

September 30, 2010

Comments on HM Treasury's Bank levy

Japanese Bankers Association

The Japanese Bankers Association is an organization that represents the banking industry and is comprised of 139 domestic banks and 45 foreign banks operating in Japan.

We, the Association, would like to express our gratitude for this opportunity to comment on the consultation document, "*Bank Levy*" released on July 13, 2010 by HM Treasury.

We hope that our comments below will further assist HM Treasury in its efforts to formulate the rules.

I. General Points

In view of the fact that the UK is home to an international financial market, this proposal is thought to have a great impact on discussions regarding the tightening of international regulations. With the deliberations on increasing the quality and quantity of bank capital by the Basel Committee on Banking Supervision underway, we are concerned that the build-up of bank capital will be delayed as a result of the implementation of the bank levy.

Furthermore, when applying the bank levy to the UK branches of foreign banks, we believe that sufficient consideration should be given, in accordance with the main purpose of the levy, to the degree of impact it may have on the British financial system and real economy, rather than introducing it in the same way as it is applied to UK banks. It is inappropriate to apply the bank levy under the same conditions for UK banks as for UK branches of foreign banks, which are unlikely to receive support from the British government during a liquidity crisis.

In formulating the framework of the bank levy, we ask that HM Treasury discusses adequate transition measures, etc. after taking into consideration the implementation dates of the abovementioned tightening of capital requirements, so as not to negatively affect the build-up of bank capital. Furthermore, during implementation, we request that an excessive administrative burden be avoided. Overall, we appreciate your consideration to secure level playing field for foreign banks and UK banks under the new Bank Levy.

II. Specific Points

Implementation date (p. 5 of original text)

Introduction of this proposal is planned for January 1, 2011, but we are concerned that the preparation period is too short. Currently, there are many uncertainties, such as those regarding deductions and the computation method. After these are finalized, banks would need enough time to take measures, such as data extraction, exclusion of deductions and tax calculation, and develop a system infrastructure. We therefore request that HM Treasury discloses information concerning the direction following the consultation at an early stage and provides ample preparation time.

Non-deduction of payment of the levy (p. 7 of original text)

The fact that payment of the bank levy “will not be deductible for Corporation Tax” will place a great tax burden on banks. Payment of the bank levy should be deducted from the computation of taxable income for the purposes of Corporation Tax.

Definition of banks and banking groups (p. 9 of original text)

We would like to confirm that the definition of a “banking group” subject to the levy refers only to groups that are engaged in banking operations, and that groups which have banks as a part of their business, in other words, “financial holding companies” will not be included. In particular, we would like to confirm whether in the case of banks which although they exist under the umbrella of a financial holding company are independent entities operating their own individual businesses, with separate branches or subsidiaries of the bank in the UK, they will each be taxed on an individual banking group basis.

Aggregation (p. 10 of original text)

The consultation document proposes that either the accounting standards of IFRS or UKGAAP must be used to determine taxable liabilities. However, many of the foreign banks do not prepare aggregate balance sheets of only entities residing in the UK. It would be extremely burdensome to prepare an aggregate balance sheet under the IFRS or UKGAAP for all entities in the UK solely for bank levy purposes. Furthermore, we feel that this is highly unfair compared to UK banks, which can use their original consolidated balance sheets for that purpose. Therefore, our request is that measures to reduce the administrative burden of foreign banks to prepare an aggregate balance sheet be considered, for example, by exempting entities under a certain size.

Calculation of branch liabilities (p. 11-12 of original text)

Intra-entity funding is a vital and stable funding source for branches of foreign banks, however, the framework is such that they are not deductible from taxable liabilities. Some UK branches of foreign banks function as fund procurers for their other bases in other European countries as well, serving as an efficient and stable funding system. For such financial institutions, the bank levy would become an economic burden in the face of their optimum funding system, which would oppose the levy's original objective of financial stabilization.

On the other hand, the new liquidity regulations of the UK's FSA set forth Liquidity Modification which permits a framework for an entire bank to secure sufficient and stable liquidity. We would like HM Treasury to permit full deduction of intra-entity funding for financial institutions whose application for such a Liquidity Modification has been approved. Furthermore, we ask that net liabilities—resulting from the offset of assets and liabilities within the group—be the only object of taxation because intra-entity funding conducted for the purpose of providing funds to offices of the same entity in other countries are not funds for UK businesses.

Threshold (p. 13 of original text)

In the case where total liabilities exceed 20 billion pounds, we think that, rather than the “threshold” method, where a bank levy is placed on the entire amount, the “allowance” method, where a bank levy is placed on only the excess amount, is more appropriate. With the current proposal, not only is the burden great, but it could work as an incentive for banks to restrict liabilities to less than 20 billion pounds and, as a result, we anticipate various harmful effects, such as the inability to respond to a sudden demand for funds, even for healthy businesses.

The Levy Base (p. 15 of original text)

For a foreign exchange transaction conducted with a counterparty with an ISDA Master Agreement (CSA Agreement) and which is settled through CLS, there is no credit risk or settlement risk and exposure is very small. As such, it is a low risk transaction and so we think that it should be added to the items not subject to the taxation.

Tax computation / Payment of the Levy (p. 20-21 of original text)

Even if the threshold is not reached and the bank levy is clearly not to be applied, depending on deduction items, preparing attachments of corporation tax returns or

submitting a return of the bank levy will create an excessive administrative burden. If calculations are made in line with the corporation tax system, which is a self-reporting system, and it is found that the bank levy does not apply, we would like to confirm that there will be no requirement to write out the computation method on the tax return or attach a return of the bank levy.

Furthermore, in line with the corporation tax system, the bank levy is to be paid through Quarterly Instalment Payments (QIPS). However, since the computation method of the bank levy differs from that of corporation tax, and as the targeted banking groups vary in terms of size and characteristics, flexibility in payment methods should be allowed. Therefore, we think the option of making a one-time payment after the end of an accounting period should be provided.

Double taxation (p. 22 of original text)

If a similar bank levy is introduced in another country, the same balance sheet can be liable to double taxation. Under current tax treaties, it is possible to avoid double taxation in relation to income and profits. In contrast, taxes on balance sheets, such as the bank levy, are not covered by tax treaties. Measures to avoid double taxation are presently not being discussed in the international arena, and so introduction of a bank levy by the UK poses a problem. We therefore strongly request that construction of a framework to avoid double taxation be established before the bank levy is introduced.