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Complaints of the PIBS Holders

Dear Mr Woods-Scawen,

As you are probably aware, we are representing the interests of the PIBS holders in your Society. I wish to make the following points:

1. The "corporate restructuring" involving the debt of the Society seems to have taken place behind closed doors and without any involvement of the PIBS holders. Although it was no doubt a critical matter to restructure the debt so as to meet the FSA's requirements in terms of capital adequacy, and there was apparently only a few days in which to achieve agreement, what seems to have happened is that a deal was arranged by your chief executive with about 15 of the main subordinated debt holders, and including changes to the terms of the PIBS, when holders of the latter were neither consulted nor advised that such discussions were taking place. Neither were they given the opportunity to be legally represented in those discussions, nor able to put their point of view. The end result is a deal that is prejudicial to the interests of the PIBS holders, as might be expected from the failure to involve them; the subordinated debt holders would have been promoting their interests with no countervailing arguments.
2. The Society appears to be claiming that it can change the basic terms of the PIBS as defined in the original prospectus, in other words the interest rate paid on the PIBS, at its pleasure by a simple board resolution. I do not believe that this is a correct interpretation of the original prospectus. Who would ever invest in an offering of a fixed interest security (which is what PIBS are) on that basis?

I was astonished to hear from the Chief Executive of your organisation at our recent meeting that he had not actually read the prospectus but was simply relying on advice from a third party. Well let me spell out the issue to you. Below is an extract from the relevant pages of the prospectus.

From the Special Conditions defined in pages 17 to 19 of the Prospectus:

“(3) (a) If, on any day within the 30 days preceding a scheduled Interest Payment Date, the Board:

(i) after consultation with the Supervisory Authority (as defined below) and having taken appropriate legal advice, is of the opinion that on the relevant date, the Society is, or payment of the relevant interest payment will result in the Society being, or there is a reasonable likelihood that payment of the relevant interest payment will in the foreseeable future result in the Society being, in noncompliance with any requirement relating to capital adequacy imposed on the Society by or pursuant to the Financial Services and Markets Act 2000, including any statutory modification or re-enactment thereof; and

(ii) passes a resolution cancelling or, as the case may require, reducing the interest to such extent as may be necessary to secure that, in the opinion of the Board (after consultation with the Supervisory Authority and having taken appropriate legal advice), such payment would not cause or contribute to such non-compliance, then the Society shall, as soon as practicable, give notice to all PIBS holders of such resolution in accordance with Condition 10(12), and such interest payment or part thereof, as the case may be, shall not be made. On the passing of a resolution cancelling or reducing an interest payment, each PIBS holder shall cease to have any right to the interest for that period so cancelled or, as the case may be, any interest other than the reduced amount payable in accordance with that resolution.

(b) If, in circumstances other than as set out in Condition 4(3)(a) above, on any day within the 30 days preceding a scheduled Interest Payment Date, the Board passes a resolution cancelling or requiring a reduction in the interest payable on such Interest Payment Date, then the Society shall, as soon as practicable, give notice to all PIBS holders of such resolution in accordance with Condition 10(12) and, subject to Condition 4(3)(c), such interest payment shall not be made. On the passing of any such resolution, each PIBS holder shall cease to have any right to the interest for that period so cancelled or, as the case may be, any interest other than the reduced amount payable in accordance with that resolution.

Whilst Condition 4(3)(b) entitles the Society, in its sole discretion, to cancel, in whole or in part, any scheduled interest payment as required by current policy of the Supervisory Authority, it is the Society’s intention not to cancel any part of a scheduled interest payment other than in the circumstances described in Condition 4(3)(a).”

The italics in the last paragraph are in the original – they were not added by me. The obvious intention of these clauses is to enable the Society to cancel or reduce the interest payment on the PIBS when the Society is in straightened financial circumstances, and it specifically refers to “capital adequacy” laid down by the FSA in Para 3 (a) (i). This is not unreasonable and is similar to the terms attached to many publicly quoted PIBS.

Even if the last paragraph (in italics) is not a specific and binding condition attached to the PIBS, the other terms certainly are and the combination clearly demonstrates that any cancellation or reduction in the interest can only be a temporary measure, and such was the original intention. This is also supported by the fact that the Society has to call a member’s meeting to review the matter on every occasion this is invoked (which I understand implies every six months).

The intention of the original prospectus is obviously being ignored if the Society attempts to interpret this in any other way. The paragraph in italics was clearly a part of the prospectus and was used to convince the original investors to subscribe for these PIBS. As a mutual association I find it astonishing that the Society should ignore the rights and interest of its own members in this regard (I believe the PIBS holders are members of the Society).

I would also point out that the restructuring of the subordinated debt and its conversion into PPDS (which has in fact taken place) means that the capital adequacy rules laid down by the FSA have in fact been met, so this could only have been used as a very temporary justification for reducing the dividend, if at all.

If the Society continues to ignore this matter and the rights of the PIBS holders to have a say in the future terms that apply to the PIBS (and the current proposals are clearly enormously damaging to their interests), then we will encourage the PIBS holders to take this matter up through legal channels. I also intend to raise this matter with the FSA, as I believe has already been done by Mr Morgan.

In addition I would point out that the Society surely has a moral, if not a technical legal obligation to enable the PIBS holders to be properly informed on this matter. A meeting of members is I understand planned and we request that a simple statement of our view, and that of many PIBS holders, be included in any material circulated to members on this issue.

Yours sincerely

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