This new, fully updated fifth edition of Investors’ Guide to the United Kingdom provides an authoritative and essential guide to the current investment climate in the United Kingdom. This includes the principal sectors of opportunity for foreign investors, the grants and incentives available, the financial sector and the laws and business regulations that affect foreign investors.

In its World Investment Report 2012, the United Nations Conference on Trade and Development (UNCTAD) confirmed the UK as the largest recipient of foreign direct investment stock in Europe. The Ernst & Young European Attractiveness Survey 2010 found that the UK is the most attractive location for investment in Europe. This reflects its enterprise culture, business-friendly employment laws, world-class support services and relatively benign fiscal policies.

Aimed at foreign businesses of all sizes, from multinationals to SMEs and private investors in the UK, this unique guide offers in-depth briefings on the technical aspects of investment as well as business start-up, covering topics such as:

- Grants and incentives
- Financial reporting
- Banking and Finance
- Commercial law
- Immigration
- Mergers & acquisitions
- Private equity and venture capital, AIM market of the London Stock Exchange
- Company formation
- Business taxation
- Local Enterprise Partnerships
- Intellectual property
- Pensions and benefits
- Joint ventures

Investors’ Guide to the United Kingdom is published in association with UK Trade & Investment. Includes a Foreword from Lord Green, Minister of State for Trade and Investment.
WE SPEAK YOUR LANGUAGE
Our multilingual account managers provide all the support you need to access specialists and experts to help you build a successful business in the UK.
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INTRODUCTION
The UK has an open and transparent system for setting up companies. No permission is required to set up a business, although some industries, such as financial services, may require specific authorisation before they can commence trading. This chapter looks at the options available to investors wishing to set up a new enterprise in the UK or expand an existing one.

COMPANY TYPES
In the UK, there are four main types of company that can be separated into two categories:

Unlimited liability
The owners of organisations having unlimited liability are personally liable for all the debts that the business may incur. Should the enterprise fail, the owners may have to liquidate some (or all) of their personal assets in order to pay the enterprise’s outstanding debts. Examples of such businesses are sole traders, unlimited companies and partnerships.
Limited liability
The owners of these types of business are only liable for the amount that they originally invested in the company. Should the business fail, investors in the failed company will only lose the original value of their investment or the amount they agreed to contribute, as set out below.

In the UK there are three main types of Limited Liability Company:

1. A private company limited by shares – the liability of members is limited to the amount unpaid on shares they hold.
2. A private company limited by guarantee – members are only liable for the amount they agreed to contribute to the company’s assets should the company be wound up.
3. A public limited company – these companies are permitted to sell shares to the general public, and their liability is limited to the amount unpaid on shares they hold.

COMPANY FORMATION – METHODS AND LEGAL IMPLICATIONS
The majority of businesses setting up in the UK register as limited companies and are therefore subject to the Companies Act 2006. This Act sets out the rules governing the setting up and day-to-day running of companies.

To set up a company in the UK, you can use a company formation agent, arrange for your professional adviser (solicitor or accountant) to form the company, or you can incorporate a company yourself by using the web incorporation services operated by Companies House.

Companies House is the government agency responsible for incorporating, dissolving and registering companies, and making company information available to the public.

Eligibility for company directorship
Any company setting up in the UK must have formally appointed officers. The number of officers depends on the type of company that is being set up:

- A private company must have at least one director and may have a company secretary. The company’s sole director cannot also be the company secretary.
- A public company must have at least two directors and the company secretary must hold a formal qualification.
Procedure to incorporate a company
To register a private or public limited company, the following documents must be sent to Companies House:

- A Memorandum of Association
- Articles of Association
- Form IN01

The Memorandum of Association is a document that sets out the company’s name and the address of its registered office (which must be a valid UK address).

The Articles of Association set out the standard rules and procedures that state how the company runs its internal affairs. A company can adopt the model articles in their entirety as prescribed by the Companies Act 2006.

Form IN01 provides details of the first director(s) and company secretary (if appointed), the address of the company’s registered office, a statement of the issued share capital on incorporation and the names and addresses of the subscribers (first shareholders). The directors must also include personal details such as their address, date of birth, occupation, nationality and country of residence.

CAPITAL FOR PRIVATE AND PUBLIC LIMITED COMPANIES
When first registering, the members of the company must agree to take some (or all) of the shares, and their names must also be included on the memorandum. Shares have a par value, which can be of any amount. The value of the shares held by the shareholders (number of shares multiplied by their par value) is the company’s ‘Issued Share Capital’.

The amount of share capital required differs depending on the type of company you are setting up and the requirements of the business. A private limited company has no maximum or minimum authorised or issued share capital required in order to commence trading, save that it must have at least one share in issue (although the regularity requirements of its particular industry may require a specific minimum, for example, those regulated by the Financial Services Authority). The rules for public limited companies are more complex.

Capital for public limited companies
For a public limited company to trade, the requirement is that it must have at least £50,000 or Euro equivalent of issued share capital, of which 25% must have been paid up and the whole of any premiums (that is the amount investors are asked to
pay for the shares less the par value) on these shares. As with private companies a company operating in a particular industry may be required to have a significantly higher issued share capital.

Once the share capital has been paid up as above, the company can send the relevant information to the Registrar of Companies, who will then issue a ‘Certificate to commence business and borrow’. Without that certificate the company cannot trade or carry on business.

**MANAGEMENT OF COMPANY**

A private limited company must have at least one director, and a public limited company must have at least two directors. In both types of company, the directors are responsible for the day-to-day running of the business, and are personally responsible for any decisions made. The main responsibilities include:

- producing the annual accounts and making sure that a copy of these is sent to Companies House (a legal requirement for both public and private limited companies);
- making sure any other information required by Companies House is sent there (for instance, notification of a change in address of the company’s registered office or a change in the identity of the directors of the company).

Some of these responsibilities are required by law and, as such, any breach by the directors is a criminal offence for which the penalties can be severe (prosecution, fines, and/or imprisonment).

**OTHER FORMS OF COMPANY**

**Sole Trader**

Sole traders are businesses set up by individuals. They are typically small and usually financed by the individual. They are unlimited liability businesses, so the owner is responsible for meeting all the debts of the business. Sole traders are not required to publish annual accounts, although they must keep financial records for tax purposes.

**Partnership**

Regarded as a step up from a sole trader, this is where a group of two or more individuals set up a business together. Partnerships are regulated by the Partnership Act 1890 (as amended). Normally, a partnership agreement is drawn up before trading commences and this agreement usually contains information on the names...
of the partners of the business, how profits and/or liabilities will be shared, how the partnership will be run, and the procedures for dissolving the partnership.

As with a sole trader, partnerships have unlimited liability, with the partners jointly and severally liable for all debts, that is, if one or more of the partners is unable to meet these debts, then the remaining partners will become liable for them. A partnership in England and Wales does not have a separate identity from its partners, as a company has from its members. Partnerships are not required to publish their annual accounts, although they must keep financial records for tax purposes.

**Limited Partnership**

It is still possible to register a limited partnership under the Limited Partnership Act 1907, although they have been superseded in the main by the Limited Liability Partnership (see below). Limited partnerships are very similar to partnerships with these exceptions:

- There are two types of partner: general partners, who are liable for all the businesses debts, and limited partners, who have limited liability up to the amount of money they have invested as capital in the business. Limited partners cannot take back any money invested in the business during the partnership’s lifetime, nor can they have a management role in the business.
- By law, limited partnerships must be registered at Companies House by sending a form signed by all partners giving the name of the business, what the business does, and details of all the money invested by the limited partners.

**Limited Liability Partnership (LLP)**

The Limited Liability Partnerships Act 2000 created a new business vehicle, the Limited Liability Partnership (LLP) which combines the organisational flexibility and tax status of a partnership with limited liability for its members.

Members of limited liability partnerships benefit from limited liability because the partnership, rather than its members, is liable to third parties. However where the members of an LLP are professional people, a negligent member’s own personal assets may still be at risk because under general law, a professional person owes a duty of care to his or her client. While the government originally intended to restrict the use of LLPs to members of regulated professions, the LLP Act makes LLPs available to two or more persons carrying on any trade or profession. In view of this, as the LLP combines the tax/NIC (National Insurance Contributions)
advantages of partnerships with incorporation and limited liability, it may well become a popular vehicle for small businesses.

LLP profits are taxed as if the business were carried on by partners in partnership, rather than by a body corporate. There are no special tax treatments, or reliefs, available to LLPs or members of LLPs beyond the treatments or reliefs available to partners and partnerships.

