issues in

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question, particularly those relating to competition in United Kingdom retail banking, which Mr Smethurst highlights in his note of dissent. But I am clear that whatever differences of judgement there may be, they are not sufficient to merit taking the exceptional step of not following the Commission's report. This is also the view of the Director General, who has made a number of criticisms of the report's arguments and conclusions. He has however recommended me to accept the report, and not to allow either merger. This is the course which I propose to follow.

I have discussed the report with the Chancellor of the Exchequer and he too agrees that its recommendations should be followed. This is also the view of the Secretaries of State for Foreign Affairs and for Scotland. I understand that the Bank of England, despite some disappointment that the report does not adopt their point of view on all the issues, would likewise wish its recommendations to be followed.

There is intense speculation about the report and I should like to publish it as soon as practicable, the more so given the report in today's newspapers. I therefore propose to publish at the earliest time which can be managed which is the afternoon of Friday 15 January. I would propose to issue a brief press notice avoiding comment on the merits of the arguments, but accepting the report's conclusions and inviting the Director General to seek appropriate undertakings from the parties not to proceed.

I am copying this minute to Geoffrey Howe, Peter Carrington, George Younger, Patrick Jenkin and Sir Robert Armstrong.

Department of Trade
1 Victoria Street
London, SW1H 0ET

11 January 1982

WJB

WJB

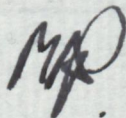
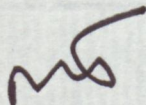
CONFIDENTIAL
MARKET SENSITIVE

PRIME MINISTER

You asked about the handling of the MMC Report on the Royal Bank of Scotland, given the market sensitivity of the issues concerned.

Mr. Biffen has already decided to accelerate the publication timetable. He hopes now that it will be possible to publish about 20 January.

He will be considering the recommendations with officials early next week, and will then write to you and a few selected colleagues. I gather that he would not be surprised if there is a request for a meeting of those colleagues with direct interests.



4 January 1982

CONFIDENTIAL

2

Prime Minister



Econ P57

Mus 3/11

cc Mr. Walters

PRIME MINISTER

BANK TAKEOVERS AND MERGERS

I understand that this topic is to be considered at E Committee on Thursday 5th November. I am sorry that I shall be unable to attend since I am appearing for the Revenue before the House of Lords in an appeal.

My concern is that in paragraph 14 of his Note of 23rd October (E(81)104) the Chancellor of the Exchequer states that he would propose to make it clear that the new powers would not be used to object to either of the present bids for the Royal Bank of Scotland, and that he cannot see how "existing cases could be objected to...without retrospection of an indefensible kind".

The offers from the Standard Chartered Bank and the Hong Kong and Shanghai Banking Corporation each included conditions to the effect that, in the event of a reference being made to the MMC, the offers would lapse. I understand that the offers from both have lapsed. While it is reasonable to assume that, if the MMC does not recommend against either or both situations, new offers will be submitted, the offerers are under no obligation to do so and any new offers could be in quite different terms from the original offers.

Conditions that an offer will lapse on a reference to the MMC are a common feature of such transactions and are designed to ensure that, in the passage of time between a reference to the MMC being made and the Report being published, the offerer is not bound, and if he decides to make a new offer he will be able to take account of any material change in circumstances which may affect his interests. The purpose of such a condition is therefore designed to benefit the offerer. Where the offerer, in his own interests, has decided not to be bound by his offer after the reference, why should HMG bind itself to protect him against the effect of legislation announced while he is not bound and before he has decided whether to put in a new offer at all, and if so, on what terms?

It may be argued that there is some sort of moral or substantive retrospection involved, but in my view that is not the case either. Both Standard Chartered and Hong Kong and Shanghai Banks have now put themselves in a situation where they are not committed in any way to the Royal Bank or its shareholders, and their future actions cannot be taken for granted.

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If the new legislation is to have effect from the date of its announcement, and if that announcement is made before the MMC reports, then in my view to include the Royal Bank situation in that legislation would not involve any retrospection.

I am sending copies of this minute to members of E, the Lord Chancellor, the Lord President of the Council, the Secretary of State for Scotland, the Attorney General, the Paymaster General, the Parliamentary Secretary to the Treasury and Sir Robert Armstrong.

M J C

MACKAY OF CLASHFERN

3rd November 1981

CONFIDENTIAL

for the E folder

Econ Pol



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FROM THE PRIVATE SECRETARY
TO THE SECRETARY OF STATE
FOR WALES

32 OCT 1981

CONFIDENTIAL & COMMERCIAL IN CONFIDENCE

28 October 1981

Dear Mr. Kerr,

BANK TAKEOVERS AND MERGERS

My Secretary of State is accompanying Their Royal Highnesses The Prince and Princess of Wales on their tour of the Principality and will not be available to attend E Committee.

My Secretary of State is of course concerned about the aspects of banking legislation which affect the regions. He had noted with interest that in his minute of 16 September the Chancellor had envisaged the possibility of an amendment to the Banking Act which would deal with the difficulty arising from the appeals against refusal to grant recognised bank status. The Commercial Bank of Wales appeal has not yet been determined: and in any case this will depend upon E Committee's decision on the takeovers and mergers issue. Nevertheless I am sure that my Secretary of State would want me to express the hope that, if there is to be a Bill, the Chancellor will feel able to consider including such a provision in it.

I am sending a copy of this letter to the Private Secretaries to Members of E Committee, the Secretary of State for Scotland and Sir Robert Armstrong.

*Yours sincerely,
Leifur Dan*

PP- MISS G C EVANS
Private Secretary

J O Kerr Esq
Private Secretary to
The Rt Hon Sir Geoffrey Howe QC MP
Chancellor of the Exchequer
HM Treasury
Parliament Street
LONDON

Ref. A05826

PRIME MINISTER

Bank Takeovers and Mergers

E(81) 104 and 105

BACKGROUND

The Chancellor of the Exchequer (E(81) 104) and the Secretary of State for Trade (E(81) 105) agree that there should be legislation in 1981-82 to ensure that the Government has powers to control takeovers of United Kingdom banks, and in particular overseas bids for clearing banks. They differ on the form this legislation should take. Whatever the form, there is at present no place for such a Bill in the 1981-82 programme.

2. For many years the Bank of England have operated a non-statutory control whereby the banking system understand that takeover proposals are not to be pursued without the Bank's consent. By bidding for the Royal Bank of Scotland (RBS) without that consent, the Hong Kong and Shanghai Banking Corporation (HSBC) broke ranks. Their bid has now been referred to the Monopolies and Mergers Commission (MMC), together with a parallel bid by the Standard Chartered Bank. It is hoped that the MMC will report by the end of the year.

3. Whatever the MMC's findings on the present case, the HSBC's action means that the Bank of England's informal arrangements can no longer be relied upon. In paragraph 6 of E(81) 104, the Chancellor of the Exchequer advises that further overseas bids, probably by American banks, for United Kingdom clearing banks are a distinct possibility in the coming months. He wishes to move quickly to stop this loophole by legislation in the 1981-82 Session. In earlier correspondence, the case for early legislation has been supported by the Secretaries of State for Trade, for Industry, and for Scotland and by the Lord Privy Seal.

Alternative Approaches to Legislation

4. The Chancellor of the Exchequer, after consultation with the Governor, proposes new powers to veto changes in control of banks on prudential grounds (competence, probity, financial standing) and for reasons of the public interest more generally, including questions of overseas control. His decision to object



to a takeover under the new powers would be taken after receiving advice from the Bank of England, and he would be obliged by the legislation to exercise his powers and give reasons for his decisions by a Statutory Instrument subject to Negative Resolution. He would wish to announce as soon as convenient the Government's intention to introduce this legislation and to make clear that it would take effect from the date of his announcement. He would then introduce the Bill in the New Year and would want Royal Assent by the summer. It would be short, and relatively easy to draft.

5. The Secretary of State for Trade argues in E(81) 105 that the new powers should be confined to prudential controls. In his judgment it would be very difficult in practice for the Chancellor of the Exchequer to announce that he was rejecting a bid solely on grounds of nationality; to try to do so could have adverse consequences for inward investment and for relations with the United States of America. He recommends that, instead, the Government should rely on the MMC's present powers to take account of the public interest. The MMC is a quasi-judicial body representative of a wide range of interests and operating at arms-length from Government. If they were to declare a bid against the public interest it would, arguably, be seen as a different matter from such a declaration by the Chancellor of the Exchequer.

