

PRIME MINISTER

TAXATION OF GILT EDGED SECURITIES OF BUILDING SOCIETIES

The Treasury are proposing to tax the profits on the realisation of gilts by building societies as part of their trading profits rather than as capital gains. This follows advice they have received from Counsel. I suspect the findings of Counsel are not unwelcome to the Treasury who have been wanting to make this change for revenue reasons.

This will prevent building societies using capital gains on gilts to keep their margins low. This should not, however, seriously affect the flow of mortgages in the longer term as it represents on average a reduction in the margin of 0.1 per cent (the margin has been about 0.5 per cent). It could, however, be used as an excuse in the short term to delay a cut in the mortgage rate, though in practice this is unlikely to be the case as it is doubtful whether building societies will now make a move ahead of the Budget.

If the Chancellor goes ahead with a tax on the providers of credit, the building societies will not be able to complain as, notwithstanding the change in the treatment of capital gains which brings them into line with banks, their relative position will still be favourable as the credit tax will not apply to that part of their lending which attracts mortgage interest relief.

You might want to confirm with the Chancellor at your bilateral tomorrow that this measure will not have serious effects on the flow of mortgage finance.

15 February 1985