JEFFREYS HENRY LLP

Doing Business in the UK

Associated Worldwide with
Jeffreys Henry International

UK - the top destination for inward investment

With fewer restrictions concerning international ownership than any other major European city, a favorable tax regime and a springboard to Europe, the UK continues to be Europe's leading investment destination for companies expanding and developing their global business…

The easiest place to set up and run a business in Europe

The World Bank found that it takes just 13 days to set up a business in the UK, compared to the European average of 32 days. It ranks the UK as the first in Europe, and fifth in the world, as the easiest place to operate a business.

A stable regulatory environment

The UK has a stable regulatory environment; with a consultative approach to the formulation of regulation, so there are no surprises for business. The UK is one of the most stable political environments to do business: according to Transparency International, the UK is one of the most transparent countries in the world. It has a higher rating than France, Germany, USA and Japan.

A flexible workforce

The UK has one of the most flexible labour markets in Europe: the World Bank ranks the UK the second best place in Europe to employ workers, behind Denmark

Transport

The UK offers world-class transport links. Heathrow's Terminal 5 is open and working efficiently. Additional expansion is planned for sea container terminals at London Gateway and Felixstowe, and for the rail network, with investment in London Cross Rail and rail freight infrastructure.

Source: UK Trade & Investment

Establishing a business in the UK

There are no special restrictions on who may establish a business and trade in the UK. Both UK and foreign resident individuals and corporate entities are free to do so...

The choice of entity to carry on a business will depend on a number of factors. The protection of limited liability is generally desirable, but banks, landlords and other major creditors may require personal guarantees, which limit the protection obtained. A UK-registered company is more familiar, and therefore acceptable, to the people one does business with, but there can sometimes be tax advantages to using a non-resident company, particularly for investment purposes. Inevitably, tax considerations play a major part in determining the choice of business entity.

The following are the main forms of businesses which should be considered when establishing in the UK.

Sole Traders and Partnerships

An individual, whether UK or foreign resident, may carry on a business on his own account, or in partnership with others. Partnerships may be formed by individuals or companies, or a mixture of both. There are few formalities and registration requirements to establish a business as a sole trader or a partnership. However, it is strongly advisable for a partnership to be established by a properly drafted Partnership Agreement, which regulates the relationship between the parties, defines profit shares and capital contributions, and provides in advance what will happen if a partner leaves the business. Where there is no Partnership Agreement, the Partnership Act 1890 will apply, but the default provisions of that Act will often be inappropriate to many partnerships. Partnerships in England and Wales do not have separate legal personality, although Scottish partnerships do.

A sole trader, a partnership or, indeed, a company may often wish to trade under a name which differs from his name or the names of the individual partners. There is no longer any requirement to register business names in the UK, but the Business Names Act 1985 provides that the correct legal name of the proprietor of the business, or the names of the partners, together with the address for service of legal documents, must be stated on notepaper, orders, invoices and receipts and on a notice at business premises.

It is now possible to form Limited Liability Partnerships (LLPs'). LLPs are required to file financial information in a similar way to companies but will afford limited liability protection to its members. LLPs are generally taxed in the same way as normal partnerships and may offer significant advantages by being tax transparent.

UK companies

Companies may be incorporated in England and Wales, in Scotland, or in Northern Ireland. The following summary refers to companies incorporated in England and Wales, though similar rules apply elsewhere in the UK. Incorporation in the Channel Islands or the Isle of Man is considered under “Offshore Companies” below.

The Private Company Limited by Shares

Although a number of forms are possible, this is by far the most popular form of English company. It is the classic form of company, which will be instantly recognisable to any businessman from a common law jurisdiction. The modern private limited company offers the advantages of cheapness of incorporation, immediate availability off the shelf, flexibility of structure, and relatively low annual costs.

Its name must end with the word “Limited” (abbreviated to “Ltd.”), one shareholder is now sufficient, and there is no minimum capital requirement. Capital duty is no longer payable on the issue of shares, although stamp duty at ½% of the consideration is payable on a transfer of shares, subject to certain exemptions. Only one director is required and one shareholderand they may be the same person.

