

# Comment

## Further reflections on the Budget Will Morris, Chair of CBI Tax Committee



The emergency Budget contained two major reforms of particular importance to business: corporate taxation and the tax policy-making process.

### Corporation Tax (CT) reform

The Government's five-year roadmap for reform of the UK's corporate tax regime aims to create the most competitive CT system in the G20, and includes a phased reduction in the headline rate to 24% over the four years from April 2011.

Particularly welcome are both the small net reduction in the effective CT rate over this period, and the deferral of capital allowances reductions to the Financial Year 2012.

The Government's CT reform objective is a broad tax base, a low rate and a more territorial tax system. We look forward to seeing more details in the comprehensive document promised for later in the year.

Significant further restriction of tax relief for economically justified interest would limit businesses' ability to adopt optimal commercial financial structures and undermine competitiveness. However, even in this potentially difficult area we are encouraged by the Government's commitment to full and extensive consultation with business.

The commitments to consult on the Controlled Foreign Company (CFC) rules, and to enact interim measures in Finance Bill 2011 ahead of more substantive changes the following year, are also welcome. Interim and permanent changes must be co-ordinated, but interim action on, for example, a motive test, would be very helpful. In the longer term the CFC system should reflect the core principle that the regime is only intended to catch income artificially diverted from the UK.

We strongly believe that the roadmap reforms should be treated as an overall package, rather than a set of individual measures.

### An improved policy making, legislative and administrative process

We also welcome publication of the Treasury/HMRC Discussion Document 'Tax policy making: a new approach', which reflects the radical new approach to tax policy-making long sought by the CBI. A planned and integrated long-term strategy is needed, with the central objective of improved UK competitiveness from a business perspective.

Achieving greater certainty and stability of the CT regime will require major improvements to the process of making, legislating and enforcing tax law. The policy-making process in HMT and HMRC following the O'Donnell review needs to be rebalanced. Parliamentary scrutiny can also be made more effective by:

- removing most corporate tax legislation from the annual Finance Bill to provide greater time for examination
- establishing joint committees with separate staff, taking evidence direct from business
- allowing for independent post-implementation reviews.

Early, open and consistent consultation is essential to prevent unintended consequences and excessive compliance burdens. Finally, business involvement in the proposed Office of Tax Simplification would provide relevant commercial experience.

## Bank levy and more bonus scrutiny Helen Buchanan, Tax Partner, Freshfields Bruckhaus Deringer



The benefit of lower corporation tax is tempered for banks by the new bank levy. As trailed in the Coalition Agreement, the bank levy will be imposed from 1 January 2011, raising £2 billion a year. The stated aims are to encourage banks to move to less risky, longer-term funding and to ensure a 'fair contribution' to the UK financial system, reflecting the risks they pose. The levy is not an insurance fund and proceeds will not be ring-fenced – so can be spent.

Details are sketchy. We are told the levy will be imposed on consolidated balance sheets of UK banking groups and building societies; aggregated subsidiary and branch balance sheets of foreign banks and banking groups operating in the UK; and balance sheets of UK banks in non-banking groups. No definitions are given – the bank payroll tax definitions may be recycled, leaving winners and losers.

The levy applies if relevant aggregate liabilities exceed £20 billion. Tier 1 capital, insured retail deposits, sovereign debt repos and some retail insurance liabilities are excluded but net derivative liabilities are included.

## An interesting question is whether / how banks will pass on the cost. Heavy lobbying is expected over the summer

For bank branches, branch liabilities and Tier 1 capital will be calculated using the capital attribution methodology used for UK corporation tax purposes. The levy is 0.04% of relevant liabilities for 2011 and 0.07% thereafter. The rate is halved for wholesale funding liabilities with a maturity of greater than a year, which may increase banks' appetite for wholesale funding. Again, definitions will be important and anti-avoidance rules will be included.

The levy is not deductible for corporation tax and a big question is whether overseas bank levies (notably in France, Germany and the US) will be creditable. Another interesting question is whether / how banks will pass on the cost. Heavy lobbying is expected over the summer. Although bank payroll tax has not been extended, bonuses remain under the spotlight. Taking its lead from the International Monetary Fund, the Government will explore a 'financial activities tax' on profits and remuneration, in conjunction with other countries ('FAT cat' headlines are inevitable).

Consultation on a 'remuneration disclosure code' is also announced and the FSA is asked to consider new factors in reviewing its remuneration code. Of the other many consultations announced, ones for banks to watch include a consultation on UK corporation tax reform and competitiveness (including a new more territorial system for branch taxation from 2011 and new controlled foreign company rules from 2012), a(nother) review of the non-domicile rules and a review on tax policy making, including a possible general anti-avoidance rule.

In brief: lots to watch but light on detail.