



# COUNTRY PROFILE, NORTHERN IRELAND

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## Introduction and Country Background

Northern Ireland has no official language; the use of English has been established through precedent

### Key Facts

|                         |   |
|-------------------------|---|
| Capital - Major Cities  | Belfast   |
| Area                    | 14,139 km <sup>2</sup>  |
| Population              | 1.759 million (12-2007)   |
| Languages               | English (Irish and Ulster Scots are officially recognised minority languages)       |
| Currency                | GBP (Pound Sterling)  |
| Telephone Code          | +48   |
| National/ Bank Holidays | 2009 – 1, 2* Jan; 10, 13† Apr; 4, 25 May; 3*, 31† Aug; 30* Nov; 25, 28 Dec          |
| Bank Hours              | 9:30-15:30 (some till 17:30) Mon-Fri, some branches open Saturday mornings          |
| Business Hours          | 9:00 - 17:30 (some till 20:00 or later) Mon-Fri<br>10:00-16:00 (or 11:00-17:00) Sun |
| Stock Exchange          | London Stock Exchange   |
| Leading Share Index     | FTSE 100  |
| Overall Share Index     | FTSE All-Share Index  |

Northern Ireland is the smallest of the four Home Nation's economies of the United Kingdom

### Economic Performance (UK)

|                                      | 2005   | 2006   | 2007   | 2008   |
|--------------------------------------|--------|--------|--------|--------|
| Exchange Rate - GBP/EUR <sup>1</sup> | 0.6836 | 0.6816 | 0.6840 | 0.7944 |
| Exchange Rate - GBP/USD <sup>1</sup> | 0.5498 | 0.5434 | 0.4994 | 0.5973 |
| Money Market Rate (%) <sup>1</sup>   | 4.67   | 4.73   | 5.80   | 5.16   |
| Consumer Inflation (%) <sup>2</sup>  | 2.0    | 2.3    | 2.3    | 3.8    |
| Unemployment Rate (%) <sup>3</sup>   | 4.8    | 5.4    | 5.4    | 5.4    |
| GDP (GBP billions) <sup>4</sup>      | 1,195  | 1,229  | 1,266  | 1,279  |
| GDP (USD billions) <sup>5</sup>      | 2,174  | 2,262  | 2,535  | 2,370  |
| GDP Volume Growth (%) <sup>2</sup>   | 2.1    | 2.8    | 3.0    | 1.0    |
| GDP Per Capita (USD)                 | 36,094 | 37,363 | 41,670 | 38,838 |
| Current Account (% of GDP)           | -2.6   | -3.4   | -3.8   | -3.6   |

Sources: International Monetary Fund, UK National Statistics, Bank of England, European Central Bank

<sup>1</sup> Period average

<sup>2</sup> Year on year

<sup>3</sup> Per annum (seasons adjusted)

<sup>4</sup> Constant prices: index, 2000=100

<sup>5</sup> Per average exchange rate

The Northern Ireland seasonally adjusted unemployment rate was 4.3% ending November 2007.

The restoration of the devolution of

### Government

powers to the Northern Ireland Assembly occurred in March 2007 ended the longest period of its suspension since its inception

#### Legislature

Northern Ireland is a constitutionally distinct region of the UK with 12 representatives in the British House of Commons. The terms of the Government of Ireland Act in 1920 established a semiautonomous government – the Northern Ireland Assembly. In 1972, however, after three years of violence between Protestants and Catholics that resulted in more than 400 dead and thousands injured, Britain suspended the Ulster Parliament.

As a result of the “Belfast Agreement” – also known as the “Good Friday Agreement” of 1998, a new coalition government was formed on December 2, 1999, with the British government formally transferring governing power to the Northern Irish Parliament. David Trimble, Protestant leader of the Ulster Unionist Party (and winner of the 1998 Nobel Peace Prize), became first minister. The government has been suspended four times since then, the longest such period being from October 14, 2002 to May 7, 2007. The St Andrews Agreement (Northern Ireland Act 2006) provided for a Transitional Assembly to take part in preparations for the restoration of devolved government in Northern Ireland in accordance with the St Andrews Agreement.

#### Northern Ireland Assembly

The Assembly is a unicameral body consisting of 108 members from 18 member constituencies, elected by proportional representation. The Assembly is based on the principle of power-sharing, in order to ensure that both communities in Northern Ireland (Unionists and Nationalists) participate in governing the region.

An election to the then-suspended Northern Ireland Assembly was held on 7 March 2007. Secretary of State for Northern Ireland, Peter Hain signed a restoration order on 25 March 2007 allowing for the restoration of devolution at midnight on the following day. The two largest parties following the election, the Democratic Unionist Party (DUP) and Sinn Féin, agreed to enter power-sharing government together, and power was eventually restored on 8 May 2007.

The First Minister is elected by the Assembly on a joint ticket with the Deputy First Minister. Their joint nomination must obtain an overall majority in the Assembly along with a majority of both designated nationalists and unionists. This dyarchy was created to enable the leaders of the main unionist and nationalist parties to work together as a team jointly representing both communities.

First Minister: Peter Robinson (Democratic Unionist Party) since 5 June 2008

Deputy First Minister: Martin McGuinness (Sinn Féin) since 8 May 2007

#### United Kingdom Parliament

The UK is a constitutional monarchy with a bicameral parliament. The House of Lords and the House of Commons. The chambers sit separately, and are constituted on different principles. However, the legislative process involves both Houses.

- The House of Lords: Currently there are 742 members, consisting of 26 "Lords Spiritual" and the remainder "Lords Temporal". The Lords Spiritual includes the 2 archbishops and 24 most senior bishops of the Church of England, while the Lords Temporal are the current Life Peers, as well as 90 Hereditary Peers and

## 2 Great Officers of State.

- The House of Commons: 646 elected members, term: up to 5 years  
The next election is due by May 2010.

Unlike laws enacted by the UK Parliament, Acts of the Northern Ireland Assembly are subject to judicial review. A law can be struck down if it is found to exceed the competences of the Assembly but also if it violates European Union Law or the European Convention on Human Rights, or if it is found to discriminate against individuals on the grounds of political opinion or religious belief.

Although the British monarch is not formally a component of the Assembly, all bills passed by the Assembly must receive the Royal Assent in order to become law. This is not a mere formality. If the Secretary of State believes that a bill violates the constitutional limitations on the powers of the Assembly, the Secretary of State can advise the monarch to veto the bill, and the monarch will abide by this advice. In almost all other circumstances, however, the monarch is bound by convention to sign a bill into law.

### Head of State

First Minister Peter David Robinson (leader of the Democratic Unionist Party) since 5 June 2008 and Deputy First Minister Martin McGuinness (chief negotiator for Sinn Féin) since May 2007 and re-appointed 5 June 2008. In cases of suspension of the Northern Ireland Assembly the de facto head of state is Queen Elizabeth II (United Kingdom sovereign since 1952).

### UK Political Leader

Prime Minister Gordon Brown, leader the Labour Party. Prime Minister since June 2007. Last election May 5, 2005 where the Labour Party received 352 of the total 646 constituency votes.

### European Union

The UK has been a member of the EU since 1973 with two current opt-outs (Schengen and stage three of the European Monetary System, i.e. the euro).

## Banking Environment

Banking services are generally offered by the large UK banks although local players exist

### Overview

#### Introduction

Banking services in Northern Ireland are to a very large extent offered by the large UK banks placed in London. The local marketplace in Northern Ireland is dominated by four large banks: Ulster Bank (owned by Royal Bank of Scotland), Bank of Ireland, Northern Bank (owned by Danske Bank) and First Trust Bank (part of AIB UK).

The City of London is one of the largest financial centres in the world. In addition to several large domestic banks, there are a significant number of foreign banks represented in London. In total around 25,000 firms within personal investment, investment management, securities and futures, banking, insurance, credit unions and other firms have obtained authorisation from the Financial Services Authority (FSA) to operate in the UK. As a result, a wide diversity of financial services are offered.