6. The Chancellor of the Exchequer's counter-argument is that the Secretary of State for Trade's approach would be satisfactory if it could be assumed that the MMC would always concur with the Government's judgment of the public interest. No such assumption can, however, be made; and, if the MMC were to find in a particular case that there were no features against the public interest the Secretary of State for Trade does not have powers that would enable him to overrule them. In the Chancellor of the Exchequer's judgment, powers confined to prudential controls would give no assurance that the present loophole was effectively plugged.

7. Either legislative route would add to the problems of managing the programme in the 1981-82 Session; the business managers may argue that it is probably too late to drop any other Bills to make room for a Banking Bill.

Application to the Royal Bank of Scotland

8. The legislation would formally apply to the current bids for the RBS, but the Chancellor thinks that it would be retrospection of an indefensible kind to use



it to prevent the HSBC's bid from going through, if the MMC do not oppose it. In their minutes to you of 8 and 15 October the Secretary of State for Scotland and the Lord Advocate argue that it would then be open to the Government to exercise the new powers in relation to the HSBC bid, if the MMC do not object to it on competition grounds but the Government wish to stop it. They believe that anything less would be criticised as locking the stable door after the Royal Bank horse had bolted. The Lord Advocate advises that it would not be improper to include the RBS if legislation is announced either before the MMC reports or at the same time. The RBS is important because it accounts for 40 per cent of the Scottish banking system, and also owns one English clearing bank, Williams and Glyn's; and the Chancellor's point on retrospection loses some of its force when considered against the fact that it is necessary to take legislation only because the control that was believed to be effective and available has been destroyed by the HSBC's action in flouting it.

HANDLING

9. After the Chancellor of the Exchequer and the Secretary of State for Trade have introduced their papers, the main Ministers who will probably wish to comment are the Secretary of State for Scotland and the Lord Advocate, and the Lord Privy Seal (NB It seems that the proposals do not give rise to any overriding European Community problems). You will then wish to hear the views of the Lord President of the Council and the Chancellor of the Duchy of Lancaster on the implications for the management of the legislative programme; the Chief Whip may wish to comment on how well the proposed Bill might be received. The Secretary of State for Industry may also wish to comment.

10. On the assumption that the Bill is not ruled out solely on grounds of pressure on the 1981-82 programme, the main questions seem to be:

- (i) Should new powers in relation to takeovers be confined to prudential powers, as proposed by the Secretary of State for Trade, or should they also include wider powers to veto for reasons of the public interest, as proposed by the Chancellor of the Exchequer? The argument turns on a judgment of how effective the MMC would be in taking account of the public interest.



- (ii) If a majority of the Committee were to prefer to confine the powers to prudential questions, would the Chancellor of the Exchequer want to proceed now with such legislation?
- (iii) He will probably wish to take such powers in due course but he may not wish to press for those powers alone to be taken in the 1981-82 Session.
- (iii) If it is agreed that there should be legislation, should the announcement make clear that it would apply to the present Royal Bank of Scotland case in the event of the MMC not opposing the merger?
- (iv) When could any announcement of new legislation be made?

CONCLUSIONS

11. You will wish to sum up with reference to the Committee's decisions on the four questions listed above. If it is agreed that there should be legislation, you might invite the Chancellor of the Exchequer to arrange for Treasury officials to consult with the Foreign and Commonwealth Office to ensure that any European Community aspects are taken fully on board in the announcement and in the legislation.

ROBERT ARMSTRONG

28 October 1981

FROM:

THE RT. HON. LORD HAILSHAM OF ST. MARYLEBONE, C.H., F.R.S., D.C.L.

cc Walter



Prime Minister

Ms 28/10

HOUSE OF LORDS,
SW1A 0PW

CONFIDENTIAL

Prime Minister

Bank Takeovers and Mergers

1. I have some reservations about the potential political implications of the proposals in the Chancellor's paper E(81)104 for legislation to give the Government formal power to control bank takeovers in the public interest.
2. However the proposals are presented, my anxiety is that they may make future Labour arguments for the nationalisation of the banks more difficult for us to counter. In the event of a veto by a Conservative Government of a proposed banking takeover, nationalisation may well be presented as a simpler alternative, involving no major differences of ideology or principle. By bringing the issue of banking control to the fore, we might in other words be paving the way for measures which, carried to their logical conclusion, would result in public ownership of the banks with all the attendant evils of a socialist state which this would imply.
3. I am sending copies of this minute to members of E, the Lord President of the Council, the Secretary of State for Scotland, the Attorney General, the Lord Advocate, the Parliamentary Secretary to the Treasury and Sir Robert Armstrong.

H: of S: M.

28 October 1981.

CONFIDENTIAL

PRIME MINISTER

BANK MERGERS AND TAKE-OVERS: E COMMITTEE 29 OCTOBER 1981

1. The Bank/Treasury Proposal

The Chancellor's suggestion is that the Government take on arbitrary powers such that it may disallow bank mergers or take-overs, whether involving foreign banks, colonial banks, or domestic banks, if these are deemed to be against the "public interest".

2. The Biffen Proposal

This would simply extend the powers of the authorities supervising the banking sector to approve or disapprove changes of control on specified "prudential" grounds. These would be defined by statute similar to those used for the Secretary of State for Trade's control over insurance companies, namely doubts about confidence, probity, and financial standing of the bidder.

3. The Case Against the Chancellor's Proposals

3.1 They would inhibit the spur to efficiency which comes from the threat of take-over. Under the stimulus of the additional competition introduced in recent years, the clearers have become both more enterprising and efficient. Yet they are still criticised, and in many respects rightly, by some of the Government's most ardent supporters, such as W.G. Poeton, Nigel Vinson, etc. There are many industrialists who would much prefer to see German and American lending practices more widely practised in Britain - as you will see in the Oct 26 report of Michael Gryll's group. And only take-over, or merely the lively threat, is likely to change the practices of the cartel of the clearers.

3.2 It will be interpreted as an attempt by the Government to reintroduce controls in the banking system. The Chancellor's Annex frankly admits that one of the reasons for having controls on mergers is that the Government may wish to introduce corset controls, credit rationing systems (and although he does not mention it also exchange controls). I suspect that the markets are bound to interpret such arrogation of extensive powers of veto as a preparation for the possibility of controls.

3. It would increase very considerably the arbitrary power of the Bank and in practice some officials in Treasury. Again the experience under the Banking Act has not been at all happy. (Walter Salomon describes the effects, with pardonable exaggeration, as a fiasco.) And it is inconsistent with the Government's general attitude to confer large powers of veto with no requirement to make a specific case and no rights of appeal. It also gives the right essentially for the Bank and Treasury to limit a shareholder's appropriation of his capital.

3.4 London has become the banking centre of the world because the powers of the Authorities on non sterling operations were minimal. Since the abolition of exchange control the distinction between sterling and non sterling has become less important. It is important to maintain the "open door" policy as much as possible. In practice, our clearers have been buying extensively into banks abroad, and particularly in the United States. The Chancellor refers to rumours about the acquisition of clearing banks by United States banks. However, in recent years the opposite has occurred. For example the Midland Bank has acquired Crocker National, the thirteenth bank in size in the United States. Any legislation on our part would invite reciprocal reaction by foreigners. Yet I am sure that Britain can only gain from the most open free trade in banking services. It is one field where we have a relative advantage.

4. A Critique of the Biffen Proposal

Generally the Biffen proposal seems to be much more consistent with the main moral, political and economic precepts of Government policy. The Bank has powers under the Banking Act to supervise banks for their "prudential" arrangements. These could easily be extended, if indeed it is legally necessary to do so, to cover the issue of mergers and take-overs. I think we should be careful, however, not to embrace the additional concept of banning mergers if they are in "the public interest". This is a portmanteau term that has been used for virtually every piece of Socialist legislation in the last 30 or 40 years. The public interest is normally transmuted into private purpose. A worrying feature of the present system of informal control and the Chancellor's proposal is that there is an apparent interlocking interest between politicians, senior civil servants and the banks. Retired Treasury officials

/such as

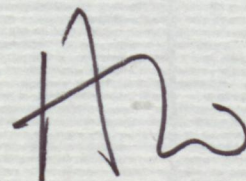
(such as Lord Armstrong) and ex-Bank employees (eg Jeremy Morse) naturally seem to end up in the banking system. We cannot prevent such appointments. But we can avoid the concentration of power in the hands of the Authorities which make such appointments potentially embarrassing.

