



GES NewsFlash

United Kingdom – Pre-Budget Report 2009

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Summary

Following a steep fall in UK tax revenues, Alistair Darling outlined in his annual Pre-Budget Report how additional taxes will be levied on higher earners in order to narrow the gap between Government income and expenditure. The measures include:

- Doubling the previously announced Class 1 NIC increase from 0.5% to 1% for both employers and employees. As previously announced, the increase will apply from 6 April 2011.
- Imposing a special 50% banking payroll tax on bonuses, to the extent they exceed £25,000. A banker who expects to benefit from a bonus pool of £100,000 for 2009 would receive a net bonus of just £42,138 instead of £59,000; a reduction of 28.6% in take-home pay.
- Extending the pensions special annual allowance charge so that from 9 December 2009 any individual with income over £130,000 is affected if the employer contributes more than £20,000 annually.

Deloitte's View

Although positioned as provisions to balance UK finances, it is clear that the new measures will make the UK a less attractive place for higher earners.

Bank payroll tax

Responding to concerns over the levels of bonuses payable to bankers, the Chancellor announced a 50% levy on bonus payments in excess of £25,000.

Key features:

- 50% levy payable by banks on new bonus awards made from 9 December through to 5 April 2010;
- Payable on the excess of any award over £25,000;
- Levy will not qualify for corporate tax relief;

- “Bonus” includes discretionary cash awards and non regular benefits. Share remuneration is also caught based on its ‘cost’ at award (ignoring restrictions);
- The term ‘Banks’ includes companies mainly or wholly undertaking ‘Relevant Regulated Activities’ in the UK, e.g., accepting deposits, dealing in investments, arranging deals in investments, safeguarding and administering investments etc;
- Contractual bonus payments awarded prior to 9 December are specifically excluded;
- Non-residents and non-domiciliaries working in the UK are fully liable in the same way as UK residents.

Detailed anti-avoidance rules have been introduced to catch arrangements designed to avoid the levy through loans or other agreed deferrals.

Deloitte’s View

This levy will have a substantial impact on the payment of bonuses within the financial services industry. Some employers may decide to hold off awarding bonuses until after 5 April 2010 whilst others may choose to restrict bonus awards so that the effective cost of the levy is borne by the employee.

The levy will represent a significant additional cost for employers who tax equalise bonus payments and where there is no scope to either defer the award or have the employee bear the tax cost. The rules are widely drafted and would appear to catch share remuneration which may ultimately be forfeited. It is also unwelcome that the rules may be extended past 6 April 2010.

Increase to national insurance contribution rates and thresholds

The Chancellor announced an increase of 0.5% in the rates of national insurance contributions (NIC) payable by employees and employers, in addition to the 0.5% increase already stated in the 2009 budget, which will be effective from April 2011.

The main rate of Class 1 NIC for employees from April 2011 will therefore rise to 12%, with 2% payable on amounts above the upper earnings limit. The main rate of Class 1 NIC for employers will increase to 13.8% (rather than the 13.3% previously announced) on earnings above the secondary threshold. The increase will also apply to Class 1A and Class 1B NIC rates.

There will be no change to the thresholds and rates of NIC payable by employees and employers for the 2010/11 tax year, with the exception of small increases to the lower earnings limit. From April 2011, the primary threshold and lower profits limit will be raised by an extra £570, over and above the increase announced in the last Budget. This is to ensure lower earners are not adversely affected by the increased

Deloitte's View

The additional increase to NIC rates is not unexpected, given the level of national debt. Clearly employers will not welcome the additional NIC costs from 2011. However, we welcome the increase to the primary threshold and lower profits limit to assist lower earners.

Pensions: special annual allowance charge

Changes announced in the April 2009 Budget, which will apply from 6 April 2011, will remove higher rate income tax relief for pension contributions for those with incomes in excess of £180,000, and taper it away for those with incomes between £150,000 and £180,000.