The European Public Limited-Liability Company

The European Public Limited-Liability Company or ‘Societas Europaea’ (SE) is available to businesses operating in more than one member state. It has been possible to set up this type of legal entity in the UK since October 2004.

The purpose of the SE is to make it easier for businesses to structure and carry out cross-border activities within the EU. In practice, however, they are probably of more value for presentational purposes, although the ability to change the domicile of an SE by an administrative procedure can prove to be useful in certain circumstances.

The SE European Public Limited – Liability Company. An SE may be created on registration in any one of the Member States of the European Economic Area (EEA). Member States are required to treat an SE as if it is a public limited company formed in accordance with the law of the Member State in which it has its registered office. UK national laws that apply to public limited companies also apply, in many respects, to SEs registered in the UK.

Overseas companies carrying on business in the UK

Some companies might still want to do business in the UK without registering a company in the United Kingdom. This can be done by setting up a branch.

A branch is part of an overseas limited company that employs local representatives in the UK to carry out its trading activities. To register a branch with Companies House, the company must complete a OSIN01 Form (this lists details such as the company’s name and directors, and details of the branch being set up), the most recent set of audited company accounts, and a certified copy of their constitutional documents (both these must be in the home language of the company). If these are not in English, then a certified translation made in the country where the company was incorporated must also be submitted. A non-UK company can establish one or more branches and must register each one separately, but it is only necessary to file the constitutional documents once.

Overseas companies may also wish to set up a joint venture with a UK firm, usually through a partnership or a limited company.
2.6 COMPLYING WITH THE UK’S MONEY LAUNDERING REGULATIONS

Kim Hurst, Mazars

The UK’s Money Laundering Regulations came into force in December 2007, replacing and updating the existing regulations; their purpose is to protect the UK financial system. Any business covered by the regulations must implement controls to prevent it being used by criminals or terrorists for money laundering activities. Failure to comply with the law could have serious consequences.

WHICH BUSINESSES ARE COVERED BY MONEY LAUNDERING REGULATIONS?

Regulations apply to a number of business sectors, including:

- most UK financial and credit businesses such as banks, currency exchange offices, cheque cashers or money transmitters;
- independent legal professionals;
- accountants, tax advisers, auditors and insolvency practitioners;
- estate agents;
- casinos;
- 'High Value Dealers' - businesses that accept cash payments for goods worth 15,000 Euros or more either in a single transaction or in installments;
- Trust or Company Service Providers.
If your business falls into one of these business sectors there is a requirement for it to be monitored by a supervisory authority. It may be the case that your business is already monitored, for example by a professional body, such as the Law Society, or by the Financial Services Authority, but if it is not you will probably need to register with the UK Revenue & Customs (HMRC).

To register with HMRC under Money Laundering Regulations you must complete an application form (MLR100) to register each place where you carry on business activities that require supervision. There is a fee for registering each business premises and a subsequent annual renewal fee.

If your business is a Money Service Business or a Trust or Company Service Provider, you are also required to apply for the 'fit and proper' test (form MLR101) in addition to registering with HMRC. The ‘fit and proper’ test must be taken by all those people who are involved in the running of the business.

CRIMINAL OFFENCES UNDER THE ANTI-MONEY LAUNDERING LEGISLATION

Money Laundering is the term used for a number of offences involving the proceeds of crime or terrorist funds. It includes possessing, or in any way dealing with, or concealing, the proceeds of any crime. It also involves similar activities in relation to terrorist funds, which include funds that are likely to be used for terrorism, as well as the proceeds of terrorism.

Someone is engaged in Money Laundering if they:

- Conceal, disguise, convert, transfer or remove (from the United Kingdom) criminal property;
- Enter into or become concerned in an arrangement which they know or suspect facilitates (by whatever means) the acquisition, retention, use or control of criminal property by or on behalf of another person;
- Acquire, use or have possession of criminal property.

Criminal Property is very widely defined, but, in summary, property is Criminal Property if it:

- constitutes a person’s benefit in whole or in part (including pecuniary and proprietary benefit) from criminal conduct; or
- represents such a benefit directly or indirectly, in whole or in part; and
- the alleged offender knows or suspects that it constitutes or represents such a benefit.
Criminal Conduct is conduct that constitutes an offence in any part of the United Kingdom or would constitute an offence in any part of the United Kingdom, if it occurred there (subject to the exemptions listed below). This includes tax offences committed abroad if the action would have been an offence were it to have taken place in the United Kingdom. There is no need for there to be any consequent effect on the United Kingdom’s tax system.

However, no offence is committed in any of the following circumstances where:

- the persons involved did not know or suspect that they were dealing with the proceeds of crime;
- the act is committed by someone carrying out a law enforcement or judicial function;
- the conduct giving rise to the criminal property was reasonably believed to have taken place outside the UK, and the conduct was in fact lawful under the criminal law of the place where it occurred, and the maximum sentence if the conduct had occurred in the UK would have been less than 12 months (except in the case of an act which would be an offence under the Gaming Act 1968, the Lotteries and Amusements Act 1976 or under sections 23 or 25 of the Financial Services and Markets Act 2000, which will fall within the exemption even if the relevant sentence would be in excess of 12 months).

It is a general rule that an element of intent is required before many criminal offences can be committed. For example, theft can only be committed where the offender is dishonest and has intent to deprive permanently. In some cases, where the monetary proceeds of a suspected theft or tax fraud are small, it may be that the perpetrators were acting in error or in the mistaken impression that they had permission to act as they did.

It is also important to note that for indirect tax, section 167(3) Customs & Excise Management Act 1979 provides that a wide range of innocent/accidental errors are criminal offences (although they are in practice generally dealt with under the civil penalty regime).

For the avoidance of doubt, Criminal Property includes (but is by no means limited to):

- The proceeds of tax (direct or indirect) evasion including the under declaring of income and the over claiming of expenses.
- A benefit obtained through bribery and corruption (including both the receipt of a bribe and the profits earned from a contract obtained through bribery or
the promise of a bribe).

- Benefits obtained through the operation of a cartel.
- Benefits (in the form of saved costs) arising from a failure to comply with a regulatory requirement, where that failure is a criminal offence, e.g. a breach of health and safety regulations.
- Property, even of minimal value, acquired by theft (including, for example, not telling a customer that they have erroneously paid twice. Overdrawn director’s current account in a relevant company.

The following can constitute a criminal offence:

- Providing assistance to a money launderer to obtain, conceal, retain or invest funds if you knew, or in some cases, if you should have known that the funds were the proceeds of serious criminal conduct. Making a report precludes a charge of assisting a money launderer.
- Tipping off a person, or any third party, in connection with an investigation into money laundering. This could include, for example, informing someone of your money laundering suspicions.
- Failing to report a suspicion of money laundering if the suspicion was acquired in the course of your employment (or, as the case may be, your profession). It is a criminal offence not to comply with the Regulations and a criminal offence may also be committed by anyone who has consented to or connived at non-compliance with the Regulations, including where such non-compliance is attributable to their neglect.

There are thousands of criminal offences in the United Kingdom that, if committed, are likely to result in a person benefiting from an offence and thereby having Criminal Property. The key point to note is that Proceeds of Crime Act (POCA) introduced an ‘all crime’ reporting regime. That is, Money Laundering offences can relate to the proceeds of any criminal activity not just, for example, drug trafficking.

In addition to the offences under the POCA, there is also an obligation for businesses to report belief or suspicion of the proceeds from, or finance likely to be used for, terrorism, or it’s laundering, based on information which came to them in the course of its business or employment.

**MONEY LAUNDERING CONTROLS AND PROCEDURES**

Businesses covered by the Money Laundering Regulations must put controls in
place to prevent them being used by criminals or terrorists for money laundering purposes. The controls include:

- Assessing the risk of the business being used by criminals to launder money.
- Appointing a 'nominated officer'.
- Implementing a procedure to check the identity of customers and ‘beneficial owners’ of corporate bodies and partnerships and keeping all relevant documents.
- Ensuring employees are aware of money laundering regulations.

The ‘nominated officer’ must be a person in the business; they cannot be an external consultant. As it is an important role, it must be undertaken by a person who:

- has access to all customer records and documentation;
- can make the decision, without reference to others, whether or not to report suspicious activities;
- can be trusted with the responsibility.

If you are a sole trader in a regulated business with no employees, you must act as the ‘nominated officer’ yourself.

The duties of the ‘nominated officer’ include:

- being the first point of contact for reports of suspicious activity from any employee in the business;
- considering all information and assessing whether evidence of money laundering or terrorist financing exists;
- reporting any suspicious activities or transactions to the Serious Organised Crime Agency (SOCA);
- requesting permission from SOCA to continue with any transactions that they have reported, and ensure that no transactions are continued illegally.