#### Sector Figures

At year end 2005, according to the Bank for International Settlements' "Red Book" (last updated March 2007), there were 391 financial institutions operating in the United Kingdom with some 13,827 branch offices and 113.72 million accounts valued at £3,757.60 billion. This includes domestic and foreign banks:

- 217 commercial banks whose accounts are valued at £1,490.20
- 174 foreign banks whose accounts are valued at £2,267.40

Estimates from 2009 state that approximately 160 banks operate in the UK, and as many as 177 foreign banks have one or more branches — the vast majority of these are located in London - the "City" which has the highest concentration of foreign banks in the world. There are 53 building societies.

#### Recent Developments

On 22 February 2008 Northern Rock, one of the top five mortgage lenders in the UK, was nationalised. The nationalisation was a result of two unsuccessful bids to take over the bank, neither being able to fully commit to repayment of taxpayers' money, which were extended by the Bank of England via a liquidity support facility due to problems in raising funds in the money market to replace maturing money market borrowings.

The US government's proposed £500 billion (approx. \$850 billion) bailout package will cover five leading UK banks, which together own around \$175 billion (approx. £95 billion) of distressed assets, newspaper reports said. Of the affected UK banks, HSBC holds about £45 billion in illiquid assets, Barclays has £17 billion, Royal Bank of Scotland £16 billion, HBOS £13 billion and Lloyds TSB, which agreed to buy HBOS for £12 billion on 18 September 2008, has distressed assets of about £3 billion.

A quarter of the bailout package would then go to the British banks if they opt to fully tap into the rescue plan. Prime Minister Brown has stated that there will be no US-style bailout plan for UK banks, instead relying on increasing liquidity in the markets via the Bank of England's lending facility.

On 29 September 2008, the British government announced that Bradford & Bingley, a former building society with retail and mortgage lending operations, whose profits were adversely affected by the credit crunch, was to be nationalised (the bank's mortgages) and sold the savings portion of the bank to Abbey, owned by the Spanish bank Grupo Santander. The acquisition price paid by Santander will be £612 million, including the transfer of £208 million of capital relating to offshore companies. Santander bought Bradford & Bingley's 197 retail branches, 141 agencies and related employees and will combine the business with those of Alliance & Leicester (which Santander acquired only weeks prior) and Abbey. The Bradford & Bingley brand will also remain.

On October 8th, the British government announced a bank rescue package totalling some £500 (approximately \$850) billion. Most simply the UK shall provide a £250 (€317) billion guarantee to banks, enabling them to secure medium-term borrowing. The credit crunch has forced banks to fund their long-term obligations with costly short-term money, so this will pump much-needed money into the system. Shortly thereafter on October 13th, £37 (\$64, €47) billion in fresh capital was injected into UK banks - with the government taking ownership stakes - to avert financial sector collapse or UK "banking meltdown" and protect against rising bad debts: £20 billion to RBOS (63% stake), £13 to HBOS (43.5% stake) and £4 billion to Lloyds TSB (43.5% stake). The government stressed, however, that it was not "standard public ownership" for the banks would return to private investors "at the right time". Barclays raised money directly from investors, instead of government help.

A second bank rescue package totalling at least £50 billion was announced by the British government on 19 January 2009, as a response to the ongoing global financial crisis. The package was designed to increase the amount of money that banks could lend to businesses and private individuals. This aid comes in two parts: an initial £50 billion being made available to big corporate borrowers, and a second undisclosed amount that forms a form of insurance against banks suffering big losses.

After the October 2008 bailouts of RBS, HBOS and Lloyds TSB and the latter's January 2009 merger with HBOS, the Government was holding a 43% stake in Lloyds Banking Group, but then on March 6, 2009, after it became apparent that the HBOS merger had been bad for Lloyds since HBOS had made losses of £11bn, the Government announced it would increase its stake in Lloyds to 65% (77% if non-voting preference shares are included).

#### Sector Wide Agreements

In 2005, the EU reached political agreement on the proposed directive for new capital-adequacy rules, known as Basel II, which have been implemented in the UK.

Pound Sterling is used in Northern Ireland

## Central Bank

### Background

The Bank of England (founded in 1694) is the central bank of the United Kingdom. In May 1997, the Bank of England was given operational autonomy by the Government. The current legal framework of the Bank is laid down in the 1998 Bank of England Act. As governing bodies the Act provides for a Court of Directors, a Monetary Policy Committee (MPC) and a Committee on Non-executive Directors within Court (NedCo). The latter doing, among other things, procedural reviews. The Governor of the Bank of England is Mervyn Allister King.

### Currency

The Bank has a monopoly on the issue of Pound Sterling banknotes in England and Wales. Note that, in Scotland banknotes are issued by Bank of Scotland (HBOS), Royal Bank of Scotland and Clydesdale Bank. However, all banknotes from the above issuers are generally accepted throughout the UK.

### Responsibilities

As set out by the Court of Directors, the Bank has two main purposes, approved in May 2004.

(1) Monetary Stability: the Bank (through MPC) independently sets monetary policy - i.e. it decides on the level of short-term interest rates necessary to meet the inflation target of the Government, - currently 2% per annum. The Bank implements its interest rate decisions by setting the interest rate at which commercial banks can borrow.

(2) Financial Stability: financial stability entails detecting and reducing threats to the financial system as a whole. The Bank has to make sure the overall system is safe and secure and that threats to financial stability are detected and reduced. By monitoring and analysing the behaviour of participants in the financial system and the wider financial and economic environment, the Bank aims to identify potential vulnerabilities and risks, with a view to making the system stronger. The Bank's role includes oversight of payment systems, which facilitate transactions between individuals, businesses and financial institutions. To this end, the Bank works closely together with the Economics and Finance Ministry (HM Treasury) and the Financial Services Authority (FSA). This includes activities for handling financial crises should they occur. In this respect, the Bank is the financial system's "lender of last resort" (prevention of bankruptcy if fatal consequences).

## Financial Authorities

The Treasury aims to raise the rate of sustainable growth

### HM Treasury

Her Majesty's Treasury (HM Treasury) is the United Kingdom's economics and finance ministry. Generally it is responsible for implementing the Government's financial and economic policy. Its aim is to raise the rate of sustainable growth, and achieve rising prosperity and a better quality of life with economic and employment opportunities for all.

The FSA's brand of light touch regulation is grounded in its principles-based philosophy in contrast to the typical prescriptive rules-based regulation employed elsewhere in the world

### Financial Service Authority

The FSA is an independent non-governmental organisation given statutory powers by the Financial Services and Markets Act (FSMA) 2000, which supervises and authorises individual banks and other financial organisations including recognised financial exchanges such as the London Stock Exchange. FSA's operations are financed by the financial services industry. However, FSA is solely responsible to HM Treasury, and through them to Parliament. The overall aim of the organisation is to promote efficient, orderly and fair markets; and helping retail consumers achieve a fair deal. FSA will also be involved in any merger or acquisition in the financial industry. FSMA states four statutory objectives: market confidence, public awareness, consumer protection, and the reduction of financial crime.

The BBA represents over 260 banks

### British Bankers' Association

The banks are represented by the British Bankers' Association, which is by far the biggest trade association for companies in the financial industry. As of April 2009, the BBA has 260 members, of which 203 are member banks and 57 associate members. The vast majority of members are of non-UK origin.

Financial sector continuity has been addressed by regulators

### UK Financial Sector Continuity

The UK's tripartite financial authorities – the Bank of England, HM Treasury and the Financial Services Authority – has established a website (see the end of the this profile for hyperlinks) to provide a central point of information about work on continuity planning that is relevant to the UK's financial sector.

## Legal & Regulatory Issues

The UK has a liberal legal environment

### Introduction

The UK has a liberal legal environment. No special purpose legislation applies, e.g. regulations within account ownership and account types are non-existing and reporting requirements are very limited. This makes the UK and especially London an excellent location for a group treasury centre and for setting up regional or global cash pools.

Residency status is determined by location and control

### Resident and Non-Resident Status

A company has status as a resident company if it is incorporated in the UK or centrally managed and controlled in the UK. Some companies with resident status can be considered as resident in another country for the purposes of a double taxation treaty.

Any type of account can be owned

### Account Ownership

Any type of account can be owned by a resident as well as a non-resident company.

Regulations allow for the majority of cash management products and services

### Cash Pooling Regulations

Cash concentration and notional pooling are allowed domestically as well as cross-border. The accounts of the cash pool must be held by companies within the same group. Resident and non-resident companies can participate in the same cash pool. Under UK legislation multicurrency cash pooling is permitted, although it is not widely offered by the banks.