5. The Hong Kong Shanghai Bid

This bid has been the occasion for reviewing the legislation. There is no doubt that the HSBC is acting within the law. But it has caused consternation, particularly at the Bank of England, because the Hong Kong Shanghai Banking Corporation (HSBC) has been very aggressive. Sandberg, the Chairman, has much upset the Bank. We cannot control the HSBC; that is regulated by the Government of the Crown Colony. But if the HSBC did acquire the Royal Bank of Scotland, the RBS would still be controlled through the normal banking legislation and regulations in the United Kingdom. (I understand that the HSBC have made it known that they are willing to give undertakings of their intention that RBS will conform with the normal practices and regulations of banking in the UK - including the prudential requirements. Thus it appears that if the "prudential" version of the Biffen proposal were adopted, this is unlikely to prevent the take-over occurring.)

6. Conclusion

The Chancellor's suggestion that there be an arbitrary veto power on bank mergers and take-overs is inconsistent with the general principles pursued by Government and may generate many fears that the Government is laying down the basis for extensive controls of the banking system and perhaps also foreign exchange markets. The Biffen proposal is much more modest and is as far as one needs to go in the present circumstances. The Biffen proposal would avoid the acquisition of considerable power by the Bank and the Treasury.



ALAN WALTERS

26 October 1981

CONFIDENTIAL

✓ Mr. Walter²



Prime Minister

Sean
Pd

This is to be discussed

at the next meeting of E.

M

MS 19/10

PRIME MINISTER

BANK MERGERS AND TAKEOVERS

The Secretary of State for Scotland has passed to me copies of various minutes addressed to you on this matter.

At the outset I should say that I agree entirely with his minute of 8th October. However there are in particular two points which I would wish to develop.

The first is that the Lord Privy Seal in his recent minute referred to the European Community law implications of the proposed legislation, and particularly to the possibility of challenge by the Commission on the basis of Articles 52 and 221 of the Treaty. I think that Article 53 might also be relevant. However I consider that the difficulties he refers to in that connection might not be insuperable.

There are examples of situations both in respect of legislation and administrative action where matters which at first glance appear potentially discriminatory to EC nationals have not been challenged by the Commission as a result of appropriate and agreed assurances as to the non-discriminatory nature of the policy and intended effect of the matter concerned. I am thinking particularly of the assurances negotiated with the Commission in 1979 and 1980 in connection with our operation of the Petroleum Landing Requirement and connected matters. I understand that appropriate assurances may also have been given in connection with our intended operation of the provisions of sections 11 to 13 of the Industry Act 1975.

Whereas such assurances given to the Commission could not, of course, prevent proceedings before the European Court brought by another Member State, it would at least mean that the legislation could be enacted without the risk of challenge by the Commission and that it could be operated effectively against any non-community interests.

You will appreciate that my concern in this matter is aroused principally because of the present situation in relation to the Royal Bank of Scotland. In that connection I would like to support the view put forward by George Younger that the RBS should be included in any proposed legislation. Clearly the situation is not without difficulty. Given a Report from the Monopolies and Mergers Commission which is opposed to the proposed merger, inclusion of RBS would not be necessary. The problem arises if the MMC does not oppose the merger but the Government nevertheless wishes to stop it. I can see no reason for suggesting that it would be improper to include the RBS if legislation were announced before the MMC

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reports: the existing bids lapsed on the making of the reference to the MMC. Alternatively it would be possible to arrange for an announcement to be made about legislation at the same time as the MMC Report is published. Such an announcement could make it clear that the RBS was to be included. I share George Younger's concern that, as at present proposed, the legislation would catch any later bids for the Royal Bank, but not the existing bids. That seems a most undesirable situation.

I am sending copies of this minute to Geoffrey Howe, Willie Whitelaw, Peter Carrington, Francis Pym, Patrick Jenkin, George Younger, Nicholas Edwards, John Biffen and Sir Robert Armstrong.

MJC

MACKAY OF CLASHFERN

15th October 1981.

CONFIDENTIAL

CONFIDENTIAL

R H



Earl Pe...

BLIND CC Mr Walters
Mr Duguid

10 DOWNING STREET

From the Private Secretary

12 October, 1981

Bank Mergers and Takeovers

The Prime Minister has seen and noted the Chancellor's minute of 16 September. She has also seen the subsequent minutes from the Secretaries of State for Industry, Trade and Scotland, the Lord Privy Seal, and the Minister of State for Consumer Affairs.

It is clear that it will be necessary for Ministers to discuss these issues; and I understand that it is planned to place this issue on the agenda for an early meeting of E Committee.

I am sending copies of this letter to John Halliday (Home Office), Brian Fall (Foreign and Commonwealth Office), David Heyhoe (Lord President's Office), Ian Ellison (Department of Industry), John Rhodes and Peter McCarthy (Department of Trade), Muir Russell (Scottish Office), John Craig (Welsh Office) and David Wright (Cabinet Office).

M. S.

John Kerr Esq
H M Treasury

CONFIDENTIAL

ETH



c Mr. Walters

NEW ST. ANDREWS HOUSE
ST. JAMES CENTRE
EDINBURGH EH1 3SX

CONFIDENTIAL AND COMMERCIAL - IN CONFIDENCE

Prime Minister

BANK MERGERS AND TAKEOVERS

I have seen Geoffrey Howe's minute to you of 16 September.

I very much agree with the logic of Geoffrey's arguments; indeed it was the kind of considerations set out in his minute which led me to seek reference to the Monopolies and Mergers Commission of the Royal Bank of Scotland bids.

I do however see considerable difficulty about one aspect of Geoffrey's proposal - his suggestion that the new legislation should apply to all future bids but not cover the current bids for the Royal Bank. If, in the event, the MMC conclude that the current Royal Bank bids are not contrary to the public interest, an announcement of our intention to legislate would give rise to very considerable criticism that we were locking the stable door after the Royal Bank horse had bolted. It would be suggested that while the Government recognised the need to give itself an opportunity to exercise direct control over such mergers, the Royal Bank case was not thought to merit such consideration. I do not need to emphasise the difficulties that this would create for me politically, especially as it would appear to everyone in Scotland that it was the controversy surrounding the bids for the Royal Bank which had made Government conclude that it could not accept a similar fate for the English clearers. The proposal does also, as John Biffen points out, raise implications for our policies on inward investment - though I think that a clear distinction can be drawn between inward investment which leads to the creation of considerable numbers of new jobs in the UK and inward investment which simply leads to loss of domestic control of part of what is a very concentrated as well as strategically vital sector of our economy. I would therefore be uneasy about John's suggestion that our ability to examine proposals for changes of control should be limited to their prudential aspects.

For these reasons I think that it would be most desirable for us to consider the whole issue in E Committee. A number of factors need to be weighed, including the political difficulties to which I have referred, the Governor's particular concern about the HKSB bid for the Royal Bank and the difficulty of appearing to discriminate against it in view of our relations with the Hong Kong Government. In my view it is essential to bring the legislation forward in such a way as to enable us to consider collectively the two current bids for the Royal Bank as well as any other later bids for the Royal Bank that might emerge following the announcement of the MMC's conclusions. Under Geoffrey's present proposals it appears that any such later bids would be caught while the two present bids would not. It follows that the announcement of the intention to legislate would

require to be made before the MMC have completed their investigation, and should make clear that the current bids for the Royal Bank will be caught.

I am copying this minute to Geoffrey Howe, Willie Whitelaw, Peter Carrington, Francis Pym, John Biffen, Patrick Jenkin, Nicholas Edwards and Sir Robert Armstrong.

L.Y.

8. October 1981



c Mr Walters.

Prime Minister

We now have comments from Mr Biffen, Mr Younger and Mr Atkins. A discussion at E looks inevitable now.

PRIME MINISTER

BANK MERGERS AND TAKEOVERS

Ms 9/10

I have now had time to consider the Chancellor's minute of 16 September to you, about which Sally Oppenheim wrote on 17 September.

As the Chancellor says, his proposals raise a number of important political and economic issues. Patrick Jenkin has commented on some of these in his minute of 28 September, and has made the point (rightly, I am sure) that the way in which we present any change of policy may well prove as important in the immediate term as the change of policy itself. In my view, the issues merit a full discussion among colleagues before a firm decision is reached; and I suggest that you may like to hold a meeting of E for the purpose, later this month.

Meanwhile, perhaps I could set out my preliminary views. My detailed Departmental interest in the Chancellor's proposal is twofold, covering not only the Government's policy towards merger control but also our practice in formulating a regime for supervising financial institutions (where I have statutory responsibilities in relation to insurance companies). More widely, I am of course concerned with the international aspect of our economic policies, and the possible commercial effects on UK firms of any adverse reaction overseas to changes in very longstanding British policies on such questions as inward investment.

Against this background, I recognise the case which the Chancellor has made; and I agree - though not without hesitations - that we should introduce legislation amending the Banking Act so as to provide for powers to approve changes in control of banks. The question which concerns me is the extent of those powers, and the risk that they could be criticised either within the country (as removing UK bank mergers from the ambit of competition policy) or internationally (as providing a route towards a discriminatory policy on inward investment, contrary to our traditional United Kingdom practice).



