

Pre-Budget Report 2009

PERSONAL & EMPLOYMENT TAXES

The Pre-Budget statement was one of enhanced political significance against the backdrop of a forthcoming General Election. It was widely expected that some measures would be taken against the banking sector. The scale and breadth of ramifications of the bank payroll tax provisions are, however, surprising. There were some significant revenue raising measures which have been highlighted below, together with measures put forward twelve months ago which will have a concertina effect of significantly higher taxes, now for city workers on bonuses and for the higher paid generally from April next year which we remind you of; as well as a surprise national insurance increase across the board.

Raising tax revenues is a high priority for the Chancellor and measures announced in the 2009 Budget and Pre-Budget Report appear to be targeting the highest earners.

Bank Payroll Tax

The bank payroll tax to be imposed is being applied against the banks themselves rather than the individuals. The levy will apply in relation to bonuses paid that are discretionary in nature, or are contractual bonuses not already in place at 9 December 2009. The bank payroll tax is applied to any bonus that exceeds £25,000 (whether in cash or other form) and there are a myriad of anti-avoidance measures that might be aimed at circumventing these rules. The charge is at 50% on the bonus proposed by the bank and no corporate tax relief will be available either.

The balance of the sum in the city employees' hands will be subject to current higher rate tax (and national insurance where applicable) at 41%. With employer national insurance levied, the share to the Treasury can exceed the level of the gross bonus proposed.

The technical notes seem to widen the headline of a change to a small select number of banks. The definitions seem to include financial trading companies in banking groups, a broader spectrum of investment businesses such as hedge funds and foreign banks operating through UK branches.

50% Tax Rate

From 6 April 2010 a new 50% tax rate will be introduced for those earning above £150,000 per annum. Dividend income which falls into the taxable band above £150,000 will be taxed at a new rate of 42.5%. When taking into consideration the 10% notional tax credit the effective tax rate will be 36.11% (currently 25%).

In addition the personal allowance will be eroded by £1 in every £2 of income above £100,000.

Pension Contributions

Higher rate relief for pension contributions will be removed from April 2011 for those with income in excess of £150,000. A Special Annual Allowance charge (SAA) was introduced to prevent individuals from making extra contributions in the years leading to the change, in order to secure the relief.

Broadly, the SAA works by applying a 20% charge on contributions in excess of £20,000 per annum. The 2009 Budget initially announced that the charge will apply to individuals with incomes in excess of £150,000 in the 2009/10 tax year or the two preceding years. However, this has now been reduced to £130,000 in the Pre-Budget Report.

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Inheritance Tax

The nil-rate band from April 2010 is to remain at £325,000. It was initially proposed that the band would be extended to £350,000.

Offshore Evasion

Individuals who fail to declare offshore income will face tough penalties for deliberate tax evasion. There will also be a new requirement to notify HM Revenue & Customs (HMRC) when opening offshore bank accounts in certain jurisdictions. In addition to the penalties for evasion, penalties will apply for failure to report offshore accounts. The combined effect of these penalties is reported to be up to 200% of the unpaid tax.

The 'New Disclosure Opportunity' gives those with undeclared offshore accounts a final opportunity to disclose offshore income that previously has not been reported, to pay the tax due, interest and a reduced penalty. The deadline for notifications is 4 January 2010. Individuals who do not make a disclosure can expect new legislation in the 2010 Budget to impose severe penalties.

CORPORATION & BUSINESS TAX

With the Chancellor primarily concerned with protecting tax revenues, there was very little introduced in the Pre-Budget Report to provide relief to businesses.

Corporation Tax Rates

These continue to remain unchanged. For companies with taxable profits of less than £300,000 the small company's rate remains at 21%, and the full corporation tax rate remains at 28% on taxable profits in excess of £1.5m. The effective marginal rate of corporation tax for taxable profits between £300,000 and £1.5m is 29.75%. The proposed increase in the small company's rate to 22% has been postponed until 1 April 2011.

National Insurance Contributions (NIC)

There is to be an increase in the rates of NIC to have effect from April 2011. An additional 1% will apply to the rates applicable to employers, employees and the self-employed. The rate of Class 1 (employee) NIC will be 12% and the Class 4 (self-employed) NIC will be 9%. Employers' NIC will increase to 13.8%. The additional rate of Class 1 and Class 4 NIC will increase to 2%.

The use of NICs as effectively a 'back door' income tax increase, is frustrating to US taxable persons because even if they were to have capacity it does not generally represent a creditable tax in the US.

Business Payment Support Service (BPSS)

The BPSS was introduced in the 2008 Pre-Budget Report, further extended in the Finance Act 2009, and it was confirmed in the Pre-Budget that this service is to remain available. The BPSS allows businesses facing temporary financial difficulties more time to pay their tax bills, including PAYE.

Capital Allowances/Tax Depreciation

The first year allowance introduced in the 2009 Budget is to end 31 March 2010 as initially planned. The recently introduced Annual Investment Allowance (AIA) allows for full deduction on the first £50,000 of expenditure on most plant and machinery and this is to remain in place.

VAT

As announced in the 2008 Pre-Budget Report, the standard rate of VAT will return to 17.5% on 1 January 2010. In addition for businesses in the flat rate scheme their applicable percentage will return to the rate in place prior to the reduction to 15% on 1 December 2008.

Patent Box

A 10% rate of corporation tax is to apply to income from patents from April 2013. This is in addition to current research and development tax credits available and is designed to make the UK a preferred destination for innovation companies.

Worldwide Debt Cap

The Worldwide Debt Cap was introduced in the 2009 Budget. The Cap is designed to restrict the deduction for finance costs in UK companies to the consolidated finance cost of the worldwide group. The Cap will not affect the majority of companies as there is a de minimus test in place. There will be some amendments in the 2010 Budget to ensure the Cap works as intended.

Taxation of Foreign Profits

The 2009 Budget announced from 1 July 2009 dividends from foreign companies will, in most circumstances, be exempt from UK corporation tax. There is to be a consultation proposing that profits (and therefore losses) of foreign branches will be exempt from UK corporation tax.

If you have any queries regarding this newsletter, please do not hesitate to contact your usual Frank Hirth representative.