All employees, particularly those in customer-facing positions, must receive regular training to ensure that they are aware of the money laundering laws, understand how the business’ procedures affect them and appreciate the penalties of non-compliance. They should also be able to recognise suspicious activity and know what to do about it.
THE PENALTIES FOR NOT COMPLYING WITH THE MONEY LAUNDERING REGULATIONS

If you do not comply with Money Laundering Regulations there are various measures that can be taken, from warning letters to criminal prosecution. Although criminal prosecution is a last resort, the penalty may be harsh; depending on the severity of the offence, the courts can impose penalties ranging from unlimited fines to lengthy imprisonment, or both.
4.1 FINANCIAL REPORTING AND ACCOUNTING: AN OVERVIEW

Ben Young, Mazars

INTRODUCTION
All limited and unlimited companies in the UK, regardless of whether they are trading or not, are required to keep accounting records throughout the period. This chapter sets out the key financial reporting and accounting requirements for companies trading or investing in the UK.

GENERAL PRINCIPLES
Where formal accounts are required, in particular for limited companies, these must include:

- A trading profit and loss account;
- A balance sheet signed by the director;
- A director’s report signed by the director or the company secretary;
- Notes to the accounts; and
- Group accounts (if applicable);
- An auditor’s report signed by the auditor (if required).

In general, all private and public limited companies are required to send a full copy
of their accounts to Companies House every year.

Small companies are entitled to certain disclosure exemptions in relation to the accounts they must send their shareholders, and can, in addition, file abbreviated accounts with the Registrar of Companies. Medium-sized companies can also send abbreviated accounts to the Registrar but the reduction in disclosure in these accounts is negligible. They must, however, provide a full set of accounts for their shareholders. For both small and medium-sized companies, the production of abbreviated accounts is entirely voluntary.

For a company to qualify as small, at least two of the following conditions must be met:

- Turnover must be less than £6.5 million;
- Gross assets must be less than £3.26 million; and
- Average number of employees must be less than 50.

For a company to qualify as medium-sized, again, at least two of the conditions below must be met:

- Turnover must be less than £25.9 million;
- Gross assets less than £12.9 million;
- Average number of employees less than 250.

The time normally allowed for companies to deliver their accounts to Companies House is:

- 9 months from the ARD (Accounting Reference Date) for a private limited company;
- 6 months from the ARD for a public limited company.

The ARD is the period-end date to which all accounts are prepared and normally covers a period of 12 months, although this can be extended to a maximum of 18 months. Filing of financial statements for a first year entity must be within 21 months of incorporation. Late delivery of accounts to Companies House will result in a late filing penalty, which is, technically, a criminal offence for which Directors can be prosecuted.

*Once received, all accounts filed and held at Companies House are available to the general public on request.* For this reason the option to file abbreviated accounts is attractive to some small companies.
ACCOUNTING
Regulations regarding the presentation of the primary financial statements in the UK are found in several sources such as UK company law and UK and international accounting standards. Note that subsidiaries of overseas firms incorporated outside the UK are subject to the normal UK accounting practices. Branches or places of business of overseas firms have special registration procedures.

Accounting Principles
All accounts in the UK are prepared in accordance with two fundamental accounting concepts:

- **Going concern** – the accounts are prepared as if the company will be trading in the foreseeable future.
- **Accruals basis** – income and expenditure should relate to the period in which it occurred, not the period in which it was received / paid.

The use of historical cost values is widespread under UK GAAP (Generally Accepted Accounting Practice), although there is increased use of “fair value” accounting as a result of convergence with International Financial Reporting Standards.

Whichever accounting policy is selected, they must be transparent and reflect industry and sector norms.

Financial Reporting
Every company is required to set out their accounts to specific standards. Currently, there are 30 FRS (Financial Reporting Standards) for companies to follow. There is a FRSSE (Financial Reporting Standard for Smaller Entities) specifically designed for small companies or groups, which basically is a single, more simple standard of financial reporting which makes it easier for smaller companies to produce their accounts.

Until relatively recently, Financial Reporting Standards were developed solely by the Accounting Standards Board (ASB). These standards, in conjunction with the requirements of UK companies legislation (principally the UK Companies Acts), helped make up what is known as UK GAAP, which gives guidance to companies and auditors on how UK accounts should be prepared to give a ‘true and fair’ view of the company’s financial position.

However, due to increasing globalisation in the world economy, it became necessary to produce a set of International Financial Reporting Standards (IFRS)
so that potential investors can compare firms on a global scale.

EU firms with securities that are publicly traded on a regulated stock exchange are required to apply EU-adopted IFRS when producing consolidated accounts. In the UK, this means any company listed on any of the markets of the London Stock Exchange. Individual subsidiary companies are not yet required to prepare financial statements under IFRS.

At present, only the types of company detailed above are required to adopt IFRS. However, even companies not required to do so can choose to adopt these new standards. A company that chooses to use IFRS to produce its accounts for one financial period cannot change back to UK standards in the following years. There are limited exceptions to this, such as if the company becomes a subsidiary of a group that uses UK standards as opposed to IFRS, in which case the company can revert back to using UK standards.

At the current time there has been an overall agreement that current UK GAAP is in need of review for the purposes of reaching greater convergence with international standards. The ASB in the UK has recently identified that an international framework, originating from the IFRS for Small and Medium-sized Entities (IFRS for SMEs) would provide the foundations for a suitable UK GAAP replacement.

Under the proposals, UK companies will apply a new financial reporting framework, which would split UK entities into three tiers (defined by public accountability and size) for financial reporting purposes, the effective date for which is anticipated to be 1 January 2015.

As this new regime will require a full 18-month implementation process, companies should be considering the new rules from early 2013 to ensure they are suitably prepared for the transition.

AUDIT
Audits must be carried out by someone authorised to provide an audit, by:

- Being a member of a Recognised Supervisory Body (RSB); and
- Having the necessary qualifications / eligibility of that RSB to be an auditor.

An RSB can be a professional body such as the Institute of Chartered Accountants for England and Wales. UK companies are required to be audited unless they are designated as ‘small’ in size, or are dormant. This ‘small’ exemption is subject to a number of detailed conditions which must be met in order for it to apply.

If a UK small company is part of a group of companies (UK or worldwide), the group in its entirety must meet the definition of ‘small’, otherwise the small UK
company will be subject to an audit regardless of its individual size.

If a group of companies (UK or worldwide) contains a listed entity with its shares traded on a recognised stock exchange anywhere in the world, then any UK company which is part of that group will require an audit regardless of its own individual size.

Note here that exemption from the audit requirement does not exclude the company from having an audit if it so wishes.

Auditors are normally appointed in the following ways:

- They are appointed by a newly formed company, or by an existing company that requires a new auditor.
- They are reappointed by a company for which they are already existing auditors.
- They are ordered to be auditors of a firm by the Secretary of State.

This last case occurs when a company requiring an audit fails to agree to appoint an auditor.

The company’s auditors are appointed / reappointed each year by either majority vote of the shareholders, or for a private company the provisions of deemed re-appointment of an existing auditor may apply. Directors have the authority to fill a vacancy that arose during the year but this will need to be later confirmed by the shareholders before the new auditor may continue in office for subsequent financial years.

Upon appointment, the auditor should send the company an engagement letter confirming their appointment as auditors, and setting out other items relating to the audit, such as the work they will carry out, confirmation of their independence and payment of audit fees.

An auditor ceases to audit a company in the following ways:

- They resign from the post of auditor of the company.
- They are removed by the company.

If an auditor resigns they must provide a written notice to the company and a statement of circumstances to the Registrar of Companies and anyone else entitled to copies of the company accounts.

If the members of a company wish to remove the existing auditor, the auditor has the right to have written circularisation to all members and the right to be seen and heard at the company’s general meeting at which their removal is proposed.
4.2 BUSINESS TAXATION

Andrew Ross, Mazars

INTRODUCTION
This chapter is divided into the following parts:

- The key forms in which an overseas company could set up in the UK with a view to carrying on business.
- The basis of taxation in the UK, summarising the key taxes an investor needs to be aware of.
- Setting out the basis of calculation of taxable profits, noting the key rules on tax deductibility of expenditure and certain important tax reliefs and anti-avoidance provisions.

VEHICLES FOR DOING BUSINESS IN THE UK
There are several different vehicles that could be used when doing business in the UK, each with their own legal and commercial peculiarities. When considering the most suitable form of vehicle to use, investors would be recommended to consider such factors in addition to taking account of the differing tax treatment of each.