Accounts are available in all tradable currencies

### Account Types and Charges

Current accounts can be held in all exchangeable currencies and are offered with or without overdraft limits. GBP accounts are convertible into foreign currency. Interest rates can be either fixed using a basic rate of the bank or based on a market rate (e.g. LIBOR) less a spread. Account maintenance fees will normally apply but are negotiable. Lifting fees (per mille of transferred amount) are normally not levied

#### Payment Fees

The UK has opted out of EU2560, which regulates the fees of cross-border transfers.

No FX controls apply

## FX Controls

The Pound Sterling flows freely but the Central Bank can intervene in order to stabilise the exchange rate. There are no restrictions on capital flows (exchange controls). There are no restrictions on spot and forward foreign exchange transactions. Residents and non-residents are permitted to deal in foreign currency notes and coin.

Central bank reporting is not applicable

## Central Bank Reporting Requirements

Central bank reporting is not applicable.

Laws are in place to prevent money laundering according to European and international standards

## Money Laundering

The UK has enacted anti-money laundering legislation, including legislation implementing the three EU anti-money laundering directives (Terrorism Act 2000 as amended, Proceeds of Crime Act 2002 as amended, the Serious Crimes Act of 2007 and the Money Laundering Regulations 2007).

As a Financial Action Task Force (FATF) member, the UK observes most of the FATF-49 standards. The UK is also a member of the Caribbean Financial Action Task Force (CFATF) as a Co-operating and Supporting Nation, and has observer status of the Asia Pacific Group on Money Laundering (APG), the Eurasian Group on Money Laundering (EAG) and the Eastern and Southern Africa Anti-Money Laundering Group (ESAAMLG). The UK has established a financial intelligence unit (FIU), housed within the Serious Organised Crime Agency (SOCA), which is a member of the Egmont Group.

Financial institutions in the broadest sense are required to record and report suspicious transactions to the SOCA. Individuals entering or leaving the EU with EUR 10,000 or its equivalent in other currencies must make a written declaration to the customs authorities. All records must be kept for at least five years after the relationship has ended or the transaction has been completed. Account opening procedures require formal identification of the account holder and beneficial owners. All financial institutions have to identify clients in respect of any individual or aggregated transactions, where the amount involved is equal to or greater than EUR 15,000. Where an applicant for business acts for or appears to act for another person, reasonable measures must be taken for the purpose of establishing the identity of that person.

Electronic signature and transaction legislation is in place

## Regulations Applicable for Electronic Transactions

EU-directives on electronic signatures and cross-border credit transfers have been implemented in the UK. Electronic signatures are accepted as legally binding (Electronic Signature Regulation 2002 No. 318) and electronic invoicing is allowed.

## Market Dominant Banks

Four large banks dominate the banking market in Northern Ireland

### Introduction

The commercial banking market in Northern Ireland is dominated by four large clearing banks: Ulster Bank, Bank of Ireland, Northern Bank and First Trust Bank.

Market Dominant Banks per 31 Dec. 2008

| Bank                          | Assets (USDm) |
|-------------------------------|---------------|
| Ulster Bank <sup>1</sup>      | 4,449,975     |
| Bank of Ireland               | *300,454      |
| Northern Bank <sup>2</sup>    | 695,033       |
| First Trust Bank <sup>3</sup> | 267,896       |

\* Interim statement as at 30 September 2008.

<sup>1</sup> Part of the Royal Bank of Scotland Group

<sup>2</sup> Part of the Danske Bank Group

<sup>3</sup> Part of the Allied Irish Bank (AIB) Group

Note: Figures are consolidated assets in millions USD.

Source: Banks' annual reports.

One of the largest banks in Northern Ireland and also present in the Republic of Ireland

### Ulster Bank

Established in Belfast in 1836. Following the takeover of National Westminster Bank (NatWest), under which Ulster Bank has operated since 1916, by The Royal Bank of Scotland in 2000, Ulster Bank continues to operate independently within the Royal Bank of Scotland Group. Ulster Bank acquired First Active, a leading mortgage provider in the Republic of Ireland, in January 2004. Both retain their own brands, branches and distinctive customer propositions. This multi-brand distribution strategy, with shared manufacturing, is consistent with the approach implemented by the Royal Bank of Scotland in the UK following its acquisition of NatWest.

The Ulster Bank Group is one of the largest banks in Northern Ireland, and together with their presence in the Republic of Ireland, the bank provides a comprehensive range of financial services to personal, small business and large corporate and institutional customers - in total some 1.8 million. Ulster Bank operates 284 branches (92 in Northern Ireland and 192 in the Republic of Ireland) and over 1,154 ATMs throughout the island. The group has 8,200 employees.

The RBS bank group, founded in 1727, is made up of four business areas with a combined total of 40 million customers: personal finances, wealth management, business and commercial, and corporate and institutional. The group operates nearly 50 brands including ABN AMRO, NatWest (National Westminster) and Ulster Bank. The bank has over 2,000 UK branches and is the leading bank within corporate and commercial banking, small business customers, private banking and runner-up within personal banking.

Before the acquisition of parts of ABN Amro's business, the RBS Group had a limited presence outside the UK with offices in around 10 European countries. Now the bank is one of Europe's largest. The group made a 5% equity stake in 2005 in the Bank of China, the second largest bank in China.

In October 2008, to help recapitalise the bank, the British government took a 58% stake due to lower shareholder participation in a rights issue. In January 2009, when the Treasury announced plans to inject further funds into the UK banking sector, the Government announced its' intention to convert the preference shares in RBS that it had acquired in October 2008 to ordinary shares. This would remove some of the repayment conditions made at the time but would increase the state's holding in the bank from 58% to 70%, effectively nationalising the group, however the bank itself remains nominally independent of Government. On the same day RBS released a trading statement in which it expected to post full-year trading losses (before writedowns) of between seven and eight billion pounds. The group also announced writedowns on assets (primarily related to the takeover of Dutch bank ABN-Amro) of around twenty billion pounds. The combined total of £28 billion is the biggest ever annual loss in UK corporate history.

To raise cash, RBS has sold off some subsidiaries and strategic investments, like the Bank of China.

One of the largest Irish banks

## Bank of Ireland

Bank of Ireland Group is one of the largest Irish banks by total assets, with market leading positions in the chosen domestic markets and niche status in other selected markets. The bank was established in 1783 by Royal Charter and today is located in 6 countries. The bank operates some 265 branches in the Republic of Ireland. Furthermore, in 2004, the bank signed a joint venture contract with the UK Post Office to sell financial services products through their branch network - some 14,600 outlets.

The bank's profits are distributed between the Republic of Ireland (55%), UK (32%) and the Rest of the World (13%). It is the Bank of Ireland's strategy to:

- Maximise returns from their position in Ireland;
- Substantially grow their businesses in the UK; and
- Grow their portfolio of niche skill-based businesses internationally

Despite the Irish government's guarantees to the Irish banks, their shareholder value continued to decline sharply. Allied Irish Bank was nationalised in January 2009 and shortly thereafter in February, the Irish government announced a €7 billion rescue package for both the Bank of Ireland and Allied Irish Bank.

The largest retail bank in Northern Ireland and part of the Danske Bank group

## Northern Bank

Northern Bank, acquired by Danske Bank in 2004, is the largest retail bank in Northern Ireland serving both business and personal customers with a network of 90 branches, 13 finance centres and 7 satellite finance centres.

Measured by total assets, the Danske Bank Group is the largest financial enterprise in Denmark and one of the largest in the Nordic region offering services in banking, insurance, mortgage finance, and asset management. The vision of the Group is “One platform – exceptional brands” and its mission is to be “the best local financial partner”. In total, the Group serves 5 million retail customers and a large number of public sector and institutional organisations. Some 2 million customers use the Bank's online services.

In the mid 1990s it expanded its operations into the rest of Scandinavia, and in 2005 via acquisition in the Republic of Ireland (National Irish Bank), marking its first move out of Scandinavia. In November 2006, the Danske Bank Group acquired the Sampo Bank Group, for approximately USD 5 billion in cash. Sampo Bank is Finland's third-largest bank with a market share of 16% and 121 branches; subsidiaries in Estonia, Latvia and Lithuania; and a recently acquired bank in Russia.