Registers of the officers and shareholders and minute books of their meetings must be maintained, and certain returns filed at Companies House. Directors and shareholders must therefore be disclosed, though nominee shareholders are possible. An Annual Return must also be filed on every anniversary of the company’s incorporation. Companies House now send this out to the company partly completed, and the fee payable is £15 if filed electronically or £30 if a paper copy is filed. Annual accounts must be prepared and filed, and there are penalties for late filing. Under normal circumstances, private companies with an annual turnover of £6,500,000 or less and gross assets of not more than £3,260,000 are now exempted from having their accounts audited. Companies may give a floating charge over their assets; a form of security which is not available to partnerships or sole traders.

The Public Limited Company

Private companies are prohibited from offering their shares to the public. To do so, the company must be incorporated or re-registered as a public limited company. The name of a public limited company must end with “Public Limited Company”, or “PLC” for short.

Less than 1% of companies on the register are PLCs, and even fewer have actually made public offers of their shares. A PLC does not have to be listed on The Stock Exchange, but to be listed a company must be a PLC. Often, the reason for incorporating a public company is simply for the additional status and credibility which this gives. This credibility is not entirely misplaced, as there is a minimum capital requirement for PLCs of £50,000, of which at least £12,500 must be paid up (with the shareholders being obliged to contribute the balance in the event of insolvency). There is a minimum of two directors, and there are a number of other company law restrictions which either apply only to public companies or apply to them more rigorously. For example, private companies have 9 months from their year end to file their accounts, but public companies have 6 months, and the penalties for missing the time limit are more severe. However, if one is prepared to contribute the capital and to accept the greater restrictions, the extra prestige given by PLC status is not to be underestimated.

Offshore companies

Every company incorporated in the UK is now automatically resident in the UK for tax purposes although in certain circumstances it can be resident elsewhere under the terms of a double taxation agreement. A company incorporated elsewhere will only be resident in the UK if its “central management and control” is exercised in the UK. This will depend on the place of residence of the majority of its directors and where they hold board meetings. In practice it depends on the view taken of the position by H M Revenue & Customs, and what can be proved to them. From a UK perspective, any foreign company is “offshore”, but the term is commonly used to refer to companies incorporated in the various offshore islands and tax havens which offer this service. Amongst the favourite jurisdictions are Jersey, the Isle of Man, Gibraltar, the British Virgin Islands and the Bahamas. Other previously-popular jurisdictions, such as Panama or Liberia, have fallen out of favour in recent years due to political instability. The Channel Islands, on the other hand, have increased their respectability and security, at the cost of some loss of confidence in their confidentiality. However, no legitimate business need have any fears about incorporating in these jurisdictions. The International Business Corporation ("IBC") form of company offered by jurisdictions such as the British Virgin Islands, and now the Bahamas, has proved very popular through its flexibility, relative cheapness and guarantee of freedom from local taxes. Offshore companies are also attractive for the high degree of confidentiality they provide and the freedom from many filing requirements.

Overseas company and branch registration

Where a foreign company does establish a presence in the UK, there are certain registration requirements. Overseas company registration is a long-established procedure under the UK Companies Acts, and is required when a foreign company establishes a "place of business" in the UK. This has now largely been superseded by the branch registration regime, pursuant to an EC Directive. However, the two regimes are broadly similar. An example of a branch would be where a foreign multinational operates in the UK through a division, being a separate entity for accounting purposes only and not a subsidiary company in legal terms.

As the registration and filing requirements for overseas companies or branches are essentially similar to those for UK companies, the usual reasons for choosing them in preference to a UK subsidiary are accounting or taxation reasons, often based on the position in the home country. From a UK perspective, the place of business or branch will be liable to UK taxation on its UK profits, but it will not of itself make the foreign company resident in the UK unless it includes the central management and control (for example if a head office were opened in the UK).

TRUSTS

What is a trust?

A trust is a legally binding arrangement whereby assets are owned by one person for the benefit of others. The person who owns the assets is called the Trustee, and it is usual to have two or three, acting jointly. A person who receives the benefit is called the Beneficiary. Typical trusts are:

"Life interest" trusts

Here a Settlor directs that one person, often their spouse, shall receive the income of a fund of investments, or the right to live in a house owned by the trust, for the rest of their life. The Settlor directs who will receive the capital after the death of the person with the life interest.