In order to prevent individuals from pre-empting this measure by increasing their normal pension savings before the change becomes effective, 'anti-forestalling' measures were introduced with effect from 22 April 2009; to claw back higher rate tax relief where individuals increase their pension contributions above the amount they were previously paying on a regular basis. The claw back is made by way of a special annual allowance charge of 20% in the current tax year and 20%-30% next year.

Effective from 9 December 2009, the relevant income threshold at which the anti-forestalling rules apply is reduced from £150,000 to £130,000 per annum. However it will not apply to those with an existing pattern of normal ongoing regular pension savings (ie., made at least quarterly), provided these continue to be made at least quarterly and the rate at which they are paid is not increased. Employer contributions are not included for this purpose, but will be from 5 April 2011, unless taxable income, after adding back the individuals charitable and pension contributions, is £130,000 or less.

Pension savings made on or after the Pre-Budget Report in excess of protected amounts will be subject to the special annual allowance charge if the individual's total pension savings for the year (including those made on their behalf, eg by an employer) exceed £20,000 (or, in some cases, £30,000).

Anyone now caught by the rules, having previously been unaffected, will not be charged in respect of any irregular contributions or other non-protected pension savings made before today. However these will eat into their £20,000 (or £30,000) special annual allowance.

Deloitte's View

The Government expects that around 98% of pension savers will not have their

tax relief restricted by this change. However for the 2% who are affected it is an unwelcome complication. They will now have to get to grips with these convoluted rules for the rest of this tax year and next.

Anyone starting pension savings on or after 22 April 2009, whose income was below the £150,000 threshold and who therefore was not caught by the anti-forestalling rules as originally enacted, may be caught if they save irregularly and postponed their decision on pension savings until after today's Pre-Budget Report.

Foreign service relief for overseas pension lump sums

Extra-statutory concession A10 will be legislated following a consultation period. The concession provides relief from UK tax on certain lump sums paid from foreign pension plans where the member has spent at least part of his employment with that employer in 'foreign service'.

Payments will be totally exempt from income tax where an employee has 'substantial' foreign service (for example at least 75% of total service). Where 'substantial' foreign service does not apply, income tax relief is allowed in the proportion of foreign service to total service.

The proposal will see the relief, which is currently available on a concessionary basis, formalised into legislation. Broadly, the relief remains in its current guise, although relief will no longer be allowed where payments are made to companies, trusts or certain dependents.

Deloitte's View

Following HMRC's review of its extra-statutory concessions last year, many feared that ESC A10 would be significantly restricted. This would have had a significant impact on UK-resident members of foreign pension plans. Despite the fact that the relief will be narrowed, the measure is very welcome, as it ensures this valuable relief from UK tax for lump sums should remain available for the foreseeable future.

Cars

The company car taxable benefit arising for an employee is based on the list price of the car multiplied by a percentage – with the relevant percentage depending on the car's CO2 emissions. Currently the lowest rate is 15% except if the car is a 'Qualifying Low Emission Car (QUALEC)' and has emissions of no more than 120g/km of CO2 – in which case the percentage is 10%. From 6 April 2012, QUALECs will no longer exist as a separate category but the lowest 10% rate will be available for cars with emissions of no more than 99g/km of CO2. The rate would be 11% for cars with emissions of 100g/km of CO2 and the bands increase at 1%

intervals for each additional 5g/km of CO2.

Similarly, where an employee with a company car is provided with private fuel, the taxable benefit is based on the relevant percentage multiplied by a specified figure. That figure is to be increased from £16,900 to £18,000 with effect from 6 April 2010. Where an employee with a company van is provided with private fuel, a flat rate taxable benefit of £500 arises. This figure is also to be increased from 6 April 2010 to £550.

The percentage figure used to calculate the benefit in kind of an electric car/van, or any free fuel associated with the electric car/van, will be reduced to zero per cent from 6 April 2010 for five years. As such, provision of an electric car or van during this period is effectively a tax-free benefit.

Subject to confirming compatibility with the State Aid rules, legislation will be introduced to provide a 100% first-year allowance for business expenditure on new (not second hand) electric vans. These allowances will apply to acquisitions made from April 2010.