I take the international aspect first. Since the last war at least we have encouraged a considerable flow of inward investment, principally in manufacturing industry; and successive governments have recognised that this has been both successful and beneficial. We have similarly benefited from extensive outward investment not only in manufacturing industry but also in banking and other service industries. Our interest has been well served by a generally liberal policy among OECD countries to the flow of investment; and this has been furthered by a developing web of international obligations enshrining the non-discrimination principle, reflected not only in our EEC Treaty obligations but also in the OECD Code on Multinationals. It is very much in our interest that there should be no general retreat from these practices and obligations; and I believe that any evidence of a retreat would be quickly noticed - and no doubt acted upon - by our trading partners. United States opinion in particular has shown itself extremely sensitive to recent Canadian measures to strengthen control of inward investment.

Any change in our arrangements affecting mergers or inward investment in an important sector of our economy could therefore provoke apprehension abroad. This could be very damaging. I conclude that the measures we take should be the minimum required to meet the case.

I am also concerned that any new measures should not go so wide as to affect competition in the banking sector and the pressures which currently reinforce it. There have been recent and welcome signs of increasing competition in banking both in commercial banking, where foreign competition has brought benefits to our exporting interests, and in deposit banking. Our present arrangements, under which the Fair Trading Act provides for the Monopolies and Mergers Commission (MMC) to assess competition issues arising in monopoly and merger cases, give the Government a means of fostering competition. I believe that Geoffrey Howe and I are at one in believing that we should do nothing to restrict the continued application of these arrangements to the banking sector.



The MMC process has two further strengths which Geoffrey Howe may, I think, have underestimated in putting forward his proposals. First, the Commission is not confined by statute to considering competition questions only: it has a general responsibility to consider the issues of public interest as a whole in the matters referred to it. Secondly, the Commission has over more than thirty years achieved a deserved reputation for impartiality and objectivity, reinforced by the fact that its reports are published documents which stand or fall by the reasoned arguments they set out. In this way it has achieved acceptance, at home and abroad, as an independent quasi-judicial body appointed to make findings on public interest matters.

I underline the wide scope which these arrangements offer for considering the public interest. This scope is not merely theoretical. The Commission has shown itself in practice capable, particularly in merger cases, of considering public interest issues broader than those of competition. Indeed it can consider merger cases where no competition issues arise: an instance was the Commission's recent report (published last month) on the Davy/Enserch merger and in which the Commission found against the merger. I would by no means rule out a similar outcome if the Commission were asked to investigate foreign bids for one or more UK clearing banks.

We therefore have strong and well established machinery for judging the public interest issues arising in cases of changes of control of UK banks; and I would suggest to colleagues that we do not need controversial legislation to duplicate it. At the same time, I would agree with Geoffrey Howe that the Banking Act should be strengthened to include some mechanism for the supervisory authorities to approve changes of control. To my mind this should not be a complex mechanism for deciding on the wider aspects of the public interest: the Fair Trading Act already provides for that. I accordingly suggest that the proposed new powers need to go no further than giving the authorities supervising the banking sector powers to approve or disapprove changes of control on "prudential" grounds. These powers would correspond essentially to the powers I exercise in relation to change of control over insurance companies (for which I am the supervising authority). These are defined by statute and cover reasons of doubt about the competence, probity



or financial standing of a bidder, whether British or foreign.

A scheme on these lines would, I believe, have several strengths. First, it could be presented as a simple but necessary amendment to our banking legislation. I believe too that it would prove more effective and defensible in practice. Decisions taken by the supervisory authorities under the new powers will need to be explained and justified (as I have been called upon to explain and justify my own decisions under the Insurance Companies Act): and it is right that they should be. I believe that there would be widespread criticism, both of the legislation and of decisions under it, if the power to disallow a merger represented an absolute power of veto exercised on wide and undisclosed considerations of public interest. A narrower power, exercisable on defined prudential grounds, would avoid these hazards. Nor do I believe that a narrow power of this type would be inadequate for the purposes which the Chancellor has in mind: I should be very surprised if an applicant requiring statutory approval as a controller of a UK bank, who would surely approach the authorities first in confidence, would choose to put his proposals at risk by anticipating the authorities' decision by a public attempt to assume control without assurance of the necessary approval. And there would also be the power to refer cases to the MMC where a wider examination of the public interest was necessary.

To sum up, I acknowledge the force of Geoffrey Howe's proposal, but I consider that his objectives could be achieved by less controversial measures, both giving more recognition to the strengths of our existing arrangements and avoiding some of the possible hazards to our wider objectives. I suggest that we meet in E to discuss these points, and that meanwhile Geoffrey Howe's officials and mine should explore a solution on the lines I have suggested.

Geoffrey Howe also wrote about the timing of any announcement of our plans. I agree that this is a question over which we shall



need to take care. I should prefer, however, to reserve judgement on this until we are agreed on the substance of the measures we propose to take.

I am sending copies of this minute to Geoffrey Howe, Willie Whitelaw, Peter Carrington, Francis Pym, Patrick Jenkin, George Younger, Nicholas Edwards and Sir Robert Armstrong.

W J B

W.J.B.

Department of Trade
1-19 Victoria Street
London SW1A

2 October 1981



Prime Minister

Ms 28/16

C. M. Walters

Prime Minister

BANK MERGERS AND TAKEOVERS

The Chancellor of the Exchequer sent to the Foreign and Commonwealth Secretary a copy of his minute of 16 September. In his absence I would like to make a few comments on international implications of his proposal.

2. We clearly need to protect our banking sector from takeovers which would be against the national interest, but at the same time, as the Secretaries of State for Industry and Trade have pointed out in their minutes of 28 September and 2 October, the UK has a strong interest in the free flow of international investment. This is particularly important in the case of the US, where in the banking sector the more relaxed policy of recent years has enabled all the major British clearers to acquire substantial US banking subsidiaries. I fear that there would be resentment if, having acquired a significant share of the US retail bank sector, we passed a law which could readily be used to prevent comparable US purchases here. Our existing legislation already enables us to refer major takeover bids to the Monopolies and Mergers Commission and gives it wide terms of reference. As the Davy-Enserch case has most recently shown, the Commission is prepared to take a broad view when making its assessment of whether a proposal is likely to be against the public interest. I therefore share the doubts expressed by the Secretary of State for Trade over the need for the government to take controversial new powers and am much attracted by his proposal for less wide-ranging legislation to give greater control over bank takeovers.

/3. Perhaps



3. Perhaps I could add two more detailed points. The first concerns the compatibility of what the Chancellor is proposing with our existing obligations under European Community law. In paragraph 7 of his minute he makes it clear that he would take powers which applied even-handedly to both domestic and foreign bidders. This would certainly help us to rebut any EC criticism as he says, but I am advised that it might not in itself be sufficient. It appears from his minute - I would welcome clarification of this - that he would have discretion to refuse the acquisition of shares in banks, without being obliged to apply any publicly stated and objective criteria, and without being required to give an applicant his reasons for refusal. It also appears that an aggrieved applicant would be given no legal redress. If my understanding of all this is correct, we might be challenged by the Commission on the basis of Articles 52 and 221 of the Treaty. They could argue that the power would be open to abuse, and a national of another EC country could not be sure that, for example, he was being prevented from establishing himself as a banker in the UK (by acquiring a controlling interest in the bank) solely because of his nationality. There is also a risk that a refused bidder for a UK bank might challenge such a decision by the Chancellor in our Courts, on the basis of his rights under Article 52, which the European Court has held to have direct effect (or Article 221, which probably also has direct effect). I suggest therefore that before drafting any legislation it would be wise to look into these legal points with some care.

4. The second point is one of considerable importance in our political relations with Hong Kong. The Chancellor's minute refers throughout to 'foreign' banks, while pointing to the bid of the Hong Kong and Shanghai Banking Corporation as the immediate cause of his concern. I know he will understand that it is important that the new legislation or any explanation for it in Parliament should not state

/or even



or even imply that banks in the Dependent Territories, and particularly Hong Kong, are 'foreign' or non-British. It is essential that HMG do not appear to be distancing themselves from Hong Kong or playing down the Britishness of the Territory as this could have a serious effect on the maintenance of confidence there. Ian Gilmour explained this in his letter of 21 May to the Chairman of the Monopolies Commission about the Hong Kong and Shanghai Banking Corporation's bid for the Royal Bank of Scotland, a copy of which was sent to Treasury officials (Clift's letter of 9 June to Pirie). I should therefore be grateful if, in any draft legislation, either a clear distinction be made between foreign banks and those in Dependent Territories or some more neutral phrase, such as 'overseas banks' be used.