"Discretionary" trusts

Here a large number of potential beneficiaries is specified, but with the Trustees having the power to choose which among them should benefit. This has great flexibility of use since no beneficiary can say that he has a right to receive anything from the trust. If a potential beneficiary becomes insolvent or has marriage difficulties his creditors or former spouse may have no right to any of the trust assets.

Why have a trust at all?

- To save tax;
- To direct where any particular assets go after the death of the Settlor, not just for one lifetime, but for longer;
- To preserve the trust property in the Settlor's hands or in the hands of others;
- To provide for the deceased's family;
- To protect members of a family who are unduly extravagant from themselves;
- To provide for mentally or physically handicapped family members.

UK or offshore?

Despite recent legislature changes there remain a number of tax advantages in using an offshore trust.

Although a Settlor would have to pay professional agents in the country concerned to administer the trust,it may represent a long-term saving.

Jurisdictions most favoured are the Channel Islands (Jersey or Guernsey) or the Isle of Man. They are conveniently close to the UK and have stable economies, and also have legal frameworks that recognise and fit in with UK trust legislation.

UK based trusts have their own advantages, such as inexpensive administration and convenience, but do not have comparable tax efficiency.

Favorable tax regime

The UK continues to provide a favorable tax regime for both UK and foreign investors…

Corporations

UK corporation tax is payable by UK resident companies and by non-resident companies carrying on a trade in the UK through a permanent establishment.

A company will be regarded as UK resident if it is either UK incorporated or if its centre of management and control is in the UK. Thus it is possible to have a company incorporated outside the UK treated as UK resident for corporation tax purposes.

UK resident companies will be taxable on worldwide income subject to relief under double tax treaties.

Rates of Tax

Corporation tax is currently charged at the following rates:

Taxable profits	£0 - £300,000	21%
Taxable profits above	£1,500,000	28%

For profits between £300,000 and £1,500,000, a sliding scale operates to bring the average rate up from 21% to 29.75%.

This is subject to the important proviso that the thresholds must be divided between the number of companies under common control worldwide. Thus if there are four overseas companies and one UK company in a group, the UK company will only be subject to the 21% lower rate of tax if its profits are below £60,000 (i.e. £300,000/5).

The Government has announced that the lower rate is to be reduced to 20% from 1 April 2011. Similarly the higher rate will fall to 27% on 1 April 2011 and is set to fall to 24% by April 2014.

Profit Repatriation

One of the main differences between branches and subsidiaries is in the repatriation of UK profits. There are no tax implications in repatriating branch profits.

A company would normally have to pay a dividend to transfer profits to its shareholders. However, dividends can be paid without any withholding tax and for this reason the UK could be an attractive location for holding companies for multinational groups. Moreover, the UK does have a wide network of favourable tax treaties with many countries.

Deductions and Losses

Most categories of business expenditure are deductible against income, the most notable exception being entertaining costs. Capital expenditure is depreciated through a system of capital allowances generally at a rate of 20% (falling to 18% from April 2012) on the reducing balance. This subject to a claim for 100% allowances in the first year on the first £100,000 of expenditure (falling to £25,000 from April 2012). Increased allowances are sometimes available in the first year and there are separate rules for cars.

Research and development allowances are available that allow a business to write off immediately the whole of its capital spending on research and development against income. In addition for small and medium sized companies, research and development tax credits have been introduced which can enhance the relief for qualifying expenditure to 175% and, where losses are made, can lead to a cash repayment. For large companies, 130% relief for qualifying expenditure is available.

Trading losses may generally be relieved in various different ways:

- against other income of the same period;
- against income of the previous year (and temporarily subject to limited carry to earlier years);
- against future profits from the same trade;
- against profits earned in the same period by other UK companies in the same group.

Exemption for gains on substantial shareholdings

From 1 April 2002, gains on shares where the UK company owns at least 10% of the ordinary share capital are exempt from corporation tax. This is subject to the following conditions:-

- the company being sold is a trading company or the holding company of a trading group;
- the investing company is also a trading company or the holding company of a trading group, both before and after the disposal;
- the shares have been held for at least 12 months.

