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Setting up your business in the UK – a trading and tax overview

The United Kingdom (UK) is one of the world's leading locations for global investment and is consistently rated as the most attractive place in Europe for foreign investment.

This document takes you through some of the main issues you will need to think about when planning to set up business in the UK.

What type of business structure should we use?

A brief overview of the main structures follows. You should seek specific advice on which structure will best suit your specific circumstances:

Establishment (a branch of your overseas business)

- Not a separate legal entity but an extension of the overseas parent company
- No limited liability or ring-fencing of the UK operations
- If you have a permanent establishment (PE) in UK then profits from this are liable to UK Corporation tax
- The PE must file parent company accounts, prepared under UK Company Law, at Companies House for public inspection, even if these are not made publicly available overseas

Limited Company

- Provides limited liability and ring-fencing of UK operations
- Gives a perception of a local business, with longevity
- Corporation tax to be paid on company profits
- Required to file UK company accounts at Companies House for public view
- Accounts require auditing if in a **group** which, **as a whole**, has annual revenues greater than £6.5m or Gross Assets greater than £3.26m – audit exemption is available if the parent provides a guarantee; however there are advantages and disadvantages to using the exemption.

Limited Liability Partnership

- Members (partners) have limited liability
- Profits are allocated to members who may be either individual persons or corporate entities.
- The tax residence of the member, and where the profits in the LLP originated will
- determine in what jurisdiction and how these profits are taxed

How much Corporation Tax will the business pay?

Current Corporation Tax rates in the UK are:

	Tax rate (%)	Taxable profit (£)
Small company rate	20	0 – 300,000
Intermediate rate	20	300,001 – 1,200,000
Full rate	20	Over 1,500,000

NB: rates are for the tax year to 31 March 2016

Taxable profit bands are reduced by the number of worldwide companies. So if a US parent and a UK subsidiary make up a group, then the bands above are divided by 2.

The current Government also plans to reduce the full corporation tax rate by 1% next year resulting in a full rate of corporation tax of 22% in the 2014/15 tax year. This is in order to make the UK the most competitive corporation tax regime in the G20.
The tax rate of a PE is determined by the level of profits of the global parent entity not just on its UK activity.

If a PE incurs a loss then this loss can be offset against the parent company's profits or it can be carried forward in the UK to offset against future UK profits. If a UK subsidiary company incurs a loss this can only be carried forward and offset against future profits from the same trade. It cannot be offset against parent company profits.

What if we use the UK to set up our holding company?

The UK's competitive tax legislation means that it is a very attractive place to set up a holding company, perhaps to gain wider access into the EU market.

If a UK company holds shares in another company and these shares are subsequently sold then, subject to meeting certain criteria, the resulting gain is usually exempt from tax as long as the company held at least 10% of the share capital in the company sold and it was a trading company or part of a trading group.

Also virtually all dividends received by a UK parent company, whether from the UK or overseas are exempt from UK taxation.

The UK also does not levy a withholding tax on dividends paid to its shareholders, whether they are based in the UK or overseas.

All of which makes the UK a very advantageous location to set up a holding company.

What if we make cross-border transactions between group companies?

The UK follows internationally recognised **Transfer Pricing** (TP) rules where cross-border trading and financial transactions between affiliated entities have to be conducted on an arm's length basis. The price and terms should be the same as if the transactions had been between completely independent parties.

Typical transactions between affiliated entities that are covered by TP regulations are:

- Sale and purchase of goods
- Provision of management services
- Property rental charges
- Transfer of intangible assets e.g. trademarks, patents
- Sharing of knowledge, expertise, business contacts etc
- Provision of financial support e.g. inter-group loans and charging a "market" interest on loans

A business will need to prepare a Transfer Pricing Report proving the arm's length basis of transactions. The report will include a functional and risk analysis, analysis of the adopted pricing model and benchmarking of the arm's length basis.

SMEs are generally exempt from the UK's transfer pricing regime, so only "large" entities need to undertake detailed TP analysis. A "large entity" for TP purposes is one with greater than 250 employees, or less than 250 employees but Revenues greater than €50m and Gross Assets greater than €43m. However even if an entity is exempt from the UK's transfer pricing regime it may fall under the scrutiny of the other international tax jurisdictions where it transacts. There may also be other tax regulations which ensure transactions are undertaken at a commercial value.

What employment taxes and social security will need to be paid?

If an individual is resident in the UK then they are subject to UK tax laws. An individual is resident if they:

- Visit the UK for over 90 days a year over a 4 year period
- Arrive in the UK intending to stay for at least 3 years
- Are in the UK for more than 183 days in a tax year

Current **Personal Income Tax** rates in the UK are:

Band of income (£)	Tax rate (%)
1 – 31,785	20
31,785 – 150,000	40
Over 150,000	45

NB: rates are for the tax year to 5 April 2016

Employers and employees also have to pay UK social security, which is called National Insurance.

Current **National Insurance** (NI) rates are:

	Band of income (£)	Tax rate (%)
Employer	Up to 7,696	0
	Over 7,696	13.8

	Band of income (£)	Tax rate (%)
Employee:	Up to 7,748	0
	7,748 – 41,444	12
	Over 41,444 on excess	2

NB: rates are for the tax year to 5 April 2016

It is the employers' legal responsibility to pay over employee's tax and social security deductions to the UK tax authorities.

The UK has a Reciprocal Agreement with the USA, EU countries and many others whereby when an overseas national of those countries is seconded to the UK for a defined period of time and continues to pay social security in their home country, then the employer and employee are exempt from paying UK NI.

What is value added tax (VAT) and should the business be registered?

VAT is a "goods and services tax" on supplies made, the standard rate of which is 20%. If a business makes taxable supplies in excess of £79,000 in any 12 months, or is expected to make supplies in excess of that amount in the next month, then it MUST be registered for VAT.

There are three types of supply

- Taxable – must charge VAT on supplies, can reclaim input VAT
- Exempt – cannot charge VAT nor reclaim input VAT
- Outside the scope – not in the UK VAT system

The supply of most types of goods and services in the UK would be classed as Taxable supplies, though there are many variations. However when these supplies are made to companies which are outside of the UK advice needs to be sought as to what rate of VAT, if any, to use.

If a UK entity sells goods or provides services to its non EU parent then there is no VAT chargeable on this overseas supply, however on the basis that the supply would be taxable if made in the UK then the entity will be able to reclaim all its input VAT.

Can we provide share option plans to our staff?

Many companies see Share Option plans as being an important way of attracting, motivating and retaining key staff.

The UK has a number of "approved" share option plans which give tax benefits to employees and employers alike and it is often possible to adapt an overseas stock option plan to fit into one of these "approved" plans.

However this is a technically complex area and careful planning needs to be undertaken as soon as share option plans are being considered for implementation in the UK.

How else can we compensate our employees?

The UK has a very comprehensive range of compensation and benefit options available for companies to offer their employees.

Pensions, private medical insurance, life and disability cover are now commonplace benefits provided by many UK businesses to their workforce.

Flexible benefit packages are also gaining in popularity, giving employees options on how they wish to "spend" their benefits allowance; which can range from "purchasing" additional holiday entitlement to obtaining full family medical cover.

How we can help

As you can see there are many things to consider when setting up your business in the UK. Please do contact us for advice. We can help you make the right choices for your business and ensure you comply with all the relevant UK company and tax rules.