A sizeable player in Northern Ireland and through its parent bank, Ireland's largest

### First Trust Bank

In July 1991, the merger of Allied Irish Banks (AIB) Group's interests in Northern Ireland with those of TSB Northern Ireland. In the Northern Ireland market, the division operates under the trading name First Trust Bank from 57 full service branches throughout the province.

AIB Group is Ireland's leading banking and financial services organisation. Relationship banking and investment management businesses account for more than 90% of AIB's activity.

Internationally, AIB operates mainly in the United Kingdom (as Allied Irish Bank (GB) and First Trust Bank in Northern Ireland), and Poland (as BZ-WBK). It also owns a 22.5% stake in M&T Bank in the United States. At the beginning of 2008 AIB entered the Latvian, Estonian and Lithuanian markets by acquiring AmCredit mortgage finance business from the Baltic – American Enterprise Fund.

The group operates through five divisions:

- AIB Bank Republic of Ireland,
- AIB Bank Great Britain & Northern Ireland,
- Capital Markets,
- Poland, and
- Group functions

Despite the Irish government's guarantees to the Irish banks, their shareholder value continued to decline sharply. Allied Irish Bank was nationalised in January 2009 and shortly thereafter in February, the Irish government announced a €7 billion rescue package for both the Bank of Ireland and Allied Irish Bank.

## Clearing Systems

Four main clearing systems are in operation in the UK

### Overview

There are four main clearing systems in the UK – CHAPS, BACS, the Faster Payments Service and the Cheque and Credit Clearing (C&CC) system.

BACS Payment Schemes Limited (BACS) is responsible for the clearing and settlement arrangements for direct debits, direct credits and standing orders. BACS is the UK's largest "retail" payment system in terms of the total value of transactions settled. Faster Payments is a multilateral net settlement service enables electronic payments, typically made via the internet or phone, to be processed in hours rather than days, thereby removing the float from such payments. The Cheque and Credit Clearing Company is responsible for clearing and settlement arrangements for paper items such as cheques and paper credit vouchers.

Further, CREST, the UK's securities settlement system, and LCH Clearent Ltd, the central counterparty serving many of London's financial markets, both have "embedded" payment mechanisms. Real time settlement between CREST settlement members was introduced in November 2001.

The Association for Payment Clearing Services (APACS) is the UK trade association of banks and building societies involved in the payments system and supervises CHAPS, BACS and the Cheque and Credit Clearing Company's systems and processes. However, it is the Bank of England that acts as settlement agent for all the payment systems. APACS is a non-statutory association of institutions delivering payment services to end customers. APACS provides the forum for institutions to discuss non-competitive issues relating to the payments industry.

CHAPS provides real time gross settlement in sterling and euro

### High Value Clearing — CHAPS

Managed and operated by the CHAPS Clearing Company (CHAPSCo), CHAPS is the UK's RTGS system and enables individual and continuous payment processing during the day in real time. CHAPS is one of the largest RTGS systems in the world. Until 16 May 2008, CHAPS Euro, a TARGET-linked sub-system of CHAPS, processed high value domestic and cross-border payments in EUR. CHAPS now only processes payments denominated in GBP.

- **Participants:** Besides the 4 principal clearing banks very few UK banks are members of CHAPS. However, many of the world's leading cash management banks are included in CHAPS. 15 participate with approximately 400 financial institutions are clearing through direct members
- **Transaction types:** Urgent, same-day-value payments in sterling and euro
- **Pricing indication:** The fee which a settlement member charges its customers for a CHAPS transfer is a matter for commercial negotiation between the parties concerned. These charges may be on a per-debit item basis or part of a package negotiated by the bank with its customer.

- Operating hours: Monday to Friday 6.00–17.00 GMT.
- Clearing cycle details: The banks use the SWIFT format to instruct payments (some banks have migrated to the SWIFTNet FIN). The clearing takes place in real-time with immediate finality. The settlement between the banks are done via the member's accounts held with the Bank of England

The Bank of England takes securities as collateral against its lending to provide intra-day liquidity in the RTGS clearings. Prime securities in Sterling as well as Euro are accepted.

The Bank of England will not migrate its RTGS platform to TARGET2

## TARGET2

The current pan-European RTGS system, TARGET, migrated to a single shared platform (SSP) called TARGET2 making the RTGS systems of individual Eurosystem countries obsolete. The changeover took place in three migration waves, starting November 2007 and ending May 2008.

The Bank of England has decided that the UK RTGS system will not participate in TARGET2, so CHAPS Euro will close on 16 May 2008. After this date, CHAPS Euro members and their customers will effect TARGET payments in euro via another country's system, whether as direct members or customers of another member. Many CHAPS Euro members have already become members in this way and are running CHAPS Euro in parallel with their new membership of TARGET2. The Bank of England also has own accounts and customer business in euro, and it will access TARGET2 via De Nederlandsche Bank (DNB) to make and receive euro payments. The Swedish Central Bank will also not migrate to TARGET2.

More than 100,000 businesses transact through BACS, the UK's low value clearing settlement system

## Low Value Clearing – BACS

On 1 December 2003 BACS separated into two companies:

- BACS Payment Schemes Ltd (BPSL) is the membership-based industry body whose role is to develop, enhance and promote the use and integrity of automated payment and payment-related services. It promotes best practice amongst those companies who offer payment services and is responsible for the associated payment clearing and settlement services.
- Voca Limited (formerly known as BACS Limited prior to 12 October 2004) is the commercial company that physically processes the Direct Debit and Direct Credit payments, and maintains the payment network. Voca's products and services make all kinds of data transactions significantly more accessible to banks, governments and businesses.

However, for all users, day-to-day operation remains business as usual and the daily term used remains: BACS.

More than 100,000 UK businesses, including all of the FTSE 100, transact through BACS. There were, on average, some 22 million daily transactions in 2007. BACS has currently updated its delivery channel to adopt internet technology and public key infrastructure security; the initiative is called BACSTEL-IP and provides a direct and secure online telecommunications access to BACS services.

- Participants: BACS Payment Schemes is wholly owned by the UK's leading banks and building societies and as such it has 13 direct members. A large number of banks clear through the direct members.
- Transaction types: Ordinary payments (non-urgent) via Direct Debit, Direct Credit or standing orders in Sterling and Euro. In general up to 20,000 payments or collections can be instructed per file. Instructions can be submitted up to 30 days in advance.
- Operating hours: The clearing takes place Monday - Friday 7.00-22.30 GMT.
- Clearing cycle details:
  - Day 1: Input day when files are submitted to BACS. Via telecommunication this can be done between 8.00 (Monday from 8.30) and 21.00 on weekdays. Via BACSTEL-IP closing is extended to 22.30. Payment files are validated and confirmed upon receipt.
  - Day 2: Processing day, where the file is transmitted to the customer's bank
  - Day 3: Simultaneous debit/credit day. Hence, although it is a 3-day processing cycle there is no loss of value. Settlement takes place via Bank of England.

The first new payments service to be introduced in the UK since the introduction of BACSTEL in 1983

### Faster Payment Scheme

Faster Payments is a multilateral net settlement service enables electronic payments, typically made via the internet or phone, to be processed in hours rather than days, thereby removing the float from such payments. The new Faster Payments infrastructure was launched on 27th May 2008 and marks the first new payments service to be introduced in the UK since the introduction of BACSTEL in 1983. To date 11 banks and building societies, accounting for 95% of UK payments traffic, are committed to use the new service are committed to the new service. In the future, other financial institutions will be able to join, either as members, or to access the system through agency arrangements with a member - just as they do with other payment systems.

From the launch date, the founding member banks will be gradually implementing their own plans to deliver the new service to their customers. A phased approach to rollout is being adopted to help ensure that the service is launched smoothly, securely and with total reliability for customers. The new service will run alongside existing payment schemes in the UK such as BACS and CHAPS.

- Transaction types: one-off automated retail payments initiated online or via telephone as well as standing orders in GBP
- Value dating rules: settlement on same-day basis
- Operating hours: operates 24 hours a day
- Pricing indication: There have been no official announcements regarding the cost per transaction of FPS. However, it is expected to be around £1 - though this is likely to apply only to businesses seeking to migrate from BACS and seems unlikely any charge will apply to individual customer

Cheques and credit payments are processed locally in Northern Ireland

## Cheque and Credit Clearing Company

The Cheque and Credit Clearing Company is responsible for the bulk clearing of cheques and paper credits in Sterling and Euro throughout Great Britain. The exception is Northern Ireland where cheques and credit payments are processed locally. Members of the Cheque and Clearing Company are individually responsible for processing cheques drawn by or credited to the accounts of their customers.