Individuals

Income tax is payable by individuals and is assessed for tax years, which run from 6th April to 5th April following. The rates from 6th April 2010 are as follows:

Income Band (£)	Rate (%)
Up to 2,440	10 (savings income only)
Up to 37,400	20
Over 37,400	40
Over £150,000	50

A special rate applies to dividend income. The dividend carries a non-repayable tax credit of 1/9th of the sum received. If the individual is a lower or basic rate tax payer no further tax is due. If the individual is a higher rate tax payer tax is due at the special rate of 32.5% of the gross dividend against which the 1/9th credit is set. The result is that a tax payer in the 40% bracket pays further tax amounting to 25% of the dividend received.

In the 50% bracket the dividend tax rate is adjusted to 42.5% producing an effective tax cost of 36.11%.

UK resident individuals are liable to pay income tax on their worldwide income. Non-resident individuals (and companies not chargeable to corporation tax) are subject to income tax on UK source income only.

UK resident individuals are entitled to personal allowances which vary according to marital status. For the tax year 2010/11 a single person will be entitled to an allowance of £6,475. These allowances are not usually available to non-residents unless they are Commonwealth or EC citizens.

Residence and Domicile

It is clearly fundamental to establish whether or not an individual is UK resident. There is in addition the concept of domicile which is specific to the UK and can restrict the liability on overseas income.

Residence is not specifically defined in UK legislation. Generally, an individual will be treated as UK resident if he or she spends 183 days or more in the UK during a tax year. There is a further test for those who do not satisfy this requirement. If over a period of four tax years, an individual visits the UK for 90 days or more per year on average, then that person will be treated as UK resident. If the initial intention were to make such visits, UK residence will commence from the first of the four years. Otherwise, residence will run either from the year in which the intention changed or from the start of the fifth tax year.

Domicile is a far more nebulous concept. It is distinct from nationality or residence and an individual will be domiciled in the country which he regards as his “permanent home”. An individual could be resident in the UK for many years but if the intention is ultimately to return to his permanent home outside the UK, that individual will not be UK domiciled.

Individuals who come to work in the UK from overseas without intending to stay permanently are unlikely to acquire a UK domicile and, therefore, enjoy a highly favourable tax position as set out below.

Special rules apply in relation to an individual’s domicile status for inheritance tax.

Benefits of Non-Domiciled Status

An individual who is resident in the UK but not UK domiciled may claim only to be taxed on non-UK source income to the extent that it is remitted to the UK. Thus, investment income arising in other jurisdictions will escape UK tax unless the income is brought back into the UK. There are opportunities to remit foreign capital in preference to income and thereby avoid any UK charge. A claim normally results in a loss of personal tax allowances.

Non-UK capital gains are also subject to this remittance basis of taxation. UK assets can be converted into foreign assets by establishing a non-resident holding company, or a foreign trust.

Individuals over 18 who have been resident for 7 out of 9 of the previous tax years are obliged to pay an additional charge of £30,000 in order to claim the remittance basis.

Non domiciled employees can save considerable UK tax where duties are performed overseas. Earnings relating to work performed outside the UK for a non-resident employer will again be subject to the remittance basis. Thus where there are significant non UK duties, it may be possible to establish a separate contract of employment with a foreign company and to retain the earnings abroad.

Generally remittance planning for non domiciliaries is an area where significant tax advantages can be obtained but following new legislation introduced in 2008 considerable care is needed.

Fringe Benefits

There are a number of benefits which can be provided tax free to an employee coming to work in the UK.

1. Accommodation

   If an employee is seconded to the UK for a period of less than two years and returns to the home country of employment, the accommodation cost can be borne by the employer without creating a taxable benefit in kind on the employee. However, this is subject to the provision that the accommodation expense is reasonable. In the view of H M Revenue & Customs, “reasonable” does not include providing for extra space for the employee’s family, and in these circumstances a restriction on the relief will occur. The Revenue will also focus on the choice of area so expensive locations could well result in a restriction.