Representative office
It is important to distinguish between “trading in” and “trading with” the UK. An overseas person will not be subject to UK tax on profits simply because they are transacting with UK entities, even if the goods are delivered to UK locations or
services are carried out within the UK.

This can be the case even if the overseas investor has set up an office within the UK, although this will depend on the nature of the activities carried out by that office. If, however, those activities cross a certain line, this could result in the creation of a taxable branch or permanent establishment.

Branch / “permanent establishment”
The UK branch (referred to for tax purposes as a “permanent establishment” or “PE”) of a foreign company will be subject to tax in the UK on profits that are attributable to the branch. UK domestic legislation gives a definition of a PE which is broadly similar to that contained in many double tax treaties. Typically, a foreign company will have a UK PE if:

- it has a fixed place of business in the UK through which the business of the company is wholly or partly carried on; or
- an agent acting on behalf of the company has and habitually exercises in the UK authority to do business on behalf of the company (except where that agent is of independent status acting in the ordinary course of his business).

There are exceptions to this where, for example, the fixed place of business is for the storage of goods or purely for purchasing or information-gathering functions. In such a situation, the foreign company may not have a UK taxable presence.

Subsidiary
A UK incorporated subsidiary will be subject to UK tax on all of its trading profits, wherever those profits are earned (subject to the possibility of claiming an exemption from UK tax for profits within overseas branches).

A non-UK incorporated company can also be treated as UK tax resident (and so taxable in the UK on its worldwide profits) if its “central management and control” are located in the UK. Therefore care needs to be taken where a non-UK company is operating in the UK to ensure that the company as a whole does not become UK tax resident.

Branch vs. subsidiary
From a UK tax point of view, there is generally little difference in the basis of taxation between a branch and a subsidiary. UK corporation tax is charged at the same rates on branch or subsidiary profits and no withholding tax is charged on the remittance of funds by a branch to its head office or on dividends paid to its parent company.
Therefore, a decision on the most appropriate form will generally need to be based on commercial & legal factors and the non-UK tax implications.

One potential tax advantage of using a UK branch (particularly in start-up ventures) is that tax losses of the branch may (depending on the law of the relevant overseas country) be available to offset non-UK profits arising in the same foreign company. At the same time, those tax losses can also be carried forward to shelter future profits of the branch from UK tax (although the flip-side of this is that there may be less double tax relief to shelter those same future profits from tax in the overseas country).

**Joint ventures**
Where an investor wishes to enter into a UK joint venture-type arrangement with a third party, the parties will likewise need to agree on the form of the joint venture, for example:

- **Contractual joint venture:** Each party (through its own legal entity) enters into a contract with a view to carrying out a business transaction or a project.
- **Partnership:** This is a more formal legal structure involving the carrying on of a business in common with a view to profit. Each party (again through its own legal entity) will enter into a formal partnership agreement. The basis for sharing profits will be set out in this partnership agreement.
- **Company:** A company is set up to carry out the joint venture business, with the joint venture parties owning shares in that company. The relationship between the joint venture parties may also be governed by a shareholders’ agreement.

Again, commercial and legal considerations must be taken into account in determining the most appropriate vehicle. The tax treatment of each will also vary.

**BASIS OF TAXATION**
The main taxes payable in the UK may be summarised as follows.

**Tax on company profits**
Corporation tax is payable on the taxable profits (both income and capital) of a UK subsidiary or the UK branch of an overseas company. The rate of corporation tax is the same for both a branch and subsidiary.

Tax is calculated based on the profits of an “accounting period”, which will
normally coincide with the period for which the company prepares its financial
statements.

There are two rates of corporation tax - the main rate and the “small profits rate”.

To qualify for the small profits rate the company must be a UK-resident company with profits of less than £300,000 (the “lower limit”). There is a marginal rate when profits exceed that amount but are less than £1.5 million (the “upper limit”). However these upper and lower limits are reduced if the company has any “associated” companies at any time in the accounting period. For example, if worldwide there are 19 other associated companies (typically other members of a group), the upper and lower limits applicable to the UK company are reduced to £15,000 and £75,000 respectively (i.e. the limits are divided based on the 20 members of the group). As a result, for many groups, the small profits rate is unlikely to apply or, when it does, there is little benefit.

The current and proposed future rates of corporation tax are:

<table>
<thead>
<tr>
<th>Profits arising in year from 1 April to 31 March:</th>
<th>2012/13</th>
<th>2013/14</th>
<th>2014/15</th>
</tr>
</thead>
<tbody>
<tr>
<td>Main rate of corporation tax</td>
<td>24%</td>
<td>23%*</td>
<td>22%*</td>
</tr>
<tr>
<td>Small profits rate of corporation tax</td>
<td>20%</td>
<td>**</td>
<td>**</td>
</tr>
</tbody>
</table>

* rate has been announced, but not enacted
** small profits rate for these years yet to be announced

In charging corporation tax on companies with year ends other than 31 March, a proportionate part of profits for an accounting period is taxed at each of the applicable rates. For example, the main rate of tax on taxable profits of a company with a 31 December 2013 year end is 23.5%.

From 1 April 2013 a new “Patent Box” regime will be introduced giving a 10% corporation tax rate for “patent derived profits” for both new and existing patents.

For “large” companies (very broadly, being companies paying the main rate of corporation tax but subject to certain exceptions) the corporation tax liability for an accounting period is due and payable quarterly, the first instalment being seven months and 14 days after the beginning of the period (and hence estimates of the forecast tax for a particular year will need to be made for at least the first two quarterly payments). For companies not within the quarterly payment obligation, tax is due in a single payment, nine months after the end of the company’s accounting period. Interest is payable to/receivable from HMRC on any under/over payment of tax.
Tax on individuals

Individuals are liable to income tax on trading profits, employment income, interest, dividends and other income and are subject to capital gains tax on chargeable gains. The rates for the tax year commencing 6 April 2012 are:

<table>
<thead>
<tr>
<th>Taxable income (£)</th>
<th>Tax rate on income</th>
<th>Effective tax rate on UK/overseas dividends</th>
<th>Tax rate on capital gains*</th>
</tr>
</thead>
<tbody>
<tr>
<td>up to 34,370</td>
<td>20%</td>
<td>Nil</td>
<td>18%</td>
</tr>
<tr>
<td>34,371 - 150,000</td>
<td>40%</td>
<td>25%</td>
<td>28%</td>
</tr>
<tr>
<td>over 150,000</td>
<td>50%</td>
<td>36.11%</td>
<td>28%</td>
</tr>
</tbody>
</table>

* A reduced rate of 10% is payable on the first £10m of gains made in a taxpayer’s lifetime, on the disposal of qualifying business assets (“Entrepreneurs’ relief”).

An individual who is trading in partnership is assessed for income tax on their share of the tax-adjusted trading profits for the accounting period of the partnership ending in the tax year. The basis of calculation of taxable trading profits is broadly the same as for a company.

The rules for the calculation of individuals’ capital gains differ from the rules for companies in that “indexation allowance” (an allowance for inflation) is not available to individuals, whilst there are other reliefs available to individuals that are not available to companies (e.g. Entrepreneurs’ relief).

Interest income is taxable when received. In most cases, UK interest is paid to individuals net of basic rate income tax. The gross income is taxable, with credit given against the tax liability in the tax year for the tax deducted. Where the tax liability is less than the tax deducted, the excess withholding tax is repayable.

Income tax on trading and other income that is not subject to PAYE (see below) is due in two instalments – on 31 January within the relevant tax year and 31 July following the end of the tax year.

Payroll taxes/national insurance contributions

An employer is obliged to make deductions from pay for employee income tax and employee national insurance contributions (NIC), using the “pay as you earn” (PAYE) system.

Employer NIC is an additional cost payable by the employer based on each employee’s wages plus benefits in kind. The rates of employer NIC vary.
depending whether the employer offers a final salary pension scheme and has contracted out of the state earnings related pension scheme. The rates for the year commencing 6 April 2012 are:

<table>
<thead>
<tr>
<th>Weekly earnings</th>
<th>Monthly earnings</th>
<th>Contracted in</th>
<th>Contracted out</th>
</tr>
</thead>
<tbody>
<tr>
<td>Up to £144</td>
<td>Up to £624</td>
<td>Nil</td>
<td>Nil</td>
</tr>
<tr>
<td>£144 to £770</td>
<td>£624 to £3,337</td>
<td>13.8%</td>
<td>10.4%</td>
</tr>
<tr>
<td>Excess over £770</td>
<td>Excess over £3,337</td>
<td>13.8%</td>
<td>13.8%</td>
</tr>
</tbody>
</table>

The employer has to make monthly remittances to HMRC (by mandatory electronic funds transfer) of the amounts they deduct for employee income tax and NIC, along with the employer NIC.