- Participants: 11 full members, hereof all UK's leading banks. In addition, a couple of hundred other institutions offer cheque facilities for their clients and access the cheque clearing through the full Members
- Transaction types: Paper-based instruments such as cheques and paper-based credit transfers. No restrictions as to transaction size apply
- Operating hours: Transactions are effected on a 24-hours basis Monday to Friday
- Clearing cycle details:
  - Day One - A cheque paid into a member bank (or one of their agencies) anywhere in Britain during the course of a day's business will normally be processed by the collecting bank that evening. At the collecting bank clearing centre the cheque information is passed electronically through a secure data exchange network (called the Inter Bank Data Exchange, IBDE) to the appropriate paying bank clearing centre
  - Day Two - The next day the cheque is delivered to an Exchange Centre, where members of the cheque clearing hand over all the cheques drawn on the other banks and collect all the cheques drawn on themselves
  - Day Three - On the morning of the next working day, bank staff will review the cheques presented for payment and make decisions about whether to pay or return them. Settlement between the Members, for the net values of the cheques exchanged between them, takes place over their Bank of England settlement accounts on day three

Cheques collected in England and Wales drawn on a Scottish bank take a day extra. However, due to recent developments in Scottish clearing (standardised according to the clearing in England and Wales) these are now expected to have the same clearing cycle.

## Payments & Collections Methods & Instruments

While electronic payment methods are widespread and highly utilised, cash remains the pre-dominant means of low-value payments

### Introduction

Cash payments are the most common payment method in the UK. More specifically, the use of cash is most popular for low-value payments, with more than 96% of all payments under GBP5 in value being made with cash in 2006. In terms of the changing trends in the use of cash, 2004 was a landmark year when card payments overtook cash by value for the first time. Although the move from cash to plastic cards has been rapid, over GBP270 billion is spent each year in cash. Figures produced by APACS show that, in 2006, cash payments accounted for 63% of all transactions by volume (down from around 67% in 1999). The implementation of more contactless card payment technology is predicted to cause a further decline in cash usage.

Nearly all cashless payment methods have seen strong growth, with the recent exception of credit cards and cheques which, in volume terms, are in decline. Credit transfers remain by far the largest cashless payment method in value terms.

UK banks began offering the SEPA Credit Transfer Scheme to enable pan-European credit transfers, which can be processed in a maximum of three days, on 28 January 2008. The UK will begin to offer the SEPA Direct Debit Scheme in 2009.

#### Volume of Transactions (millions)

|                  | 2005          | 2006          | 2007          | % change   |
|------------------|---------------|---------------|---------------|------------|
| Debit cards      | 4,206         | 4,651         | 5,085         | 9,3        |
| Credit cards*    | 1,906         | 1,895         | 1,937         | 2,2        |
| Credit transfers | 2,984         | 3,058         | 3,120         | 2,0        |
| Direct debits    | 2,722         | 2,857         | 2,963         | 3,7        |
| Cheques          | 1,931         | 1,778         | 1,600         | -10,0      |
| <b>Total</b>     | <b>13,919</b> | <b>14,421</b> | <b>14,705</b> | <b>2,0</b> |

#### Value of Transactions (GBP billions)

|                  | 2005          | 2006          | 2007           | % change    |
|------------------|---------------|---------------|----------------|-------------|
| Debit cards      | 179           | 205           | 232            | 13,2        |
| Credit cards     | 119,6         | 120,0         | 128            | 6,7         |
| Credit transfers | 80,524        | 91,059        | 104,470        | 14,7        |
| Direct debits    | 797           | 845           | 883            | 4,5         |
| Cheques          | 1,682         | 1,686         | 1,646          | -2,4        |
| <b>Total</b>     | <b>83,318</b> | <b>93,933</b> | <b>107,359</b> | <b>14,3</b> |

\* Includes payments by cards with a credit and/or delayed debit function.

Note: Percentage change calculated from 2006-2007

Sources: ECB Statistical Data Warehouse

In volume terms, cards are the most heavily used non-cash payment method

## Card Payments

Cards are the most heavily used non-cash payment method in the UK. Credit cards are predominantly issued through the Visa and MasterCard schemes, but all leading providers issue cards in the UK. The main debit card issuers are SWITCH (re-branded as Maestro) and Visa/Visa Electron. Besides the conventional debit and credit cards a wide variety of plastic cards exist. Some examples are: ATM Cards, Charge Cards, Loyalty Cards, Store Cards and Purchasing Cards.

The UK migrated to a Chip & Pin-code based system to enhance security and the majority of all cards in 2005. Nearly all of the UK's some 165.4 million payment cards are chip and PIN based.

Furthermore contactless is a new feature being introduced on payment cards to make purchases quicker and more convenient for both retailers and consumers. For transactions of £10 or less customers simply hold their contactless card up to a secure reader to make their payment. A contactless transaction does not require a PIN to be entered, however, from time to time the terminal will ask that the cardholder undertake a full chip and PIN transaction. This is designed to deter fraudulent use should the card be lost or stolen; each time a PIN is used it re-affirms that the cardholder is in possession of their card.

The UK has a large net of 63,420 Automated Teller Machines (ATMs) as of year-end 2007 (compared with 33,000 at the end of 2000). Some 45 per cent of the ATMs are now at non-bank sites (known as independent ATM deployers, IADs), for example locations heavily frequented by customers, e.g. supermarkets and train stations. Cash machine withdrawals are expected to peak in 2010, at 2.9 billion. In addition, more than a million POS terminals exist nation-wide.

The following is an executive summary of financial cards in the United Kingdom by Euromonitor as of March 2008.

The UK financial services industry in general continues to be highly competitive. The two major operators appear to be having different fortunes in the credit and debit sectors: whilst MasterCard, for long the weaker operator, has grabbed a share of around 45% of credit cards in circulation and is gaining fast in transactions, Visa is in the ascendancy in debit cards. Credit cards are, however, in a phase of decline for now, whereas debit cards continue to go from strength to strength, and the impact of contactless technology from September 2007 onwards, although to be available on either debit or credit cards, is more likely to increase debit cards' dominance of the market.

With a credit card sector that appears to be saturated and stagnant, the much vaunted "war on cash" is turning the focus to the development of less cash dependence among consumers for smaller purchases under £10 (the limits are somewhat higher in the US and the Euro area). Whilst the benefits to consumers are reasonably self-evident, there could still be resistance among retailers which will either have to upgrade current POS terminal equipment or else install POS

terminals for the first time.

Over the medium term financial card usage is likely to expand in the UK with the introduction of smart cards allowing operators to introduce greater functionality and features. Although the credit industry is likely to be flat, the debit sector, be it in the form of contactless payment or mobile payments, will underpin higher usage than is currently the case. There is also some indication that the introduction of pre-pay enabled mobile phones using NFC (Near Field Communication) technology could be another step in the "war against cash" and expand the market further or else cannibalise transactions from yet-to-be introduced contactless cards.

In value terms, credit transfers are by far the most common way of transferring funds

## Credit Transfers

Credit transfers are by far the most common way of transferring funds in the UK.

A CHAPS payment is used for urgent domestic payments in Sterling or domestic and international payments in Euro. The banks guarantee same-day turnaround for payment instructions received before cut off. The cut-off for electronically instructed customer payments is at 16.00 while payments instructions by other means will have an earlier cut-off. The banks can usually provide a notification to the beneficiary as well. Payments can be instructed via fax or via an electronic banking system. There is no lower limit to amounts but the fee charged by the banks (in the range 10 to 20 Sterling) effectively prevents low-value payments.

The BACS Direct Credit is mainly used for paying wages and salaries, but Direct Credits can also be set up as standing orders. More than 70% of the workforce is paid via Direct Credit, but this payment method can be used for a wide range of other purposes. More than 150,000 organisations use BACS for supplier payments, pensions, employee expenses, insurance settlements, dividends and refunds. The customer cut-off for sending payment instructions is via the new web-application BACSTEL-IP extended to 22:30 on all weekdays. Payments can also be instructed through a standard modem-connection (cut-off at 21:00). As a rule of thumb one should make over 100 transactions per month to choose the direct BACS connection (BACSTEL-IP). Processing of BACS payments can be outsourced to an approved Bureau as well. The number of payments processed through BACS is expected to continue to increase rapidly.