5. By the same token, it is important that in any debate the Government do not use the Hong Kong and Shanghai Banking Corporation case as justification for the introduction of the new legislation.

6. I am copying this letter to the Chancellor of the Exchequer, the Home Secretary, the Lord President of the Council, the Secretaries of State for Trade, Industry, Scotland and Wales, and to Sir R Armstrong.

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Prime Minister

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We now have comments from Mrs Oppenheim for ~~Bank~~ industry on the Committee's proposal. But

PRIME MINISTER

no, J. M. Biffen also wishes to comment.

BANK MERGERS AND TAKEOVERS

Am A

Geoffrey Howe's minute of 16 September proposed legislation to provide new powers for the control of foreign bids for UK clearing banks.

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2 I share his concern about our vulnerability on this front and agree with the general principle of what he is proposing. I agree that we should be open to criticism if we were not in a position to block a foreign bid if we wanted to do so.

3 However, while supporting the proposal, I am concerned about presentation. The country has a strong interest in the free flow of inward and outward investment and we have international obligations in this respect. There will inevitably be criticism, from Community partners and the United States in particular, that the measure is aimed at foreign takeovers. A strong defence is necessary which stresses that this legislation in no way diminishes our commitment to internationally mobile investment.

4 I see no difficulty in justifying the need for special powers to exercise control over the ownership of banks. It would be



important to stress the special circumstances of banking and to give a convincing explanation of why the existing controls in the Banking Act are inadequate. This explanation must not call into question the non-discriminatory character of the powers as between foreign and British ownership.

5 We shall also need to ensure that, when announcing the proposed legislation, we say nothing that conflicts with our own criticisms of our opponents' Industry Act 1975 which contains powers concerning the transfer of control of important UK manufacturing undertakings to non residents.

6 The question of timing is also important. The Bill should be announced before any further foreign bids for UK banks emerge. It should not be delayed until the MMC report on the Royal Bank of Scotland, provided it is made clear that the new powers will not be used to frustrate that bid if the MMC themselves do not find against it.

7 I am sending copies of this minute to Willie Whitelaw, Peter Carrington, Geoffrey Howe, Francis Pym, George Younger, Nicholas Edwards, John Biffen and Robert Armstrong.

PJ

P J
September 1981

Department of Industry

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CONFIDENTIAL

PRIME MINISTER

BANK MERGERS AND TAKEOVERS

I have seen the Chancellor of the Exchequer's minute to you of 16 September which was copied to John Biffen.

2 As the Chancellor recognises the proposals in his minute have wideranging implications both for the procedures we have hitherto followed on mergers and, more generally, for our policies on competition and inward investment as a whole. I am sure that John Biffen will wish to form his own views on them on his return from the United States on 29 September. I shall of course be giving these proposals close study in the meanwhile; but I would not wish to reach a final view until John Biffen has himself had a chance to consider them.

3 I am sending copies of this minute to Geoffrey Howe, Willie Whitelaw, Peter Carrington, Francis Pym, Patrick Jenkin, George Younger, Nicholas Edwards and Sir Robert Armstrong.

Sally

SALLY OPPENHEIM

17 September 1981

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17/9

in PM's
Box

Prime Minister

2



cc Mr. Walters
Mr. Wilton

Treasury Chambers, Parliament Street, SW1P 3AG
01-233 3000

The Chancellor proposes legislation to prevent take-overs (post-Hong Kong and Shanghai) of UK banks. I think this will have to be discussed; we can decide the forum when we have comments from the Ministers concerned.

PRIME MINISTER

Thank you
M.T.

BANK MERGERS AND TAKEOVERS

As you know the Hong Kong and Shanghai Banking Corporation's (HSBC) bid for the Royal Bank of Scotland Group (RBS) in April (now under consideration by the Monopolies and Mergers Commission (MMC)) raises a wider problem - our ability to control takeovers of UK banks, and in particular foreign bids for the clearing banks.

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2. I have been considering this with the Governor, and I am reluctantly forced to the conclusion that we must legislate on this subject in the forthcoming session. I recognise that it is not easy to find time in the legislative programme at this stage. But unless we do, we could find ourselves powerless to prevent the major clearing banks falling into the hands of foreigners. Without pre-judging what we would do in any particular case, I believe we would be open to strong political criticism if we lacked the power to control such developments. John Biffen, with whom I have had an initial discussion, agrees with this general case, though we have agreed that our officials should discuss the interaction of the powers I propose with those contained in the Fair Trading Act.

3. Until now, a special control over banking mergers has been exercised informally through an understanding between the Bank of England and the banking system that takeover proposals were not to be pursued without the Bank's consent. These arrangements had been respected by UK and overseas banks alike, but

/clearly



clearly they now lack credibility. Others could follow HSBC's example. You will have seen press rumours of US interest in one or two of the big four clearing banks. The Bank in fact believe that a significant part of the British banking industry could face foreign takeover once the RBS case is out of the way.

4. I am not, of course, saying that all proposals for foreign takeovers, even of major banks, should be resisted. Each case will have to be considered on its merits. But I do not think we could tolerate a situation in which, for example, several UK clearing banks fell into American hands. We must have the powers to prevent that happening.

5. We might not have to use them. The Bank's views could still carry sufficient influence to deter unwanted bidders. An adverse verdict by the MMC on HSBC's bid might also have this effect. And it is also true that any bids that were made could be referred to the MMC under the Fair Trading Act, as has been done with the bids for RBS. But the Governor and I have concluded, reluctantly but firmly, that we would be running unacceptable risks if we sought to rely on any of these possibilities. Even if the MMC recommended on public interest grounds that the HSBC bid should not proceed, the reasons given might not be conclusive or all-embracing as far as future cases were concerned, and banks could still be subject to immediate pre-emptive strikes by bidders in the market place, by means of 'dawn raids', etc. While there are powers to prevent mergers in the Fair Trading Act, they are only available if the MMC, who are mainly concerned with questions of competition, find the merger against the public interest. This leaves great uncertainty on whether the Government could in practice prevent a banking takeover, perhaps on national interest or prudential grounds, in any particular case.

6. Given this uncertainty I do not consider that the Fair Trading Act provides adequate control over takeovers of UK banks.



..... Banking mergers have always been regarded as a special category, as the existence of the informal arrangements shows. Besides the political argument for doing so, there are a number of other cogent reasons set out in the Annex to this minute. I think it essential that we introduce special statutory powers to ensure that we are able to control them, now that the informal special arrangements have become unreliable.

7. I appreciate that the introduction of special powers could be regarded as contrary to our general approach of encouraging both foreign investment and greater competition. I would not accept this charge. The controls I have in mind would only replace the previous informal arrangements and put the UK on par with most other Western countries. There is no intention of changing our present liberal approach to foreign entry, demonstrated by the fact that London has more foreign banks than any other major financial centre. While my concern is chiefly with foreign takeovers, particularly of major clearing banks, I see the need to take powers to control all takeovers of UK banks and these powers would apply even-handedly to both domestic and foreign bidders. This would be our defence against any EC criticism, and we would of course assure the Commission that we would use these powers in conformity with our Treaty obligations.

Timing and Procedure

8. The HSBC bid which is now before the MMC must continue to be dealt with under the existing powers in the Fair Trading Act, with the consequence that we would be unable to prevent it unless the MMC find it against the public interest. But if we are to be in a position to prevent further bids following the MMC's decision, it is essential to introduce legislation next session. Recognising the difficulty for the legislative programme, I should clearly want to keep this as simple as possible. My proposal is to introduce

/an amendment

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an amendment to the Banking Act 1979 to require prospective shareholders to obtain my consent to become controller of a recognised bank or licensed institution incorporated in the UK. My decision would be taken on advice from the Bank on public interest grounds (which would include the national interest and prudential considerations). Any decision to refuse an acquisition would be subject to Parliamentary scrutiny under Statutory Instrument procedure.

9. The timing of an announcement will need careful consideration. To avoid difficulty in applying the legislation to any further bids the latest time to announce the intention to legislate would be when the Government's decision on the RBS case is made known, now expected to be in January or February next year. But there could be a case for an earlier announcement, in case the delay in the MMC's report or leaks about their findings led to further bids at an earlier stage. I shall be giving this further thought.

10. I should be grateful for your views on this proposal. Unless colleagues are able to agree to the proposal at this stage, I would propose to put a paper to E Committee in October.