**VAT**

All businesses investing or trading in the UK must register for UK VAT if they have a “business establishment” or usual place of residence in the UK. This test differs from the corporation tax tests of residence and it is therefore possible for an overseas investor to be required to register for UK VAT even though it may not have a branch that is liable to corporation tax.

VAT registered businesses are generally required to file VAT returns quarterly by way of electronic returns and therefore any VAT payable will usually be payable by not later than one month and seven days after the end of the relevant quarter. However, VAT-registered business with an annual VAT liability in excess of £2.3 million must make interim payments at the end of the second and third months of each VAT quarter as payments on account of the quarterly VAT liability. A balancing payment for the quarter is then made with the VAT return.

**Stamp duty land tax ("SDLT")**

SDLT is payable on the acquisition of any interest in land situated in the UK regardless of whether the acquirer is an individual, a partnership or a company or whether the acquirer is UK or non-UK resident.

The most common rate of SDLT when a capital sum is paid to acquire non-residential land or interest in such land (whether the acquisition is ownership of the land or on the grant or assignment of a lease) is 4%. Lower rates of SDLT apply if the purchase consideration is less than £500,000. Different rates of SDLT may apply to the acquisition of residential land; care must be taken, in particular, where residential land is to be acquired by non-UK persons since higher rates of SDLT may be payable.
On grant of a lease, in addition to the SDLT on any premium, the tenant is liable to pay SDLT at 1% of the net present value of the total rent payable under the lease, less a deduction of £150,000.

**Stamp duty**

Stamp duty, at 0.5%, is payable by the person acquiring shares or convertible loan notes of a UK registered company. There are exceptions for intra-group transfers. No duty is payable on the transfer of ownership of other assets, for example loan notes, goodwill or trade debtors. There is no duty on the issue of shares or convertible loan notes.

**Withholding taxes**

The UK does not impose withholding tax on dividends.

A 20% withholding tax is generally imposed on interest payments, although the rate may be reduced under an applicable double tax treaty or the EU Interest and Royalty Directive, provided that certain conditions & formalities are complied with prior to the payment of the interest.

There is no withholding from payments of interest by UK companies or to UK branches of overseas companies (which will include, in particular, UK branches of overseas banks), or on payments of interest on certain quoted loan stock (although HMRC has indicated that it is reviewing the future application of this rule). Where securities are issued at a discount, no withholding is applied on the discount element.

For royalties, a 20% income tax withholding applies, subject to lower rates in the relevant applicable double tax treaty or under the EU Interest and Royalty Directive.

Rent paid to a non-UK resident person is subject to a 20% withholding deduction, unless the landlord has met the requirements of HMRC’s “non-resident landlords’ scheme”.

Under the construction industry scheme, there may be a withholding requirement on payments made by contractors to sub-contractors in relation to building projects.

No withholding tax is applied on service fees, technical fees or management charges.

**DETERMINATION OF TAXABLE PROFITS OF A BRANCH/SUBSIDIARY**

The rules for the calculation of the taxable profits of both a branch and subsidiary
are essentially the same. The key issue for a branch is the extent to which profits of the relevant overseas legal entity should be allocated to the head office or the UK branch.

**Taxable trading profits**
The taxable result from trading is based on the profits for the year, as shown in the company’s financial statements.

Costs that are not deductible for tax purposes include entertainment expenditure, fines and penalties, expenditure of a capital nature and non-specific provisions. Depreciation, amortisation and gains/losses from the disposal of fixed tangible assets are not allowed or taxed. For tax depreciation, there is a statutory relief for certain classes of assets (see capital allowances, below).

Tax relief is available on the cost of the acquisition of intangible fixed assets (for example goodwill) if acquired after 31 March 2002 from a non-connected person. The amount that is tax deductible is the charge in the profit and loss account or income statement. However, a company may instead elect to have tax relief of 4% per annum on the cost.

Remuneration paid to employees is deductible on an accruals basis providing payment to the employee is no later than nine months after the year end. Remuneration paid more than nine months after the year end is tax deductible in the period when payment is made.

**Capital Allowances**
Capital Allowances is the UK term for the statutory code for deducting the cost of capital expenditure from trading profits. The main class of asset that is eligible for capital allowances is plant and machinery. This includes plant within a building or structure (e.g. electrical, heating, water and air conditioning systems; lifts; escalators; sanitary ware). No allowances are given for the cost of buildings.

Eligible expenditure on plant and machinery qualifies for tax relief at one of two rates. Certain specified expenditure can obtain allowances at a rate of 8% per annum and all others at 18% per annum. For both, allowances are calculated on a reducing balance basis.

Assets in the 8% expenditure category include:

- those with an expected life when new of more than 25 years;
- some plant within buildings;
- cars with emissions of more than 160 g/km of CO2.
Up to £25,000 of a company’s annual expenditure on eligible assets, other than cars or assets for leasing out, is subject to 100% tax relief in the year of purchase. This is known as the “annual investment allowance”. When the company is a member of a group only one annual investment allowance is given to whole group.

Full relief is also available in the year in which it is incurred (100% tax allowances) for:

- Environmentally beneficial or energy saving plant (which includes cars with CO2 emissions of no more than 110 g/km).
- Plant for research & development activities.
- Expenditure on renovating empty commercial buildings until April 2017.

On disposal of plant, the net sale proceeds, up to a maximum of cost, are deducted from the accumulated net pool of qualifying expenditure.

**Interest and finance income and expense**

In general, interest is taxed or relieved in accordance with the treatment in the company’s financial statements.

Tax relief for finance expense in “large” (as defined) corporate groups may be restricted due to the “worldwide debt cap”. This restriction is considered after making any transfer pricing (thin capitalisation) adjustments (on which, see below). Broadly speaking, the intention of the worldwide debt cap is that the tax deductible finance expense relieved against a group’s UK profits should be no greater than the external finance expense in the consolidated results of the group. However this regime will not apply if the UK net debt is less than 75% of the group’s consolidated gross debt. The rules are complex, so professional advice and guidance should be sought.

**Dividends received**

The UK has a comprehensive dividend received exemption which applies to dividends a UK-resident company receives from UK or non-UK companies. Various conditions must be met, although there is no minimum holding period or minimum ownership percentage.

**Sale of capital assets**

The taxable gain on the disposal of a capital asset is calculated as net proceeds received less the acquisition cost and costs incurred on improvements. “Indexation allowance” (an allowance for inflation) may also be given to disposals by
companies. Gains on certain assets can also be deferred by reinvesting the proceeds in replacement assets ("rollover relief").

The UK has a form of participation exemption, which can exempt from tax the gain or loss on the disposal by a company of shares in a trading company or trading sub-group - the exemption is called the Substantial Shareholdings Exemption (SSE). SSE, along with the dividends received exemption, are core features that make the UK an attractive location for holding companies.

The SSE rules contain several detailed requirements and therefore professional guidance should be sought as to whether it applies, not least because a group’s non-trading activities do not necessarily need to be substantial for the group not to be regarded as a "trading group" and hence not qualify for the relief. Advance clearance application can be made to HMRC where there is uncertainty as to whether SSE applies to a particular disposal.

Transfers of capital assets (including intangibles) between UK members of a group take place on a tax neutral basis regardless of the value of the asset or the price paid (see Chapter 4.4). However, if the transferee subsequently leaves the group still holding the asset within six years of the transfer, this can create a “de-grouping” tax charge based on a deemed disposal (and re-acquisition) of the asset at its market value at the date of the intra-group transfer.

Reliefs may apply to the transfer of a trading business to a company (a business incorporation) and to corporate acquisitions effected by a share-for-share exchange.

Losses
A company may claim to set a trading loss against all of its taxable profits within the same accounting period, and against the profits of the immediate preceding period, providing the company was carrying on the same trade in the previous period. Alternatively, or in addition, it may transfer some or all of a trading tax loss to another UK member, or UK members of a 75% group, for use against the other company/companies’ profits within the same accounting period only. This is known as “group relief”.

A trading loss not applied to the current or previous accounting period is carried forward and used against profits of the same trade arising in later periods, without time limit.

Tax relief for a non-trading company’s finance expense in excess of the company’s profits for an accounting period may be claimed against financial profits of the previous year. Alternatively, this expense can pass to another UK group member for use against that member’s profits in the same accounting period.
under the “group relief” provisions. Any unrelieved finance expense is carried forward, without time limit, to be used against future non-trading profits of the company.