Deloitte's View

The exemption from income tax and NIC for electric vehicles should prove a significant incentive for employers to provide these vehicles and in turn encourage a wider variety of such models to be made available in the UK. This, in conjunction with the tightening of the emissions thresholds for benefit in kind tax and the increase in the fuel benefit tax, continues the trend by Government to use the tax system to encourage businesses and drivers to select greener, low emission vehicles.

We believe these changes are positive news and should provide a further incentive for employers to assess their current fleet; the policy and its true after tax cost and ensure they maximize the use of the tax incentives provided by the Government.

Staff canteens

HMRC have proposed changes to the tax exemption for free or subsidised meals provided in a canteen or otherwise on an employer's premises, where this is provided 'in conjunction with' salary sacrifice or flexible benefit arrangements, and the value of the benefit provided 'is commensurate with' the salary sacrificed. From 6 April 2011, in such circumstances, the normal rules for taxing employer provided benefits will override the exemption.

The value of such a benefit under the normal rules would be based on the cost of providing the meals, not their sales price, whereas the salary sacrificed is typically

based on sales price. This means that tax and NIC savings can still be achieved on the difference. However this comes at a price. From 6 April 2011, employers wishing to provide such a benefit using salary sacrifice or flexible benefits, will find themselves with a P11D reporting obligation and the task of having to calculate the benefit in kind for each employee based on the 'cost of provision' of the meals with which they are provided.

Deloitte's View

HMRC have long held that this benefit has been exploited in a way that was never intended. Nevertheless, the proposed new legislation vindicates our long held position that the canteen exemption is in fact effective when used in this way. We also welcome HMRC's targeted approach to this particular benefit rather than taking a sledge hammer to all salary sacrifice schemes generally.

Offshore account disclosure

New rules were proposed for the detection and punishment of tax evasion in relation to offshore funds. HMRC have already obtained significant data on offshore accounts, largely through information notices served on banks. This data will be used to identify cases where offshore funds taxable in the UK have not been disclosed to HMRC, with penalties of up to 100% of tax underpaid.

UK domiciled taxpayers will also be required to notify HMRC within 60 days of opening a new overseas bank account in jurisdictions without information exchange agreements with the UK or where the account balance exceeds £25,000. The notification requirements are not expected to apply to non-domiciled individuals filing on the remittance basis, however, those who fail to declare an account would potentially face penalties of up to 100%, in addition to the penalties for non-disclosure of income. The Government's intention is that these new penalties would apply for tax periods commencing from 1 April 2011.

Deloitte's View

The introduction of enhanced penalties for the non-disclosure of offshore funds is a clear indication of the Government's drive to counter tax evasion and bolster depleted tax revenues.

The proposals will also be of particular interest to banks operating in jurisdictions that do not have automatic exchange of information with the UK. At present, these are largely limited to those countries which have fully implemented the European Savings Directive.

Although the rules do not apply to those filing on the remittance basis, those switching to the arising basis will undoubtedly have a reporting requirement. It

is not clear how the time limits for notification will be applied in these cases.

This will cause additional complexity for non-domiciliaries in organizing their UK tax affairs.

Extended tax disclosure rules for employment tax schemes

The Government is proposing a significant extension to the tax disclosure rules. Draft proposals would extend the current disclosure 'hallmarks' to include almost any employment tax planning arrangement, or any arrangement that substitutes capital for income. Approved share and pension scheme arrangements are accepted. In addition, the Government favours requiring promoters to provide a list of clients to whom scheme reference numbers are supplied and a shorter period for disclosures to be made.

Subject to consultation, the new rules will be legislated in Finance Bill 2010.

Deloitte's View

These changes would require almost routine disclosure of employment tax planning, although whether that would inevitably lead to increased anti-avoidance legislation remains to be seen.

People to Contact

If you have any questions concerning the issues in this GES NewsFlash, please contact one of the tax professionals as follows:

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