11. It might help to ease this proposal on its way if I were at the same time to propose a further modest amendment to the Banking Act. Its purpose would be to side-step the political difficulty arising from appeals (which I have to determine under the Act) against the Bank's refusal to grant recognised bank status, e.g. to the Commercial Bank of Wales, which then loses the right to use the word "bank" in its name. I am considering with the Governor what action it might be possible to take.

12. I am sending copies of this minute to Willie Whitelaw, Peter Carrington, Francis Pym, John Biffen, Patrick Jenkin, George Younger, Nicholas Edwards and Sir Robert Armstrong.

G.H.

16 September 1981

CONFIDENTIAL
COMMERCIAL IN CONFIDENCEARGUMENTS FOR SPECIAL CONTROLS OVER BANKING MERGERS

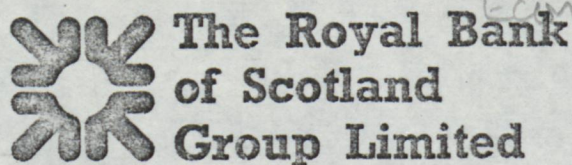
Besides the risk of political criticism if major banks came under foreign control, the reasons for maintaining special controls over banking mergers, and giving them statutory form, include the following points:-

- a) The importance of banks to the economy. Banks play a central role in the economy as recipients of savings and managers of money for the public, and as a channel for allocating funds to industry and commerce.
- b) Banks' importance to economic policy. Banks' central role and their importance for monetary policy in particular has led successive governments to seek voluntary cooperation from banks over a wide field. Practical examples include the corset, directional guidance and consumer credit controls. Such cooperation could be threatened by undesirable takeovers.
- c) Public confidence in the banking system. Public confidence in the banking system is important for both economic and social reasons, and effective prudential supervision has a significant role to play in maintaining it. Supervision should include oversight of the ownership and control of banks to ensure that they are in reliable hands, but the Banking Act includes no power over changes of control because of the existence of the informal arrangements to deal with mergers. It is unsatisfactory for the supervisory authority to be responsible for supervising an institution without power over changes in its control. And now that the informal arrangements cannot be relied on, it is desirable for prudential reasons to have power on this point - as already exist in the case of insurance companies.

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This argument, on which the Bank lays great stress, applies to domestic as well as foreign takeovers.

- d) Possible support operations. If, despite thorough supervision, a crisis of confidence occurred which created the need for immediate support, as in the lifeboat operation in 1973-74, foreign ownership of major banks could present difficulties. There could be major objections to the use of UK public money to support a foreign-owned institution in such circumstances, since the long term benefits of such support could go to overseas shareholders. Indeed, foreign ownership might increase the risk to public funds since domestic banks might be reluctant to help as much as they did in the past.
- e) Practice in other countries. Most other countries regard banking as special and have specific powers to control mergers and takeovers. In France and Italy the major banks have long been in public ownership, so that no question of foreign takeover can arise.
- f) Bank share value. Clearing bank shares stand at a substantial discount on net asset value. While the reasons for this are complex, it is unacceptable that major UK banks should be picked up by foreign buyers on the cheap.



The Royal Bank of Scotland Limited
Williams & Glyn's Bank Limited

Reference to the Monopolies and Mergers Commission of take-over
bids for The Royal Bank of Scotland Group Limited by Standard
Chartered Bank Limited and The Hongkong and Shanghai Banking
Corporation.

FACT SHEET

- 1979-80 : Lloyds Bank, the largest shareholder in The Royal Bank Group (16.4%) made informal approaches to acquire the Group.
- Late 1980 : Royal Bank decided to seek a "merger with a UK bank with a strong overseas presence."
- 1981
March 17 : Standard Chartered, with the approval of the Bank of England, made an agreed bid of £320 million for Royal Bank. As part of the deal, Royal Bank conditionally agreed to sell its 39.3% holding in Lloyds & Scottish to Lloyds Bank which, in turn, agreed to support the bid.
- March 20 : Hongkong & Shanghai Banking Corporation informed the Bank of England of its interest in acquiring Royal Bank.
- April 7 : Hongkong & Shanghai made a £500 million bid for Royal Bank. This bid was not supported by Royal Bank.
- April 23 : Standard Chartered made new agreed offer, roughly matching the Hongkong & Shanghai bid.
- May 1 : Both proposed mergers were referred to the Monopolies and Mergers Commission.

THE ROYAL BANK OF SCOTLAND GROUP

Royal Bank Group is a holding company for its wholly-owned subsidiaries, Royal Bank of Scotland and Williams & Glyn's Bank.

It was incorporated in Scotland in 1968 to effect the merger of two important existing bank groups, Royal Bank of Scotland and National Commercial Bank of Scotland Limited. At the time of the merger, Royal Bank of Scotland owned Glyn, Mills & Co and Williams Deacons Bank Limited, and National Commercial Bank of Scotland owned The National Bank Limited. The undertakings of these three English based subsidiaries were merged in 1970 to form Williams & Glyn's. The Scottish based banks of Royal Bank of Scotland and National Commercial Bank of Scotland Limited were merged in 1969 under the name 'The Royal Bank of Scotland Limited'.

Royal Bank Group has a Board of 12 directors, all of whom are also directors of one, or both, of the principal operating banks. There is a small group office to support the Board.

As at end September 1980 the Group had total assets of £6.138 bn, capital and reserves of £486 million and profit before tax for the year to that date of £100 million.

Lloyds Bank is the largest shareholder in the Group with 16.4%.

There are approximately 31,000 shareholders.

Royal Bank of Scotland has 581 branches in the UK. Of these 377 are full service branches with resident managers, 85 are full service with non-resident managers, and there are 102 sub-branches and 17 mobile offices. Locationally, representation exists at 567 branches throughout Scotland with 14 located in England. Of the latter all but three are in London.

Williams & Glyn's has 308 branches in England and Wales, of which 289 are full branches with an official in charge and 19 are offices with 'remote' managerial control.

As a result of the historical development of W & G and in particular the strong north west representation of Williams Deacon's Bank Limited, the current network has various localised concentrations around central London and large provincial centres. At September 30, 1980 W & G together with its subsidiaries had total assets of £2,629 million.

STANDARD CHARTERED BANK LIMITED

The Standard and Chartered Banking Group was formed as a result of a merger in 1970 between two complementary organisations, the Standard Bank with its large branch representation in Africa and the Chartered Bank, which still operates under that name in the Middle and Far East.

The Standard Bank was founded as a consequence of a meeting on 3 June 1857 when a committee was formed and a prospectus issued of 'The Standard Bank of Port Elizabeth'.

The Chartered Bank of India, Australia and China was incorporated by royal charter in 1853 and shortened its name to the Chartered Bank in 1956.

In 1975 the Standard and Chartered Banking Group Limited changed its name to the Standard Chartered Bank Limited and all branches of the Standard Bank and Chartered Bank in Britain became branches of the Standard Chartered Bank. Outside Europe, with one or two exceptions, the separate familiar names of the constituent banks have been retained in order to conserve goodwill.

At 31 December 1980 consolidated assets of Standard Chartered totalled £15.417 bn compared to £13.010 bn in 1979.

Market valuation at end-June was £565 million.

On an earning basis, Standard Chartered is the fifth largest bank in UK.

Standard Chartered is the largest independent British overseas banking organisation.

Unlike the English clearers Standard Chartered maintains the majority of its branches overseas in some 60 countries in Europe, the Americas, Africa, the Middle East and Asia.

It is one of the two banking groups entitled to issue bank notes in Hong Kong.

Standard Chartered maintains more than 20 branches in the UK, 5 of which are located in London, the others in major commercial centres.

Over the past decade Standard Chartered has increased its branch network in the UK, other EEC countries and elsewhere. In the US it has expanded outside New York by opening offices in Chicago, Houston, Miami and Seattle. In Toronto they have established a wholesale banking operation and in Central America their branch in Panama City is an offshore commercial bank dealing in Latin American trade.

Standard Chartered's most important recent development, however, was in 1979 when it acquired the Union Bancorp Inc. of California whose most important asset was Union Bank which, at that time, was the sixth largest bank in California and the 24th largest out of almost 14,500 banks in the US. As a direct result of this acquisition, Standard Chartered achieved a distribution of its assets in roughly equal proportions in four continents and is therefore more able to generate a balanced cash flow of its profits whatever the political and economic climate might be in any one territory.

HONGKONG AND SHANGHAI BANK

Hongkong and Shanghai was founded in 1865 by British traders in Hong Kong and became the major financier of Imperial China, achieving representation throughout East Asia.

In post-war years the bank has grown with Hong Kong, as the latter was transformed into a major industrial region and the third largest financial centre in the world. Influential Chinese entrepreneurs and a large number of immigrants from the People's Republic of China have formed the basis for the Colony's rapid commercial expansion and the bank has taken full advantage of its leading financial role and played a major part in the development of Hong Kong.