Capital losses are set against gains of the company for the same period, with any excess being carried forward, without time limit, for use against net gains of subsequent periods.

There are several anti-avoidance provisions which may deny the carry forward of all types of tax losses when a group purchases a company with existing tax losses, and the main reason for the acquisition is to access these tax losses.

**Research and Development Tax reliefs**

Enhanced tax relief is available to companies which conduct R&D for the purposes of resolving scientific or technological uncertainty with a view to achieving an advancement in science or technology, or an appreciable improvement in existing technology.

There are two schemes of relief, one for small and medium sized companies (SMEs) and one for larger companies.

An SME is broadly a company with fewer than 500 employees and not more than either £100m turnover or a balance sheet total of £86m, taking into account certain linked and partner enterprises (e.g. group companies). SMEs may claim an enhanced tax deduction of 225% of their qualifying R&D spend and, if loss making, trade in losses for a cash rebate of just under 25p in the £ of the actual qualifying spend, thereby creating an additional source of cash-flow for the company.

Large companies may claim a tax deduction of 130% of their qualifying spend and do not currently have the cash-back option. However, this could change
INTRODUCTION
This chapter follows on from the overview of the UK business tax system set out in Chapter 4.2 and covers various areas of UK tax planning that an investor should consider, both with a view to realising tax savings and also avoiding unnecessary tax costs.

ACQUISITION OF A BUSINESS: ASSETS VS. SHARES
Asset acquisitions
An asset (business) purchase could be effected using a new UK company or by a new UK branch of the overseas company. As discussed in Chapter 4.2, a UK branch of an overseas company and a UK company are subject to UK tax on profits in broadly the same way. Therefore, an overseas investor wishing to purchase a business in the form of an asset purchase will need to take into account commercial, legal and non-UK tax factors in deciding a preferred route.

One of the key non-tax advantages of an asset purchase is that any liabilities or exposures within the selling company do not automatically transfer across to the purchaser.

Share acquisitions
A company is a separate legal entity and, as such, when an investor acquires a company it is acquiring all of that company’s history and liabilities. Therefore, any
unknown or contingent liabilities (as well as those which the purchaser is aware of) will effectively be inherited by the purchaser. For this reason, a purchaser will normally seek to obtain from the vendor an indemnity against such liabilities, whether or not they had crystallised as at the date of the sale.

One of the first questions an investor will need to address is the vehicle to be used to make the acquisition, i.e. should the acquisition be made:

- directly by the overseas investor;
- by an intermediate holding company set up in the UK; or
- by an intermediate holding company set up in a third territory.

Each investor will have their individual fact pattern that may influence the choice and, as such, specific advice should be taken. But examples of factors that could, from a tax point of view, influence a purchaser towards one or other of these acquisition vehicles include:

- Where overseas tax rates are higher than UK rates, there could be an advantage to making the acquisition using the overseas investing company in order to benefit from any financing tax deductions in that territory.
- Where the overseas investor does not have sufficient profits to offset financing costs, however, a UK debt-financed acquisition vehicle may be preferable.
- If the investor wishes to create a sub-group to facilitate the cross-border expansion of the target business, it may be appropriate to set up an intermediate holding company (either in the UK or elsewhere).
- Whether the overseas territory has a favourable tax regime for the holding of shareholdings and how any local “controlled foreign company” rules may affect this.

**Asset vs. share purchase**

When acquiring shares in a company, the existing tax profile of the target company will remain and so the purchaser effectively inherits this.

From a buyer’s point of view, the potential tax advantages of buying assets or shares include:

**Assets**

- The ability to obtain tax relief for the goodwill element of the deal price.
They can claim capital allowances for plant & machinery and other qualifying fixed assets based on the consideration allocated under the Business Purchase Agreement rather than on the existing tax value of those assets within the target company (assuming the former is higher).

They avoid 0.5% stamp duty (although stamp duty land tax would be payable if land is being acquired).

**Shares**

- Existing tax losses transfer across (but subject to anti-avoidance legislation aimed at preventing the acquisition of companies solely or mainly to enable the purchaser to benefit from these tax losses).
- If the current tax value of fixed assets is greater than the purchase price allocated to those assets, a share acquisition avoids a reduction in the amount on which capital allowances can be claimed.
- They avoid stamp duty land tax, which could be significant if there is valuable land within the target business (although there will be a 0.5% stamp duty charge on the consideration paid for the shares).
- There is greater flexibility to enable the vendors to reduce or defer tax where the vendors are to retain a direct or indirect stake in the target business (e.g. by exchanging shares in the target company for new shares in the purchaser).

There will often be a conflict between the interests of the sellers and the buyers. Buyers typically prefer to purchase assets and sellers will often prefer to sell shares. See below for the tax aspects of a disposal.

**Acquisition of a Business: Financing**

The funding for an acquisition could be sourced in a number of different ways – e.g. existing cash resources within the investor, third party borrowings, equity injection by the ultimate shareholder(s) – and this will need to be taken into account when determining the optimal financing structure from a tax point of view.

Likewise, a review will need to be carried out of the tax regimes of both the overseas territory and the UK in determining the optimal place for locating interest deductions if the funding is to be effected through loan finance.

Questions that may need to be considered include:

- **Is the acquisition to be made by the overseas investor directly or by a UK acquisition vehicle?** Clearly, if the investor is to make the acquisition
directly, any external funding will need to be taken out by the investor (even if the assets of the target business are used as security, which has been possible over recent years following the relaxation of the “financial assistance” rules).

- **What capacity do the investor and the target company each have to utilise interest deductions against forecast taxable profits?** No benefit will accrue from deducting interest in a territory in which there are insufficient taxable profits against which those deductions can be offset.

- **Is the corporate tax rate in the investor’s home territory higher or lower than the UK rate?** The preference may be to locate borrowings (and hence interest deductions) in the territory with the higher tax rate.

- **What restrictions apply to the deductibility of interest in the UK and the overseas territory?** In relation to the UK, for example, transfer pricing/thin capitalisation considerations and the “worldwide debt cap” will need to be taken into account even if all or some of the finance is being provided by a third party (see Chapter 4.2 for more detail).

- **Will the borrower be required to withhold tax on payment of interest?** Third party lenders will often include a gross-up clause such that any withholding tax will effectively be a cost to the borrower rather than a lender. Therefore the borrowing may need to be structured in such a form or location that avoids or minimises any withholding taxes.

Consideration will also need to be given to how interest payments are to be financed. Where the acquisition is funded out of existing cash resources provided by the investor, this may be less of an issue, but where third party lenders are involved, the investor will need to have a clear plan of how payments of interest are to be funded. A UK company can remit cash to an overseas parent free of UK tax, whether by way of dividend or an upstream loan (although such a loan should itself be interest-bearing in order to meet transfer pricing rules), but the parent will need to consider the taxation of such receipts under its local tax regime. In this regard, it should not be assumed that an upstream loan would be tax-free for the investor, as some tax regimes can treat such loans as deemed dividends.

**Repatriation of Profits**

No withholding taxes are charged on a repatriation of profits. This applies to dividends paid by a UK company, irrespective of the identity of the shareholders, as well as to repatriation of branch profits to head office.

As well as the use of dividends, groups should also consider the extent to which
other charges should be levied on the UK business – for example, royalties, service fees and management charges. Provided that such charges relate to the UK business and are calculated on an arm’s length basis (so that transfer pricing legislation is not applied), those charges can be deducted against UK taxable profits. The withholding tax position on such payments is covered in Chapter 4.2.

**Tax Groups**
Where an investor has an existing UK business, there will be advantages to structuring the acquisition so as to create a UK tax group. The main advantages are:

- Current period UK trading profits of one company can be sheltered from tax by using trading losses of another UK group company arising in the same accounting period. This is known as “group relief”.
- Capital assets can be transferred between UK members of the tax group without crystallising a tax charge. This would enable the tax-neutral combination of two UK businesses, if commercially desirable.
- Capital gains arising in one company can effectively be offset against brought forward non-trading losses (including capital losses, expenses of management and non-trading loan relationship debits) of another company in the UK group.

Where investors are part of a consortium, it is also possible in certain scenarios to use some of the tax losses in the consortium-owned company to shelter taxable profits arising in one of the consortium members.

The definitions of “group relief” groups and capital gains groups differ and so care must be taken where companies are not 100% owned, since in some situations not all of the above benefits of tax grouping will be available.

