Bank Payroll Tax – Impact on Executive Remuneration and Employee Share Plans – Some Q&As

What is Bank Payroll Tax?

Bank Payroll Tax ("BPT") is a levy being imposed on certain elements of remuneration provided by banks, building societies and certain financial services businesses between 9 December 2009 and 5 April 2010. It will be payable by the employer (not the employee) at a rate of 50% on any relevant remuneration paid to employees in excess of £25,000. The application of BPT will lead to remuneration within the scope of the charge being subject to tax at an effective rate of 103.8%. Crucially, it appears that the draft legislation applies to "standard" executive share plans and not just "bankers' bonuses".

Which companies are subject to BPT?

One of the unexpected elements of the draft BPT legislation is that its scope is wider than was anticipated. Financial services companies generally – including asset managers and insurers – will therefore need to carefully review the definition of a "taxable company" contained in the draft legislation so as to establish whether or not they, or any part of their group, will be subject to BPT.

Which elements of remuneration are subject to BPT?

Any element of remuneration taxable as earnings or which constitutes a benefit provided by reason of employment will be subject to BPT.

That benefit does not need to be subject to income tax in order for a BPT charge to arise.

This means that, as expected, annual bonuses will be within the scope of the charge to BPT.

However, what was unexpected is the fact that it appears that the operation of standard employee share plans (other than HMRC approved all-employee plans) could also give rise to a charge to BPT. This would appear to include the grant of awards under standard long-term incentive plans such as performance share plans, deferred share bonus plans and share matching plans, as well as the grant of options under both approved and unapproved executive share option plans. In addition, it has been suggested that the vesting of awards and/or the exercise of options could also be within the scope of the charge to BPT.

As such, if you are subject to BPT on the basis of the draft legislation, you should speak to your usual Hewitt New Bridge Street consultant to seek specific advice prior to the grant of any further share plan awards and/or in advance of the vesting of existing awards.

Presumably the broad scope of the legislation in terms of the types of companies and remuneration covered was unintended and the Government will be clarifying the position?
This remains to be seen.

We have sought clarity from HM Revenue & Customs ("HMRC") as to the application of the BPT rules to standard employee share plans. We understand that HMRC will shortly be publishing some "Frequently Asked Questions" in connection with the draft legislation.

We are also aware that both the Association of British Insurers and the Investment Management Association are lobbying the Government for clarity as to which companies should be subject to BPT.

Will the acceleration of the payment of bonuses to minimise the impact of the proposed new 50% income tax rate be caught?
Yes. Affected companies who have been planning to accelerate the payment of bonuses so that the payment occurs before 6 April 2010 (when the new 50% income tax rate is introduced for those with earnings in excess of £150,000 per annum) will need to consider whether or not any amounts received before 6 April 2010 as a result of such acceleration could expose the company to a charge to BPT.

Are there any ways in which a charge to BPT can be avoided?
The draft legislation contains both general and specific anti-avoidance provisions which are likely to make it difficult for affected companies to avoid a charge to BPT. As well as containing provisions which are designed to ensure that arrangements entered into in order to avoid BPT remain within the scope of the charge, the legislation also specifically states that bonuses provided in the form of loans or via an employee benefit trust will be subject to BPT. These provisions would appear to be designed to ensure that rewards provided through sub-trust/family benefit trust structures, in which interest has increased since the proposed new 50% income tax rate was announced, are subject to BPT.

What if we just agree to defer the payment of bonuses until after 5 April 2010?
Deferral of payment beyond 5 April 2010 is still likely to lead to a charge to BPT. In addition, if the employee has earnings in excess of £150,000 per annum any such deferral will also have the effect of increasing the income tax liability in respect of the relevant bonus from 40% to 50%.

What if the employee agrees to sacrifice their annual bonus into pension?
Any such bonus sacrifice arrangement entered into between 9 December 2009 and 5 April 2010 will still be caught by the BPT legislation and, consequently, a charge would still arise.

Are any elements of remuneration excluded from BPT?
Salary, wages and regular benefits are all excluded from the scope of BPT, as are awards made under HMRC approved all-employee share plans.

More importantly, any amounts due to be paid pursuant to contractual obligations which existed before 9 December 2009 are exempt from BPT, meaning for example that amounts paid pursuant to guaranteed bonus arrangements which were entered into before that date will be exempt from BPT.

Does this really mean that affected remuneration will effectively be taxed at more than 100%?
Yes. Any remuneration subject to BPT will be taxable at an effective rate of 103.8%. For example, if £100,000 of an employee's bonus is subject to BPT the total tax payable would be:

Income tax and employee National Insurance	= £41,000
Employer National Insurance	= £12,800
BPT	= £50,000
Total tax payable	= £103,800
Effective rate of tax	= 103.8%

Does BPT apply in respect of all employees?

No. BPT only applies in respect of employees who are UK tax resident or who perform their duties in the UK if, in either case, the duties of such employees are wholly or mainly concerned with money lending or certain regulated activities under the Financial Services and Markets Act 2000.

Will affected companies be able to claim a corporation tax deduction in respect of any BPT paid?

No. Unlike other employee remuneration costs, such as a bonus itself and the related employer National Insurance, affected companies will not be able to claim corporation tax relief in respect of any amounts of BPT paid.

For what period will BPT apply? Is it genuinely a one-off charge?

BPT will apply to any relevant remuneration provided between 9 December 2009 and 5 April 2010. HMRC has, however, indicated that it may extend the application of BPT beyond 5 April 2010 in certain circumstances (potentially until the relevant provisions of the Financial Services Bill come into force).

When must any amount of BPT due be paid – does it have to be paid under PAYE at the same time as any relevant income tax and National Insurance?

No. Any amounts of BPT payable become due on 31 August 2010.

Are there any other compliance requirements?

Affected companies will be required to report details of all bonuses in excess of £25,000 awarded during the period 9 December 2009 to 5 April 2010, regardless of whether or not they believe that BPT applies to them. This appears to be an attempt by HMRC to ensure that compliance or otherwise with the new provisions can be determined by HMRC and not by companies themselves. In addition, companies will be required to keep full records of all bonus payments in excess of £25,000 awarded during the relevant period, together with any evidence necessary to determine whether or not they are subject to BPT. The submission of any incorrect returns, a failure to retain the relevant records or a failure to submit returns by the relevant date will lead to penalties being imposed.

If you would like any further advice in connection with Bank Payroll Tax please contact your usual Hewitt New Bridge Street consultant or telephone Neil Sharpe, David Tuch or Matthew Findley on 020 7939 4000.