

# Setting up your business in the UK - what are the issues you need to consider?

The United Kingdom (UK) continues to be one of the world's leading locations for global investment, being rated again as the prime business location in Europe for foreign direct investment.

However, there are a number of issues which you must consider when you are looking to set up your business in the UK. This document takes you through some of the common questions that we come across and it also gives you practical information about the issues that you need to consider.

## **What type of business structure should we use?**

There are advantages and disadvantages to all of them, and there is no one correct answer. It is dependant on your specific business circumstances and needs, a brief overview of the main structures is below:

### **Establishment (a branch of your overseas business)**

- Is not a separate legal entity but an extension of the overseas parent company.
- There is no limited liability or ring-fencing of the UK operations.
- If you have a permanent establishment in the UK then profits from this PE are liable to UK corporation tax.
- Must file parent company accounts, prepared under UK company law, at Companies House for public inspection, even if these are not made publically available overseas.

### **Limited company**

- Provides limited liability and ring-fencing to UK operations.
- Gives a perception of a local business, with longevity.

- Corporation tax has to be paid on company profits.
- Have to file UK company accounts at Companies House for public view.
- Accounts require auditing if the group as a whole exceeds two of the following three criteria: Revenues > £10.2m; Gross Assets > £5.1m; Employees > 50.

### **Limited Liability Partnership (LLP)**

- Members (partners) have limited liability.
- Profits are allocated to members who then personally pay income tax on these profits.
- 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?**

The current corporation tax rate in the UK is 19% for the tax year to 31 March 2018, no matter what the size of the company.

The Government has announced that the corporation tax rate will reduce to 17% from 1 April 2020.

If an establishment incurs a loss then this loss can be offset against the parent company's profits if in the UK it can be carried forward to offset against future UK profits. A similar treatment applies in a group situation, where UK companies are owned or under common ownership of 75% or more by the parent company.

If a UK subsidiary company (owned by less than 75% by its parent 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's 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.

If a UK company holds shares in another company and these shares are subsequently sold after being held for at least a year, then the resulting gain is 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 of 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.

The UK also has an extensive network of double taxation treaties.

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 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 etc.
- 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 TP 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 base.

SMEs are generally exempt from the UK's TP regime, so only 'large' entities need to undertake detailed TP analysis. A 'large entity' for TP purposes is one with, or part of a group with > 250 employees, or < 250 employees but revenues > €50 million and gross assets > €43 million. However, even if an entity is exempt from the UK's TP 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. The UK Statutory Residence Test comprises of three tests to determine whether an individual is resident or not in the UK – the 'automatic overseas test', 'automatic residence test' and 'sufficient ties test'. These tests can be complex and we would advise any new entrant to the UK or person who spends time working in the UK to take professional advice to determine whether they are a UK tax resident.

Current **personal income tax** rates in the UK are:

| Band of income (£) | Tax rate (%) |
|--------------------|--------------|
| 1-33,500           | 20           |
| 33,501 – 150,000   | 40           |
| Over 150,000       | 45           |

*NB: Rates are for the tax year to 5 April 2018*

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

Current NI rates are:

|          | Band of income        | Rate (%) |
|----------|-----------------------|----------|
| Employer | Up to 8,164           | 0        |
|          | Over 8,164            | 13.8     |
| Employee | Up to 8,164           | 0        |
|          | 8,164 – 45,000        | 12       |
|          | over 45,000 on excess | 2        |

*NB: rates are for the tax year to 5 April 2018*

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 service' tax on supplies made, the standard rate of which is 20%. If an established business makes taxable supplies in excess of £85,000 in any 12 months then it **MUST** be registered for VAT. A non-established business **MUST** register for VAT as soon as it makes any supply in the UK, i.e. there is no threshold for non-UK businesses making taxable supplies in the UK.

There are three type 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. 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 company, then there is no VAT chargeable on this overseas supply, however on the basis that the supply would be VATable 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 very 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.

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We have offices across London and the South East and employ over 500 staff including 52 partners. Kreston Reeves is a top 25 accountancy firm.

Through our membership of Kreston International, one of the world's leading networks of accountancy firms, we are also able to assist our clients with their global needs.

With over 25 years experience in assisting overseas companies set up and develop their businesses in the UK, we have the knowledge and expertise to make the process as easy as possible.

Our expertise with international business has also been recognised by UK Trade & Investment (UKTI), the government body which promotes the UK to overseas business. We are very proud to have been approved as members of the UK Advisory Network, which has been set up by the UKTI and in their words 'consists of members with essential knowledge and invaluable expertise'.

### **How we can help**

Please contact Michael O'Brien, member of Kreston Reeves' International team at [michael.obrien@krestonreeves.com](mailto:michael.obrien@krestonreeves.com) or on +44 (0)330 124 1399.

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