“**Group relief**” group: Comprises companies in which a shareholding of at least 75% is held directly or indirectly by the parent company (provided that the shareholder is also entitled to at least 75% of profits available for distribution and assets on a winding up). Non UK resident companies can be taken into account when tracing 75% ownership. In Figure 4.3.1, tax losses can be surrendered between UK 1 (owned 80% directly) and UK 3 (owned 81% indirectly). However, UK 2 is owned only 72% indirectly by Overseas Parent and therefore UK 2 cannot surrender losses to UK 3 (or vice versa).
Figure 4.3.1 – Example of how “group” relief may be applied according to levels of ownership

**Capital gains group:** This comprises companies which are held at least 75% by their immediate parent and which are indirectly held more than 50% by the top company in the group (provided also that the top group company is also entitled to more than 50% of profits available for distribution and assets on a winding up). Thus, in the above diagram UK 1, UK 2 and UK 3 are all part of the same capital gains group.

A tax group cannot be formed unless there is a common corporate parent company. Therefore, if an individual investor directly owns a number of UK companies, that investor will need to interpose a common holding company (which need not be a UK company) in order to create a tax group as illustrated in Figure 4.3.2:

**Figure 4.3.2 – Creating a tax group**
Even where there is no tax group in place, i.e. the individual holds both companies directly, the relationship between the two UK companies is such that they may still be regarded as associated or connected with each other for UK tax purposes. Hence:

- Transfer pricing rules can still apply to transactions or dealings between the two companies, to ensure that they are taxed on an arm’s length basis.
- Transfers of assets must be for an arm’s length consideration, failing which HMRC can substitute an arm’s length value for the actual consideration.
- In determining the corporation tax rate payable by each company and, particularly, whether the small profits rate or marginal relief is available, both companies must be taken into account in calculating the number of “associated companies” – see Chapter 4.2 for the impact of this on the corporation tax rate payable.

Exit Considerations

When structuring an acquisition, an investor should also be mindful of the likelihood of a future exit, what form that exit might take and the tax implications of such an exit event.

**Business held via a UK branch of an overseas company**

- The disposal would need to be effected via an asset sale (assuming that a sale of the overseas company would not be feasible).
- This will trigger a UK tax liability, with any gains on the sale of chargeable assets being taxed at the prevailing corporation tax rate. Overseas tax may also be payable (subject to double tax relief for UK tax paid, depending on the tax regime in the overseas territory).
- The branch could be packaged up into a new UK company, with the overseas investor selling that new company. This is a more complex area and could give rise to both UK tax charges in the new company and overseas tax charges in the overseas company.

**Business held within a UK company**

- Gives the flexibility to sell via a sale of assets or sale of shares.
- A sale of shares would generally not give rise to a UK tax liability within the target company (although a “de-grouping charge” could arise if the UK
company holds assets that were transferred into it from another UK group company within the preceding six years). If the overseas parent company benefits from a “participation exemption” regime, this could enable a sale of the business, by way of a sale of shares, free of both UK and overseas tax.

- A sale of assets would generally be less tax effective, since a UK tax charge would arise in the UK company on any gains and an overseas tax charge could arise on a subsequent remittance of the disposal proceeds by the UK company.

**Employee Incentivisation**

Where an investor wishes to incentivise or recruit/retain key employees by means of the issuing of shares in the target business, there are a number of different share plans that can assist in achieving this objective in a tax efficient way. Ultimately, the most appropriate plan will be dependent on commercial requirements and the characteristics of the investors (e.g. UK vs. overseas; company vs. individual).

The area of share options and employee incentivisation is a complex one on which specialist advice should be sought.

**Investor Tax Reliefs**

There are also incentives aimed at encouraging UK resident individuals to invest in smaller, higher-risk trading companies, by offering tax reliefs for the purchase of new shares in such companies. So far as direct investment in companies is concerned, the main schemes are as follows.

*Enterprise Investment Scheme (EIS)* – Under EIS, an investor can claim income tax relief (i.e. a reduction in their income tax liability) of up to 30% of the amount invested (up to a maximum investment of £1,000,000 in a single tax year). The investor can also use the amount invested to defer other capital gains (whether or not on shares), with the deferred gain crystallising when the EIS shares are disposed of. In addition, disposals of EIS shares after three years may be free from capital gains tax. EIS is aimed at smaller, unquoted companies and enables such companies to raise up to £5m in any 12 month period.

*Seed EIS (SEIS)* – An individual subscribing for shares that qualify for SEIS can claim income tax relief of up to 50% of the amount invested. In addition, disposals of SEIS shares after three years may be free from capital gains tax. (For the tax year commencing 6 April 2012 there is also an exemption from capital gains tax on gains realised from disposal of other assets, where the gains
are reinvested through the SEIS in the same tax year.) SEIS is available for
shares issued between 6 April 2012 to 5 April 2017 and is targeted at companies
whose trade is less than two years old and whose assets (pre-subscription) do not
exceed £200,000.
INTRODUCTION
Outsourcing non-core functions is increasingly common for businesses large or small. Engaging an external provider can release a company’s senior management team from often time consuming and burdensome fiscal compliance, allowing them to focus on the activities that really matter to the growth and success of the business and giving them piece of mind that the company is being looked after.

WHY OUTSOURCE FINANCIAL FUNCTIONS?
Compliance
When someone creates a company in the UK and becomes a director there are a number of responsibilities that the individual takes on. There are both civil and criminal penalties if these rules are not complied with. One responsibility is to maintain proper accounting records and by outsourcing the financial function this can help in ensuring local legislation is met. This is a key benefit to outsourcing the finance function and can give the security and peace of mind that the business is compliant.

Risk management
Every business investment carries a certain amount of risk. Markets, competition,
government regulations, financial conditions and technologies can all change quickly. An external outsourcing provider is responsible for keeping abreast of regulatory changes and ensuring that the business is up-to-date and fully compliant. This is particularly relevant for inward investment organisations where the parent company and the management of the organization operate outside of the UK and are therefore less exposed to or aware of regulatory changes. The result of non-compliance can be hefty penalties and fines.

**Local knowledge**
Using an external provider with local knowledge and experience ensures the investor is aware of the country-specific taxes and concessions that may be available to them. This is an area where a proactive provider may be able to save the business both time and money.

**Staffing and recruitment**
It can be expensive to recruit a new resource and getting the right resource to cover all requirements can be difficult when a business is in its early stages. There tends not be enough work for a full-time financial controller and issues can arise which need a greater level of skill than a regular book-keeper can provide. Recruiting and training staff can also take time which can be avoided with the use of a suitably experienced outsourcing provider.

**Additional resource**
If staff are recruited there may be busy times of the month or year when extra support may be needed. This could be to meet deadlines, provide cover for a member of accounting staff on long term leave, assist with accounting reconciliations or incomplete records, or to enable post acquisition accounting alignment. In these situations an external outsourcing provider can be flexible in the level of resourcing provided, both in terms of skills and manpower, enabling the business to cope with the peaks and troughs in its workflow. This can provide greater continuity in the staff engaged and ensure that knowledge is not lost.

**Variable costs**
Outsourcing converts fixed costs into variable costs. In the early stages of a new business venture when the pace of growth is uncertain, outsourcing can help management control costs by managing them flexibly.
**Legal redress**
An external supplier will provide services in line with a legally binding contract which has financial penalties and legal redress. This gives the business a level of accountability and assurance which does not exist when services are provided by an internal team. However consideration should be given to the size and reputation of the firm delivering the service and its ability to resolve any issues that might arise.

**Focus on the core business**
Productivity can be increased as an external provider can take on volume transactions or labour-intensive procedures and carry them out quickly and efficiently using tried and tested processes. This allows the company’s management team and staff to focus on the core functions of the business where they add most value. An increase in productivity can directly influence the bottom line.

**Technical expertise and core skills**
Using an external provider can give you access to a larger pool of talent and technical knowledge. This may manifest itself in the production of consolidated reporting or the consistent reliability of monthly reporting deadlines being met. It also means that you have a quick route to deal with business critical matters such as resolution of tax queries or the settlement of payments on a local basis.

**Payroll**
The key area to any business is the people who drive it forward. With international business and personnel being transferred across borders there can be both visa issues and tax issues for the individual and the company. Outsourcing the payroll, expatriate tax advice and immigration support to one provider means that employees are looked after when overseas and local legislation is complied with. This means that they are paid on time and local tax issues are dealt with.