H & S has nevertheless been aware of the need to become more than a regional bank in order to minimise the economic and political exposure resulting from localised concentration.

In 1959 it acquired the Mercantile Bank, a UK bank with its major market in India. The 1960 take-over of The British Bank of the Middle East, another UK headquartered bank, represented a further broadening of the Bank's geographical base, although five years later its domestic power was considerably strengthened by the acquisition of a majority interest in the largest Chinese bank in Hong Kong, the Hang Seng Bank.

H & S has only a small presence in the UK. Its main office in London is concerned largely with international business; it also has branches in Edinburgh, Manchester and Birmingham.

The most recent step in H & S's transition from a regional bank into an international holding company was the acquisition in 1980 of a 51% controlling interest in Marine Midland Banks Inc., whose principal subsidiary Marine Midland Bank N.A. is the 13th largest bank in the US, with assets of US \$ 17.5 bn.

Market capitalisation at March 31, 1981 was HK \$ 24,959 million (£2,160 million). It is the largest locally incorporated bank in Hong Kong. Total assets at December 31, 1980 stood at HK \$ 237,787m (£19,387 million). The disclosed consolidated net profits for the year to December 31, 1980 were HK \$ 1,431 million (£122 million). In accordance with the bank's tradition, the net income figure is stated after undisclosed transfers to inner reserves.

The Board of H & S is, apart from the resident director in London and Marine Midland representatives, composed entirely of Hong Kong businessmen.

H & S now operates through more than 800 offices in 45 countries.

BACKGROUND TO A PROPOSED MERGER BY ROYAL BANK GROUP

The Royal Bank Group occupies an important place in UK banking: The Royal Bank of Scotland is the largest Clearing Bank in Scotland and Williams & Glyn's the fifth largest bank in England. The Royal Bank Group is, however, mainly domestic in its operations although it has in fact achieved some expansion in strategic locations in the USA, the Far East and Europe. The Royal Bank Group is convinced that its future development should be based on an expanded international network, offering corporate customers a comprehensive range of facilities for world-wide trading activities and also playing a significant role in stimulating the flow of capital into the British economy. However, it would be an unrealistically slow process to expand on the scale required using only The Royal Bank Group's own resources, to compete effectively with the major multinational banks now established in England and Scotland.

For The Royal Bank Group to continue independent would be completely feasible but the development of a broadly based international business would be a long and difficult process. It is for this reason that a partnership with another Bank which can provide a strong international network is attractive but, even so, The Royal Bank Group is prepared to surrender a degree of independence only to a partner which fulfills very demanding criteria.

Developments in 1979 indicated that time was no longer on The Royal Bank Group's side. The approaches from Lloyds were recognised by The Royal Bank Group as being detrimental to its interests, to those of its shareholders and of Scotland. They did demonstrate, however, the desirability of selecting a suitable partner of the Group's own choosing. The change of attitude by Lloyds had made the Group even more aware of its vulnerability not only to Lloyds, but generally, in the market place. At that stage there was no pending reference to the Monopolies Commission to ensure that the issues were fully examined.

Considerations in seeking a partner

The Royal Bank Group regards a number of criteria as essential:-

- (a) Any partner should have sufficient international strength to complement The Royal Bank's domestic weight.
- (b) Any partner should be fully acceptable to the monetary authorities in the UK in order to ensure the continuation of the present position under which The Royal Bank of Scotland and Williams & Glyn's accept the responsibilities of and derive benefit from their roles as integral and key parts of the British financial system.
- (c) The Royal Bank Group should have an entrenched major influence in the merged operation from the outset, in order to preserve interests deemed essential, especially autonomy effectively to manage the UK business and to deal with UK customers, recognition of particularly Scottish interests, and career development and genuine senior management opportunities for staff.
- (d) Full agreement and harmony by both managements from the start.

The Case for Merging with Standard Chartered

The proposed merger with Standard Chartered meets all the criteria noted above.

The business of the two groups is complementary. There is only a negligible overlap of branches and of 'wholesale' sterling and currency business, and a very close fit in related banking services. The merger would create a new fifth force in UK banking, well balanced as between domestic and international business.

The two groups have the same 'centre of gravity', being British, UK registered and sterling based. This establishes the commonality of interest necessary to make the merger work and to ensure the preservation of The Royal Bank Group's influence on the policies of the new group over time, reinforced by a substantial Board representation from the outset.

There is a will on the part of the management of both groups to carry through the merger successfully.

The Bank of England have indicated their approval of the merger.

The merger thus promises to produce considerable benefits:-

First for customers, to whom the new group would be able to offer improved international services, replacing correspondent relationships with direct access to overseas offices, speedier integrated cash management services on a world-wide basis, greater financing strength, and more informed advice. Second for staff, for whom greater opportunities would exist both for promotion and for broadening experience. Third for UK banking, which would be strengthened by the addition of a powerful new force. Finally for the UK economy, where the new group would contribute to better export performance and to the attraction of new overseas investment.

The Case against Takeover by Hongkong and Shanghai

The takeover would simply make The Royal Bank Group one more subsidiary among several world-wide of Hongkong and Shanghai.

Hongkong and Shanghai's base and 'centre of gravity' is outside the UK. Hongkong and Shanghai is not a sterling based bank. Board representation and location of the headquarters suggest that The Royal Bank Group could not expect to have the same degree of influence within the Hongkong and Shanghai group that they would have with Standard Chartered. Moreover, the community of interest that exists with Standard Chartered and that entrenches The Royal Bank Group's position with it for the future does not exist with Hongkong and Shanghai, whatever assurances may be given in the circumstances now prevailing.

The Case against Takeover by Hongkong and Shanghai (cont'd)

With Hongkong and Shanghai, the interests of staff career development would be less well served and career opportunities less good starting, as the staff of both banks within The Royal Bank Group would, from a subsidiary and remote position. It appears that the opportunity for staff to switch to service overseas for a few years and then return to domestic banking would not exist.

The working of the UK banking system depends to a large extent on the existence of close relationships of trust and confidence between the monetary authorities and the Clearing Banks, covering such fundamental matters as monetary control and prudential supervision. These relationships operate principally through the channels of the CLCB and the CSCB, of which both banks in The Royal Bank Group are currently members. While we believe that the present arrangements would continue after a merger with Standard Chartered; it may be difficult for them to do so after a take-over by a non-UK based bank such as Hongkong and Shanghai. This would not only have implications for the public interest but would put a question mark over the status now enjoyed by the two banks in The Royal Bank Group which could affect their competitive position.

* * * * *

July 1981



10 DOWNING STREET

CF

THE PRIME MINISTER

DS.
also.

13 July 1981

Dear Tony,

Thank you for your letter of 24 June about the Standard Chartered Bank's offer to acquire the Royal Bank of Scotland Group.

As you say, the matter is currently before the Monopolies and Mergers Commission for investigation. As with any merger reference, that does not mean that there is any presumption that either or both bids for the Royal Bank is against the public interest, but rather that John Biffen considered that a reference was necessary in order to ascertain where the public interest lies.

In your letter you refer to discussions which Sir Michael Herries had with George Younger before the Standard Chartered bid was announced - and, of course, before the mounting of the rival bid which further complicated what is a very important issue both in UK and in Scottish terms. At these meetings and at his subsequent meeting with you, I gather that George Younger expressed his concern about the implications for Scotland of the loss of the Royal Bank's independence; but he made it clear that the matter of an agreed merger was at that stage primarily one for the Board of the Royal Bank Group. Once the Commission has reported its

/findings

findings on both bids the Government will be able to take a collective view of them. Meantime I confirm that the Scottish Office, in common with other interested Departments, is submitting evidence to the Commission; and this evidence naturally sets out some of the considerations to be borne in mind in assessing the implications of the bids for the public interest in Scotland.

*Y
Lowe
Ragout*

The Rt. Hon. Lord Barber, T.D.

PRIME MINISTER

Royal Bank Merger

Lord Barber wrote to you complaining that Alex Fletcher is "going around expressing opposition to the proposed merger between Standard Chartered and the Royal Bank of Scotland".