75% of the population uses direct debits

## Direct Debits

A BACS Direct Debit is an instruction from a customer to their bank or building society authorising an organisation to collect varying amounts from their account, as long as the customer has been given advance notice of the collection amounts and dates. Seventy-five per cent of the population uses direct debit and they have authorised around 100,000 organisations to use this payment / collection method for collecting a variety of recurring (the majority) and occasional bills including utility payments, insurance, council tax, mortgages, loans and subscriptions. It is not possible to reject a Direct Debit but if an error is made by the organisation requesting the debit or by the bank the customer is guaranteed a full refund from his bank.

Cheques are still used in a B2B context

## Cheques

Consumers use of cheques is decreasing considerably but for business to business payments cheques are still the preferred payment method. The slow decrease in corporate cheque usage is probably due to custom, as there seems to be no objective reason for a corporation not switching to electronic payment methods, e.g. BACS credit transfers.

Volumes peaked in 1990 but usage has fallen since then, mainly owing to personal customers increased use of plastic cards and direct debits. Usage fell by 39% from 1994 to 2004 and is predicted to fall a further 44% by 2014.

## Electronic Banking

Electronic banking services are offered solely as bank proprietary solutions

### Introduction

In the UK electronic banking services are offered solely as bank proprietary solutions. However, the services offered by BACS through BACTSTEL-IP could be seen as sort of a common platform for payment processing: Using approved BACSTEL-IP software via the web, payments can be uploaded to BACS for further processing. Confirmation of receipts and reports are available through the same channel.

More and more banks have shifted the focus from PC based electronic banking systems to web-based platforms. The services offered through the World Wide Web include payment transactions, account information, inter-company netting solutions, FX dealings and information etc. Even though the web-based solutions are becoming more and more advanced, a number of banks still maintain sophisticated services via PC-based tools. Internet banking has increased most rapidly: use of internet banking services was eight times higher in 2005 than in 1999. WAP (Wireless Application Protocol) mobile phone banking services are currently being developed. Five mobile telecommunication companies launched the PayForIt system in September 2007, which enables low-value consumer payments below GBP 10 to be made via Web-enabled mobile phones.

Host solutions are not widely used given the predominance of cheques for supplier payments

### General Functionality of EBS Offerings

EDI or other means of host to solutions are not widely marketed for domestic clients (as cheques are still a widely used means of payment for supplier payments). The leading cash management banks in the City, hereof a number of major foreign banks, do however provide host-to-host payment solutions in support of client's payment factories.

Host-to-host solutions exist but are not widely used

### EDIFACT / Host-to-Host Solutions

EDI or other means of host to solutions are not widely marketed for domestic clients (as cheques are still a widely used means of payment for supplier payments). The leading cash management banks in the City, hereof a number of major foreign banks, do however provide host-to-host payment solutions in support of client's payment factories.

Various e-payment solutions exist

### E-payments

In the UK there is no financial industry backed e-payment solution. A number of online billing and payment providers are present, such as for example WorldPay, NetBanx, PayPal and ChronoPay. Micropayments are offered by many of the regional and "global" players. Such solutions usually rest on two important prerequisites: 1) prepayment and 2) settlement via debit or credit cards. One of the national offerings within micropayments in the UK is British Telecom's "BT

Click&Buy". BT Click&Buy offers settlement via debit/credit cards and for UK residents via a BACS Direct Debit or their British Telecom phone bill.

An electronic signature backed by an electronic certificate is recognised as a valid way of transacting in the UK.

E-invoicing services, while available, have not been widely adopted

### **E-invoice / EBPP**

All the leading banks provide EBPP (Electronic Bill Presentment and Payment) solutions via the web, although usually through sub-contractors. This form of invoicing is not widespread, which is probably related to the fact that the business-to-business payments are still effected mainly by cheques.

Faster Payment Scheme will revolutionise the UK's automated payments infrastructure and will be comparable to the best in the world

### **Faster Payment Scheme**

Faster Payments is a multilateral net settlement service enables electronic payments, typically made via the internet or phone, to be processed in hours rather than days, thereby removing the float from such payments. See the section on Clearing Systems above for more information regarding transaction types, operating hours and a pricing indication.

The current £10,000 limit on payments means that corporates will not immediately be able to move the majority of their CHAPS payments across to Faster Payments; however, this level is likely to change over time with demand. At the moment, it has been proposed that corporates will only be able to submit Faster Payments between 6.30am and 14.30pm on normal bank working days.

The date for corporates to be able to connect into Faster Payments directly through third-party software, much as they do today into Bacs using Bacstel-IP, has not yet been set - although many believe it will be sometime in early 2009. Today, corporates with more than one bank sponsor for Bacs payments are able to manage their payments through a single bank independent Bacstel-IP solution. Until direct corporate access to Faster Payments is available, corporates who wish to enjoy the benefits of Faster Payments may have to manage multiple proprietary electronic banking services, which could potentially be seen as a backward step in terms of technology and will make treasury management more complex.

## Cash Pooling Solutions

London presents an excellent environment for cash pooling solutions

Domestic notional pooling services are offered by all major cash management banks

Cash concentration is widely offered and used

Sweeping and funding of cash across borders is the primary tool for multicurrency and cross border pooling despite other services on offer

### Introduction

As mentioned above UK has a liberal legal environment with a very limited number of regulations affecting cash pooling. Together with up to date tax legislation and a high number of double tax treaties this makes London an excellent environment for setting up cash pooling solutions of any form.

### Notional Pooling

Domestic notional pooling is offered by the major cash management banks in the City of London (including the international banks). The solutions offered to avoid co-mingling of funds include interest enhancement / interest apportionment schemes and interest netting. Such solutions all retain the autonomy of the individual participant and distribute the benefit of the set-off of balances according to agreement with the bank. As the bank cannot set-off the account balances in its own books a spread between the debit interest rate and the credit interest rate will normally be charged. In order for the bank to be able to off-set balances in its own books cross-guarantees from all legal entities participating in the pool are mandatory.

### Cash Concentration

Domestic cash concentration in the form of zero or target balancing is widely offered and used in the UK. In order for the bank to be able to off-set balances in its own books cross-guarantees from all legal entities participating in the pool is mandatory. Resident and non-resident accounts can participate in the same structure. It is also possible that accounts held by different legal entities can participate in the same structure, although cross-guarantees will be required.

### Multicurrency and Cross Border Pooling

On a cross-border basis notional as well as cash concentrating pooling schemes are offered. However, the primary tool for pooling continues to be the sweeping and funding of cash across borders. One reason for this is probably that a number of large international corporations hold their master accounts / treasury accounts - mainly denominated in USD, EUR or GBP - in London and needs the physical cash in order to operate more efficiently in the money market via deposits, swaps etc.

Cash pooling solutions across currencies are usually not part of the services offered by the major cash management banks. However, some of the more sophisticated banks do offer such solutions, domestically as well as cross-border based on interest compensation models.

Other means of optimising liquidity is automated sweeps to money market funds, which is very common in the UK.

## Tax Issues

Tax information is general and individual advice should be sought

Companies are liable to tax if considered resident

The UK tax system scheduler approach is being replaced in 2009

### Introduction

The following tax information, last updated by PricewaterhouseCoopers in April 2009, should be considered general and individual advice should always be sought.

### Tax Liability

A company is considered resident and thus liable to tax in the UK if it is either incorporated in the UK or if its central management and control is located in the UK. This is generally taken to be where the directors meet and take their decisions. Resident companies are subject to tax on their worldwide income whereas foreign companies are generally liable to UK tax profits attributable to a UK permanent establishment and certain other UK source investment income.

Partnerships and most limited partnerships are treated as transparent entities for UK tax purposes.

### Tax Base

A company is liable to corporation tax on its profits which comprise income and chargeable gains less charges on income. The UK tax system operates by assessing income under various headings, known as Schedules some of which have subdivisions, known as Cases. Chargeable gains are included in the profits chargeable figure but under a heading by themselves.

