31 May 1984

PRIME MINISTER

BAD DEBTS AND BANKS

You raised the question this morning of how the banks accounted for bad debts in the UK, and the related question of the amount of tax they have to pay.

I have the accounts of Lloyds Bank to hand. Against their operating income of £1.8 billion in 1983, they made specific provisions of £143 million (related to identified advances that are going wrong) and a further £76 million pounds against general bad debts (part of a process of building up a reserve against bad advances that have not yet been identified).

After knocking off £219 million of provisions, they were left with an income of £1.57 billion. Their total operating expenses (staff, premises, equipment, etc) was £1.2 billion, leaving a profit before tax of £387 million. Lloyds also shared in the profits of associated companies, representing an additional £32 million.

On total pre-tax profits of £419 million, Lloyds had a tax bill that year of only £135 million - this represents, as always, a very low charge because of all the different ways of tax shelter.

Conclusion

UK banks do make provisions against specific and general bad debts. They write an advance down to its estimated realisable value as and when the normal banking relationship with the customer has stopped. Until breakdown, they credit interest on the advance to the profit and loss account, but make provision if they are worried about the possible breakdown in the customer relationship.

All banks have taken advantage of the facility to up their specific and general provisions, given the international uncertainties, and I can see no case for making the tax regime even more favourable towards them.

JOHN REDWOOD

LATAAX