I attach a draft which has been prepared by the Scottish Office in consultation with the Treasury and the Department of Trade. The draft does not actually mention Alex Fletcher. I am told that he did tell one or two people in Scotland that he was opposed to the merger, which was obviously unwise. He is now keeping silent on the subject. George Younger, who has considered the draft carefully, advises strongly that you should not in effect disown Mr. Fletcher because

- 1 copy*
- (i) it would be embarrassing, and
 - (ii) he (Mr. Younger) is not impressed with Lord Barber's handling of this issue. Apparently, he had a very bad meeting with Mr. Younger, showing total insensitivity to the Scottish aspects of the merger. By contrast, discussions between Mr. Younger and the Hong Kong Bank have been extremely cordial.
- R*

10 July 1981

Econ Pd



SCOTTISH OFFICE
WHITEHALL, LONDON SW1A 2AU

CONFIDENTIAL

Tim Lankester Esq
Private Secretary
No 10 Downing Street
LONDON SW1

2 July 1981

Dear Tim,

ROYAL BANK MERGER

Thank you for copying to me your letter of 26 June to John Rhodes, Department of Trade, about the letter to the Prime Minister from the Chairman of the Standard Chartered Bank concerning that Bank's proposed merger with the Royal Bank of Scotland.

In view of the subject matter of Lord Barber's letter, I agreed with Department of Trade that we should initiate the draft reply which you requested. I now attach such a draft which, after discussion with the Treasury and Department of Trade at official level, has been approved by my Secretary of State. My Secretary of State is strongly of the view that Lord Barber has greatly over-stated the significance of the discussions which Mr Younger had with himself and other interested parties, and he is quite clear that the Government's position in the matter has been in no way prejudiced by such discussions as he and Mr Fletcher have had. The draft attached reflects this.

I am copying this to John Rhodes, Department of Trade, John Wiggins (Treasury), and Francis Richards (Foreign and Commonwealth Office).

Yours ever,

GODFREY ROBSON
Private Secretary

DRAFT FOR PRIME MINISTER

Rt Hon Lord Barber
Chairman
Standard Chartered Bank Ltd
10 Clements Lane
Lombard Street
London EC4N 7AB

Thank you for your letter of 24 June about the Standard Chartered Bank's offer to acquire the Royal Bank of Scotland Group.

As you say, the matter is currently before the Monopolies and Mergers Commission for investigation. As with any merger reference, that does not mean that there is any presumption that either or both bids for the Royal Bank is against the public interest, but rather that John Biffen considered that a reference was necessary in order to ascertain where the public interest lies.

In your letter you refer to discussions which Sir Michael Herries had with George Younger before the Standard Chartered bid was announced - and, of course, before the mounting of the rival bid which further complicated what is a very important issue both in UK and in Scottish terms. At these meetings and at his subsequent meeting with you, I gather that George Younger expressed his concern about the implications for Scotland of the loss of the Royal Bank's independence; but he made it clear that the matter of an agreed merger was at that stage primarily one for the Board of the Royal Bank Group. Once the Commission has reported its

findings on both bids the Government will be able to take a collective view of them. Meantime I confirm that the Scottish Office, in common with other interested Departments, is submitting evidence to the Commission; and this evidence naturally sets out some of the considerations to be borne in mind in assessing the implications of the bids for the public interest in Scotland.



JFH
Econ
PSC

10 DOWNING STREET

From the Private Secretary

26 June 1981

You will have seen the letter from Lord Barber of 24 June to the Prime Minister about the proposed merger between Standard Chartered and the Royal Bank of Scotland. I enclose a copy for convenience.

The Prime Minister wishes to reply to this herself and I would be grateful if you could let me have a draft - which will need to be prepared in consultation with the Scottish Office and the Treasury. It would be helpful to have this by Friday 3 July.

BF

I am sending a copy of this letter and its enclosure to John Wiggins (HM Treasury), Godfrey Robson (Scottish Office) and Francis Richards (Foreign and Commonwealth Office).

J.P. LANCASTER

John Rhodes, Esq.,
Department of Trade.

RH

26 June 1981

I am writing to acknowledge your letter of 24 June, which I have placed before the Prime Minister. A reply will be sent to you as soon as possible.

TPL

The Rt. Hon. Lord Barber, TD.



2

10 DOWNING STREET

PRIME MINISTER

Lord Barber has written complaining that Alex Fletcher is "going around expressing total opposition to the proposed merger between Standard Chartered and the Royal Bank of Scotland". He believes this is quite inconsistent with assurances which he was given by George Younger - that the Government would not have any objections to the merger.

You will need to reply to this yourself, and I will let you have a draft.

Must consult
with the Treasury ... π

26 June 1981

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mb

R25/6

Standard Chartered Bank Limited
10, Clements Lane, Lombard Street, London EC4N 7AB
Telephone 01-623 7500

Chairman
The Rt. Hon. Lord Barber

24th June 1981

Dear Manager,

I am sorry to trouble you with something unrelated to the important matters which are confronting the Government, and I hasten to say that, for obvious reasons, I do not expect any reply other than an acknowledgement from your private secretary that this letter has been received.

You will know that Standard Chartered has made an offer to acquire the Royal Bank of Scotland Group and that the matter is now before the Monopolies and Mergers Commission. Well before our offer was made, Sir Michael Herries, the Chairman of the Royal Bank of Scotland Group, had a number of discussions with George Younger, and at no stage was any objection raised to the offer being made. Following the publication of the offer, George Younger asked to see me and, while it was explained to me that it would be helpful if Standard Chartered could give certain assurances to meet Scottish sensitivity, he raised no objection to our proceeding.

The importance of the above is that Standard Chartered, operating in some sixty countries around the world, has always made it an absolute rule that we would not pursue an acquisition in any country if it were indicated to us that it would be against the wishes of the Authorities in that country. For instance, before we made an offer to acquire Union Bank, a major bank in

/California

California, our Managing Director and I went to Washington for the sole purpose of asking them quite informally whether they had any objection. If they had indicated that they would have preferred us not to proceed, we would have abided by their wishes.

If, before our offer to acquire the Royal Bank of Scotland Group was made, it had been indicated informally, either by the British Government or by the Bank of England, that they would have preferred us not to proceed, we would have dropped the proposal forthwith and that would have been the end of the matter.

I fully understand the reasons for the referral to the Monopolies and Mergers Commission, but what I find difficult to accept is the repeated reports, both oral and in the press (which I have good reason to believe are substantially accurate) that Alex Fletcher, Parliamentary Under Secretary at the Scottish Office, is going around expressing total opposition to the proposed merger between Standard Chartered and the Royal Bank of Scotland Group. In the light of Sir Michael Herries' and my discussions with George Younger, I must assume that Fletcher's remarks do not represent the view of the Government for, if they did, I cannot believe that such a view would not have been indicated to us.

I do not know whether the Scottish Office will be submitting evidence to the Monopolies and Mergers Commission but, if so, I hope that it will be consistent with the helpful attitude which George Younger adopted in his talks with both Michael Herries and myself.

/On an

On an entirely different topic, I was last week in Bahrain, where Chartered is the main bank, and had a long talk with the Prime Minister. He asked particularly that, when I next saw you, I should give you his personal good wishes.

I am sending copies of this letter to George Younger, and to Peter Carrington and John Biffen who also have a particular interest.

S,

Tang

The Rt. Hon. Margaret Thatcher MP
The Prime Minister
10 Downing Street
LONDON SW1

PRIME MINISTER

c.c. Mr. Ingham

We have already warned you about the Hong Kong and Shanghai bid for the Royal Bank of Scotland. This is now, of course, widely reported in today's Press.

The Governor rang me last evening to say that he was very worried about this latest bid, which is £50 million or so higher than the bid from Standard Chartered. The Royal Bank of Scotland's Board have already recommended that the Standard Chartered bid be accepted.

The Governor's concern stems partly from his dismay that there is a "contested bid", partly from the fact that he does not seem to want a foreign bank (even though the Hong Kong and Shanghai is technically British because it is based in a Crown colony) taking over the Royal - which accounts for nearly 50 per cent of the retail bank business in Scotland. He suggested that he might want to come in to see you about it.

Both bids are currently with the Director of Fair Trading. First indications are that he may not recommend a reference to the Monopolies Commission. However, the Secretary of State has power to override him and refer the bids if he so wishes. The Government could only prevent a take-over by the Hong Kong and Shanghai Bank if the Monopolies Commission so recommended. (In fact, the Government would be bound to accept such a recommendation.)

The FT this morning, interestingly, takes a pretty relaxed view as between the two contenders.

8 April, 1981.

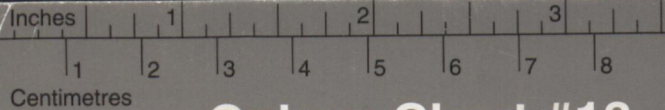
ms

12

Grey Scale #13



A 1 2 3 4 5 6 **M** 8 9 10 11 12 13 14 15 **B** 17 18 19



Colour Chart #13

Blue Cyan Green Yellow

