AFME Statement Re: Bonus Tax

The bonus tax is ill conceived – it threatens the UK’s future as the world’s leading international financial centre, harming an important sector of the UK economy and leading to a reduction in employment in the industry. This will suppress growth, delay economic recovery and reduce overall tax revenues, putting further pressure on the national debt and ultimately hurting the UK taxpayer.

The tax threatens the UK’s future as the world’s leading international financial centre. A reduction in the economic contribution of the financial services industry to the UK economy would slow the recovery of recent taxpayer investment in the sector, have a negative impact on long term economic growth, and exacerbate concerns about the long term health of UK public finances.

Legal certainty and regulatory stability are basic considerations for businesses when deciding on whether to enter, expand, or remain in a country. A government that unilaterally and without consultation levies punitive taxes on discrete constituencies to achieve political outcomes will gain a reputation for unpredictability that will deter potential newcomers or new investment.

Approximately 80% of the business conducted by financial services firms in the UK comprises of services offered to non-UK residents,1 business that could be relocated to other jurisdictions. The industry is highly mobile, and institutions and individuals (including the many financial services sector employees who are non-UK nationals) may relocate elsewhere, as recent announcements suggest.

Any revenue resulting from the tax has the potential to be hugely outweighed by the loss of future revenue that would result from an adverse effect to the UK’s financial sector. Financial services firms represent approximately 9.2% of UK GDP,ii and contributed 13.9% per cent of the total tax revenue to the UK for FY ending Mar 2007.iii

It is a concern that a thorough impact study of this adverse change to the taxation environment for such a crucial business sector does not appear to have been carried out.

The tax furthers systemic risk, which is inconsistent with the G20 implementation principles and undermines what has been learned from the crisis:

- The exemption of guaranteed bonuses and bonuses derived from formulae encourage a migration to bonus structures that the G20 explicitly criticised as inconsistent with sound risk management.
- Introduction of international inconsistency represents unilateral break from G20 agreements to implement a principles-based, integrated global framework.
- Resulting distortions in labour market (e.g., flight toward hedge funds) will encourage the type of concentration and concomitant systemic risk that G20 principles were intended to avoid.

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1 According to HM Treasury report, overseas financial institutions play an important role in the UK financial system. Six hundred overseas financial institutions operate in the UK, 420 of them European. London manages 50 per cent of the world’s sovereign wealth fund assets.

ii In 2008, the financial sector contributed 9.2% of GDP and the real estate sector 23.6% of GDP. Assuming a multiplier of 1.25x, a 10% reduction in the financial sector could induce a 1.2% loss in GDP.
The best comprehensive estimate of the UK financial industry contribution to Treasury's revenue has been done in a PwC report commissioned by the City of London (published Dec-08, full report available at www.cityoflondon.gov.uk/researchpublications). The report estimates that for the FY ending Mar2007, UK’s financial services contributed £67.8bn to UK government taxes in FY end March (13.9% of total). The revenue includes £12.2bn corporation tax (27.5% of total), £10.8bn NIC and £25.7bn in taxes related to employment. PwC further estimates that after accounting for the impact of the downturn, total tax contribution for FY 2008-09 could reduce to £58bn or 11.9% of total government receipts.

The Centre for Economic and Business Research (CEBR) has similar estimates to PwC for 07/08 and 08/09 and estimates the financial sector contribution to revenues in 09/10 to amount to £39bn (or 8.4% of total tax take).