The list of Schedules relevant to companies is set out below:

| Schedule   | Case     | Type of Income  |
|------------|----------|---|
| Schedule A |          | Rents and premiums received from letting property   |
| Schedule D | Case I   | Profits of a trade  |
|            | Case II  | Profits of a profession or vocation   |
|            | Case III | Interest and other income and foreign exchange gains on loan relationships and certain derivatives, not connected with a trade; and other annual income |
|            | Case IV  | Income from foreign securities  |
|            | Case V   | Income from foreign possessions (includes foreign dividends received)   |
|            | Case VI  | Other annual income not charged elsewhere   |
| Schedule F |          | UK dividend income  |

The scheduler approach is being replaced in 2009, although this is not intended to materially affect the way in which taxable income is computed. The distinction between the taxation of revenue items and chargeable gains is being retained...

In general, taxable profits are calculated on basis of a profit and loss account prepared in accordance with International Financial Reporting Standards (IFRS) or UK generally accepted accounting principles where IFRS is not used.

A financial year for companies runs from 1 April to 31 March and is denoted by the year in which it begins. Therefore FY2008 runs from 1 April 2008 to 31 March 2009.

The UK corporation tax rates are as follows:

| Rates of Tax          | Financial Year |        |        |
|-----------------------|----------------|--------|--------|
|                       | 2007           | 2008   | 2009   |
| Full rate             | 30%            | 28%    | 28%    |
| Upper marginal rate   | 32.5%          | 29.75% | 29.75% |
| Small companies' rate | 20%            | 21%    | 21%    |

- (i) (i) the small companies rate applies to companies with profits up to £300,000, with marginal relief up to £1,500,000;
- (ii) (ii) the full or standard rate of 28% applies to companies with profits above £1,500,000, at which point all profits are taxed in full.

The marginal rate operates in such a way as to claw back to the lower tax rate; corporation tax does not operate on an 'income slice' basis. Thus, for the financial year 2009, profits between £300,000 and £1,500,000 are effectively taxed at 29.75%. These limits are subject to reduction for the number of companies in a group.

Companies, branches and permanent establishments are subject to similar tax rules, while companies involved in oil and gas extraction activities, investment companies, unit and investment trusts, insurance companies, building societies, friendly societies, trade unions and real estate investment trusts are subject to special tax regimes.

An accounting period for corporation tax purposes normally coincides with the period for which a company makes up its accounts, but it can never exceed 12 months. Large companies are required to pay their corporation tax in four equal quarterly instalments on the basis of anticipated current year liabilities. Quarterly instalments start in months 7, 10, 13 and 16 after the start of the accounting period. Small and medium companies pay their corporation tax nine months after the end of their accounting period.

In relation to interest on underpaid tax, it is calculated from the date(s) on which the tax becomes payable. The calculation of interest on overpaid corporation tax runs from the due date (or payment date, if later) until the date on which the repayment is made (or the date on which the excess is extinguished). Large companies in the quarterly payments regime will accrue interest on underpaid and overpaid tax from each instalment on a running balance basis. Interest accrues at base rate + 1% (base + 2% prior to 20 April 2000) on underpayments and at base - 0.25% on overpayments up to the traditional nine month due date for payment of tax, at which point more punitive rates of base +2.5% and base -1% respectively apply.

Small and medium-sized companies' interest is charged or paid on underpaid or overpaid tax from the due date at base +2.5% and base -1% respectively. In addition if tax is paid before the normal due date credit interest runs at base -0.25%.

Depreciation is an accounting concept and is not allowed as a deduction from profits for tax purposes. Instead, capital allowances set by tax law are adopted. Capital allowances are principally available for plant and machinery on a reducing balance basis at rates of 20% or 10%. However, following the April 2009 Budget, for any plant and machinery purchased between April 2009 and 2010, a temporary rate of 40% will apply other than for lessors. Since 1 April 2008 a 10% rate for fixtures integral to buildings has been in place. Industrial buildings allowances are currently available at 3% on a straight line basis, however these are to be phased out over the next four years with the rate reducing to 2% from 1 April 2009 and 1% in April 2010. Capital allowances can be recaptured on a sale of assets. Other rates of allowances apply for various specialist assets and for certain forms of leasing.

In relation to leasing of plant and machinery new rules apply from 2006 onwards. Where the lease is essentially a pure long-term financing transaction (described as 'long term funding leases'), the tax treatment will follow the economic reality that the lease is the equivalent of a loan. The lessor will be taxed only on the finance element of the rentals (interest plus profit). The lessee will deduct an equivalent amount and will be entitled to claim capital allowances. The new rules will apply to all leases finalised on or after 1 April 2006, or where the term of the lease commences on or after 1 April 2006, subject to some transitional rules. There is no change to the tax treatment for any leases which are not classified as long term funding leases.

Trading tax losses can be carried forward for an infinite period of time, subject to rules relating to the change of ownership of a company or the cessation of its trade. Losses can be carried back one year.

Losses arising in other schedules and capital losses are generally carried forward, subject to change of ownership of the company.

Restructurings, i.e. mergers, divisions, transfer of assets and share for share exchange may be carried out tax free in certain circumstances, provided the conditions therefore are met.

Further restrictions on three targeted anti-avoidance rules (TAARs) in the area of capital gains and losses of companies will apply to transactions giving rise to a tax advantage on or after 5 December 2005. The TAARs include artificially generated capital losses, buying gains and losses and conversion of income into capital arrangements.

Certain trading and other losses may be surrendered to its Group under certain

## Tax Consolidation

For UK tax purposes, each company in a group is treated as a separate legal person, requiring a separate tax return.

## conditions

Certain trading and other losses, however, may be surrendered by a company which is a member of a group of companies to another company (the “claimant” company), where the company is subject to UK corporation tax, including the UK trading permanent establishments of foreign companies. Only current year losses can be surrendered.

Basically, two companies are members of a group for group relief if one is the 75% subsidiary of the other or both are 75% subsidiaries of a third company. This applies irrespective of where the companies are resident.

From 1 April 2006, a UK resident parent will be able to claim group relief for losses of a non-UK subsidiary which is resident in the EEA, provided that all possibilities of non-UK relief for the losses have been exhausted and future relief is unavailable.

## Taxation of dividends varies

**Inbound and Outbound Taxation of Dividends**

A UK company is not taxed on inbound dividends received from UK companies prior to 1 July 2009, provided the shares are held for investment and not for trading purposes (for example a broker/dealer). Currently, dividends received from abroad are subject to corporation tax but credit is generally available for withholding taxes and, where the shareholding exceeds 10%, for foreign tax on profits out of which the dividend is paid. Credit for foreign taxes paid is generally assessed dividend source by dividend source but with certain opportunities for mixing certain high and low tax dividends to optimise the position and for carry forward and back of excess credits and surrendering such credits within a group of companies. .

It is expected that from 1 July 2009, the UK taxation of foreign dividends will change. to ensure compliance with the EU treaty. These changes have not yet been finalised. However, it is expected that generally all dividends (including dividends from non-UK companies) will generally be non-taxable , other than in certain specific cases. As part of these changes, it is expected that new “debt cap” rules will also be introduced, restricting the amount of relief which UK groups are able to claim for their interest expense. These rules are expected to apply for accounting periods beginning on or after 1st January 2010.

Double taxation relief in respect of overseas tax suffered is restricted in the case of dividends or other foreign income received as part of a trade, as opposed to dividends or other foreign income received as part of an investment activity. These rules principally affect banks and broker/dealers who receive foreign dividend income which has suffered overseas tax in the course of their trade.

The basic principle of the new regime is that double tax relief in respect of overseas tax will be restricted to the UK tax on the net profits arising from the transactions which gave rise to the foreign tax. Net profit takes into account both direct and indirect costs and expenses.

Dividend payments by UK resident companies are not subject to withholding tax. A non-repayable tax credit of 1/9th of dividends paid by UK companies is available to

UK resident individual shareholders.

Taxation of capital gains and losses vary with certain special conditions and exemptions available

## Taxation of Capital Gains and Losses on Shares, Bonds, Debts, Receivables and Financial Contracts

Gains and losses on shares held as investments and not as the stock of a broker/dealer give rise to chargeable gains and capital losses. Note that special exemption provisions apply for open-ended investment companies and unit trusts.