2. <u>Relocation Expenses</u>

   There is a tax exemption for the first £8,000 of expenses paid by the employer provided the expenditure falls within specific categories. These are broadly as follows:-

   - disposal or intended disposal of old residence
   - acquisition or intended acquisition of new residence
   - transporting belongings
   - travelling and subsistence
   - domestic goods for new residence
   - bridging loans

3. <u>Travel Expenses</u>

   Where an employee who is not domiciled in the UK is in receipt of earnings for duties performed in the UK he is allowed a deduction for the cost of:-

   a) any journey from his usual place of abode (ie his home country) to the UK in order to perform duties of the employment in the UK;
   b) any journey from the UK after performing such duties here to his usual place of abode; and
   c) if he is in the UK for a continuous period of 60 days or more, up to two return journeys in a tax year per person by his spouse or children under 18 between his normal place of abode and the place where he works in the UK, provided that the journey is either to accompany the employee at the beginning of that 60 day period or to visit him or her during that period.

<u>PAYE and Social Security</u>

Where the employer has an establishment in the UK, it is necessary to deduct income tax and National Insurance (Social Security) contributions from payments made to employees. The system is known as Pay As You Earn (PAYE).

UK National Insurance contributions are charged both on the employer and the employee. There is no earnings limit for Employers’ contributions which are charged at a normal rate of 12.8%. Employees’ contributions average just under 11% up to an earnings ceiling of £43,875 for 2009/10 above which there is a 1% rate without limit.

Exemptions from contributions can usually be obtained for the first 12 months if contributions continue to be paid in the previous country of residence subject to certification.

Contributions are generally due on fringe benefits in addition to normal cash salary.

Introduction to Value Added Tax (VAT)

VAT is a turnover tax which is applied to most supplies of goods and services made in the UK in the course of business. Businesses are required to collect VAT on behalf of the UK tax authorities (H M Revenue & Customs) by adding the standard rate of 17.5% to their invoices, where applicable The rate is set to increase to 20% from January 2011.

The actual VAT remitted to H M Revenue & Customs is reduced by any VAT paid by the business on its own expenses which is reclaimable. If there is an excess of VAT paid over VAT payable, H M Revenue & Customs will refund the difference.

A business does not need to register for VAT if its turnover was below £70,000 in the previous twelve months. However, non VAT registered businesses will be unable to recover VAT on expenses.

Not all UK supplies are chargeable to VAT at the standard rate. Certain supplies are “zero-rated”, such as books or children’s clothing, whilst other supplies such as finance are exempt. Where a business makes exempt supplies it is not possible to recover VAT on expenses. There is also a reduced rate of 5% on certain items. Overseas companies will have to register for VAT in the UK if they buy and sell goods within the UK. This needs to be distinguished from merely exporting to the UK where the goods have been pre-sold before arriving in this country and no VAT is due. There may also be a duty to register if services are performed within the UK.

Overseas businesses will be particularly concerned that VAT suffered on expenses can be fully reclaimed. There are a number of options:

- If taxable supplies are not made in the UK, overseas businesses may apply for a refund under one of the EC Directives;
- An overseas business may register for VAT in the UK. Normally it is necessary for the business to make taxable supplies within the UK but it may be possible to register a “representative office” which is not trading within the UK.
- VAT also applies to new commercial buildings and optionally to existing ones. VAT is a highly complex area and requires careful consideration, particularly where there are cross border issues. Invoices raised between the UK and overseas jurisdiction may well have VAT implications; for example management charges for the supply of staff. However, in many cases VAT will not represent an additional cost to businesses provided transactions are properly structured.

JHI

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In 2009, the JHI network helped high profile client Gordon Ramsay Restaurant Group to successfully re-structure their international restaurants, providing reports on relevant structures and tax and accounting requirements including advice in the US, Australia, France and Czech Republic.

How we can help

Jeffreys Henry LLP is a leading firm of chartered accountants and business advisors in London specialising in **inward investment** and **overseas expansion**...

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** source Hemscott AIM Advisers Rankings Guide 2nd Quarter 2010. ^ 2008.*

The above summary is intended for general guidance only and we cannot accept any responsibility for any action based on the summary. The law is stated as proposed at 22 June 2010. Professional advice should always be sought on any specific proposals.

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