Disposals of substantial shareholdings by a UK company are exempt from corporation tax, provided the qualifying conditions are met. This relief is given on the disposal of any class of share, including preference shares and extends to assets relating to shares (broadly options to buy, sell and subscribe for share as well as securities convertible into shares) and of interests in shares (broadly rights as co-owners of shares). Losses from the disposal of such shares cannot be deducted. The principal conditions are that the shares sold (i) represent a 10% holding in the ordinary share capital of a trading company or trading sub-group, (ii) have been held for a year and (iii) are disposed of by a single trading company or by a company within a trading group.

Where the substantial shareholding exemption does not apply chargeable gains or losses arise. Losses (termed "allowable losses") can be carried forward indefinitely to set off against chargeable gains and can, in effect, be group relieved against other companies' chargeable gains.

Gains and losses on bonds, debts, receivables and financial contracts are taxed at the ordinary corporate tax rate of 28% as part of trading income or as interest income/expense. They are not subject to the chargeable gains/capital losses rules. Special rules apply with respect to deductibility and taxation of interest, gains and losses on intra-group debts and receivables. Furthermore, special rules apply to certain financial contracts.

UK persons with an interest of 25% or more in a CFC are charged 30% tax on their share of the CFC's profits, notwithstanding certain exemptions

## CFC Taxation

A company which is:

- (i) resident outside the UK;
- (ii) 'controlled' by persons resident in the UK
- (iii) subjected to 'lower level of taxation' in the territory in which it is 'resident'

is a 'controlled foreign company' (CFC).

UK persons with an interest of 25% or more in a CFC are charged to tax at 28% on their share of the CFC's profits as computed for UK purposes as if it were a UK resident, unless one of the 5 exemptions applies.

For the purposes of CFC legislation, a company is regarded, in any accounting period in which it is resident outside the UK, as 'resident' in the territory in which throughout that period it is liable to tax by reason of domicile, residence or place of management in a territory outside the UK.

'Control' of a company is defined, generally, as the power of a person to secure that the affairs of the company are conducted in accordance with his wishes, although in certain circumstances the condition is satisfied even if UK residents only own a 40% interest. The definition of control has been revised to include the entitlement to receive the majority of the overseas company's income and assets; it applies from 12 March 2008.

A company regarded as resident in a 'lower level of taxation' if the tax paid under the law of that territory in respect of profits (other than capital profits) from that period (the 'local tax') is less than three-quarters of the 'corresponding UK tax' on those profits. There are special rules applicable for determining the amount of tax paid where the foreign company is part of a fiscal grouping or consolidation.

Exemptions from the CFC regimes apply where:

- (i) (i) the CFC pays a dividend of 90% of its profits calculated for UK purposes to the UK within 18 months of the year end;
- (ii) (ii) the CFC is engaged in approved trading or holding company activities;
- (iii) (iii) the CFC is quoted and 35% of its shares are held by the public;
- (iv) (iv) the CFC's profits calculated for the purposes of UK tax arise at a rate of less than £50,000 per year; and
- (v) (v) the CFC is resident in an "excluded" (white-listed) country and certain conditions are satisfied, some specific to the named country.

In addition, the CFC rules are relaxed for CFCs established in EU member states which are not wholly artificial arrangements. In these cases, the measure of taxation of the profits of the CFC in the UK is limited to its profits exceeding the economic value added by the activities in the overseas jurisdiction.

Some changes to the detail of the CFC rules are expected to be introduced with effect from 1st July 2009, to align the rules with the new rules on the taxation of foreign dividend income. A wider reform of the CFC rules is not expected to come into effect until at least at 2010.

Withholding tax is 20% and royalties are subject to a withholding tax at 22%

## Withholding Tax

Interest and certain other payments are subject to withholding tax at 20%. Royalties are subject to withholding tax at 22%

From 6 April 2001, payments to any UK resident company can be made free of withholding tax if the recipient is chargeable to tax on the interest or royalty.

Where a reduced rate of withholding is allowed by any double tax treaty, whether on interest or royalties, it is usual for this reduced rate to be limited, inter alia, to amounts which are not in excess of a normal commercial rates.

Payments made on or after 1 January 2004 are exempt from UK income tax in accordance with the EU Interest/Royalties Directive (2003/49/EC), provided the required conditions are met.

Intercompany transactions must take place at an arm's length basis

## Transfer Pricing and Thin Capitalisation

UK transfer pricing rules, which are based on the OECD guidelines, require all inter-company transactions to take place on arm's length basis. Written documentation supporting the basis must be prepared and presented to the UK tax authorities on request. Transfer pricing rules are also applied to transactions within UK groups.

Thin capitalisation legislation is included within the transfer pricing rules and is also extended to cover transactions within UK groups. Both the rate of interest on loans and the amount of a loan are required to conform to arm's length standards. Guarantees, formal or informal, are required to be taken into account in assessing whether an amount of interest or loan principal is excessive.

No capital duties exist on the issue of shares in UK companies, while certain stamp duties still exist

## Capital or Stamp Duties

Stamp duties (stamp duty land tax) apply to the purchase of land and interests in lands including leases at rates up to 4%. A formulaic discounting rule applies to ascertain the value, for stamp duty land tax purposes, of leases not involving a premium. It can also affect the transfer of interests in partnerships.

Stamp duty/stamp duty reserve tax applies to transfers of shares and marketable securities in UK companies other than loan capital.

There is no stamp duty on intra-group transfers, provided there is common ownership of 75% of ordinary share capital and there are no arrangements in hand for the shares being transferred to be sold outside the group and other bona fide tests are met.

Reconstruction and acquisition reliefs from stamp duty are available where holding companies are eliminated from or superimposed on a group.

There is no capital duty on the issue of shares in UK companies.

Most goods and services are liable to a 17.5% VAT

## VAT and Payroll Duty

VAT is currently levied on the supply of goods and services at a rate of 15% (with a reduced rate of 5% for a limited range of goods and services). This is a reduced rate from the standard 17.5% which is expected to come back into force from 1 January 2010. Any person making taxable supplies exceeding £68,000 (from 1 April 2008) at the end of any month is required to register for VAT. Certain services are VAT exempt, e.g. transfer of real estate, insurance and reinsurance, certain financial services and passenger transport. VAT exempt activities reduce the right to deduct input VAT relating to the activities.

There is no payroll duty in the UK.

Income tax is withheld on a monthly basis

## **Employer Obligations – Tax and Social Security Withholdings**

Employers are required to withhold income tax on wages and salaries on a monthly basis.

Employers are also liable to pay National Insurance Contributions based on a percentage of each employee's earnings. From 1 April 2008 the rate is 12.8% on all earnings above £105 a week (£110 a week from 1 April 2009). There is some reduction for employees 'contracted out' of the state pension scheme into private scheme.

## Source and Contacts

Sources used for this country profile

### Sources

|  |  |
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| Central Bank   | <a href="http://www.bankofengland.co.uk">www.bankofengland.co.uk</a>         |
| Office of Public Sector Information (UK legislation) | <a href="http://www.opsi.gov.uk/legislation">www.opsi.gov.uk/legislation</a> |
| The Department of Trade and Industry                 | <a href="http://www.dti.gov.uk">www.dti.gov.uk</a>                           |
| The British Chamber of Commerce                      | <a href="http://www.chamberonline.co.uk">www.chamberonline.co.uk</a>         |
| HM Treasury  | <a href="http://www.hm-treasury.gov.uk">www.hm-treasury.gov.uk</a>           |
| Association for Payment Clearing Services            | <a href="http://www.apacs.org.uk">www.apacs.org.uk</a>                       |
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| Chamber of Commerce and Industry                     | <a href="http://www.nicci.co.uk">www.nicci.co.uk</a>                         |
| Northern Ireland Statistics and Research Agency      | <a href="http://www.nisra.gov.uk">www.nisra.gov.uk</a>                       |

Contact Danske Bank for cash management services

### Danske Bank Contacts

See [www.danskebank.com/corporate](http://www.danskebank.com/corporate) for contact persons for all countries.

Tax information provided by PricewaterhouseCoopers

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Market research provided by CaRisMa Consulting

### Country Research

This country profile was researched CaRisMa Consulting. For contact information see [www.carismaconsulting.dk](http://www.carismaconsulting.dk)

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