**WHICH FUNCTIONS CAN BE OUTSOURCED?**

**Setting up a company**
- Company formation
- Registration with relevant authorities

**Accounting & compliance**
- Bookkeeping
Financial Outsourcing: An Overview

- Tax compliance
- Preparation of financial statements

**Management accounting & reporting**
- Management accounts production
- KPI reporting
- Consolidation packs

**Payroll**

**Legal & administration**
- Company secretarial services
- Fiduciary services

**Interim accounting solutions**
- Provision of manpower
- Accounting support
- Emergency accounting

**High volume business processes**
- General ledger
- Accounts receivable
- Accounts payable
- Payroll
- Fixed assets

**Non-financial solutions**
- HR
- Procurement
- Insurance claims
4.8 UK TAXATION FOR FOREIGN NATIONALS

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This chapter gives a brief overview of the UK tax considerations for a foreign national coming to the UK to work. By necessity, it only highlights the areas to consider and gives some indication of the current law. Advice should be sought in all respects, preferably before coming to the UK.

BASIS OF TAXATION
There are three concepts which need to be understood with regard to taxation in the UK. These are:

1) Residence
2) Ordinary residence
3) Domicile

Residence
In the UK, the question of residence has always been a matter of case law and interpretation by the UK tax authorities, being broadly the number of days a person spends in the UK and their connections to the UK. The current rules can be summarised as:

A person is UK resident if:
● They spend 183 days or more in the UK in any tax year,
● They intend to stay in the UK for at least two years, spending more than 90 days per year in the UK, or
● They visit the UK for an average of 90 days per tax year over a period of three years with no intention of remaining in the UK, with residency commencing from the beginning of the fourth year.

The UK Government is intending to introduce a new statutory residence definition which will apply from 6 April 2013. The draft legislation contains three parts detailing rules which will result in conclusive non-residence, conclusive residence and a list of “connecting factors” which will determine residence for the individuals who do not fall within the conclusive tests.

The new rules are extensive and exhaustive but generally if a person comes here to work full time they will be resident in the UK for tax purposes.

Ordinary residence
In the UK there is currently a further residence test, known as “ordinary residence” which considers whether a person is habitually resident in the UK year after year.

It is possible to be resident but not ordinarily resident in the UK for a tax year if, for example, a person normally lives outside the UK but is in the UK for 183 days or more in a particular tax year.

An individual will be treated as ordinarily resident from the date of arrival if the intention is to stay more than three years.

Ordinary residence can give the remittance basis to a UK domicile who is resident, but not ordinarily resident for foreign investment income, and give the remittance basis on foreign employment duties. Conversely, if someone is not resident but is ordinarily resident in the UK, they can be liable to UK Capital Gains Tax on disposals.

The use of ordinary residence is to be abolished for all tax purposes except the remittance basis on foreign employment duties, currently known as “overseas workday relief” for non-UK domiciled individuals only.

Domicile
The concept of domicile is relevant to taxation in the UK only if a person is not domiciled in the UK.

Domicile is a concept of general law; not a tax law and it is determined in a different way to residence and ordinary residence.
There are three types of domicile relevant to Income Tax ("IT") and Capital Gains Tax ("CGT"). These are:

- **Domicile of origin**: An individual will normally acquire a domicile of origin from their father at birth. An individual’s domicile of origin need not be the country in which the individual was born. This is determined by the relevant parents’ domicile at the child’s birth.

- **Domicile of choice**: An individual has the legal capacity to acquire a new domicile at the age of 16. Whilst it is possible to acquire a domicile of choice, this means much more than simple residence and a person must settle in another country permanently and sever ties with the country of origin. It is extremely difficult to acquire a domicile of choice.

- **Domicile of dependence**: A child under 16 cannot have a domicile of choice. Whilst under 16 their domicile will follow that of the person on whom the individual is legally dependent.

**UK TAXATION**

In general, individuals resident in the UK will be liable on all their worldwide income and gains, known as the “arising basis” of taxation. This means that they will pay UK tax on all of their income as it arises and on their gains as they are realised, wherever that income and those gains are in the world.

Whilst an individual is non domiciled he can choose whether to use the “remittance basis” of taxation which is discussed later in this chapter.

**Personal allowances**

In general, individuals resident in the UK are entitled to an income tax personal allowance. This is set at £8,105 for the 2012/13 tax year and is the amount of income each individual can receive before they are liable to tax. For individuals with income over this amount, tax is only charged on income in excess of £8,105.

However, a personal allowance will not be available in certain circumstances, and so the individual will be chargeable to tax on all of their income. The allowances are withdrawn either where the income is in excess of £100,000 (and it is withdrawn gradually), or where the remittance basis is being claimed under certain circumstances.

There is also a CGT annual allowance available to reduce chargeable gains, which is currently set at £10,600 for the 2012/13 tax year.
UK Tax rates
Most forms of income are chargeable to tax at the following rates for the 2012/13 tax year:

- £0 - £8,105  0%*
- £8,106 - £42,475  20%
- £42,476 - £150,000  40%
- £150,000 +  50%

* If the personal allowances are still available.

CGT for individuals is currently 18% if their marginal rate of income tax is 20% or below and 28% if their marginal rate of income tax is 40% or above.

Access to the remittance basis
Where an individual is resident in the UK, but not ordinarily resident or resident but not domiciled in the UK, they will have a choice whether to use the arising basis of taxation and therefore be taxed on their worldwide income or gains as they arise or to use the remittance basis of taxation.

If a claim for the remittance basis is made, then the individual will only be liable to tax on income and gains arising in the UK and any overseas income and gains “remitted” (i.e. brought to or used to benefit the individual) in the UK.

Where an individual has been in the UK for less than 7 years, he can claim the remittance basis without paying for the privilege, however this will result in the loss of his personal allowance and CGT allowance.

Long term residents in the UK (broadly resident seven out of nine years) must pay a £30,000 remittance basis charge (RBC). Furthermore, where an individual has been in the UK for 12 out of the last 14 years, this RBC is increased to £50,000 per annum.

This is a particular area which needs specialist advice and would require a whole book to cover the rules, planning and anti avoidance in sufficient detail.

ON ARRIVAL
There are no specific tax forms which need to be completed on arrival in the UK, other than to register with HMRC as necessary. There are likely to be two registrations, one to obtain a National Insurance number and one to register with HMRC for tax purposes. Both of these are discussed briefly below.
National Insurance Contributions
Both employers and employees, including self-employed people, make compulsory national insurance contributions to HMRC in order to pay for a number of social benefits including the state pension and jobseeker’s allowance. Men over the age of 65 and women over the age of 60 are exempt from making these contributions, although the age limit for women is in the process of rising from 60 to 65 to equalise with men. For employees, their employers will calculate their NIC and deduct this from their gross pay using PAYE; self-employed persons must work out their contributions themselves.

All UK residents over the age of 16 must have a National Insurance number if they wish to work in the UK and have their contributions credited to their “account”.

So, before working in the UK, an individual will need to obtain a National Insurance number. This can be obtained by contacting HMRC and arranging for either an 'Evidence of Identity' interview or agreeing to submit a postal application in limited circumstances.

If an employee is being sent to the UK by his employer, the position in respect of social security will vary depending on the country from which the employee is being sent. It may be possible for the employee to continue paying social security in their home country or it may even be compulsory. Either way, agreement will need to be obtained from the tax authorities to ensure the appropriate compliance requirements are met.

In some circumstances, a 52 week NIC holiday may be appropriate, where the employee continues to pay social security in their home country for the first 52 weeks and then commences paying NIC in the UK.

National Insurance rates for 2012/13 are 12% for employees up to the higher rate of income tax and 2% thereafter, and for employers they are 13.8%. There is a small exemption broadly equivalent to the personal allowance.

UK tax return requirements
The UK tax year runs from the 6 April one year to 5 April of the next. The UK operates a “self assessment” system meaning that the responsibility to ensure the correct amount of tax is paid rests with the individual taxpayer. A UK tax return is likely to be required where the following circumstances apply:

• the individual is the director of a company in the UK; or
• he chooses to make a claim for the remittance basis; or
• he has income which is subject to tax (or a further tax liability) in the UK.
If an individual needs to be within the self assessment system he needs to complete form SA1 (obtainable from HMRC) to be registered.

HMRC does not generally assist an individual in the preparation of his tax return but they can ask questions and challenge certain items on the return. In general they are able to do this for up to a year after the return has been filed, though in certain cases this can be extended for up to 6 years.

HMRC may request that a return is prepared, but if they do not request a return, the individual is responsible for notifying HMRC that he is required to prepare a return for a particular tax year.

Completed tax returns need to be filed with HMRC by 31 October following the tax year end where the individual files a paper tax return. In most cases tax returns should be filed online as this provides a much more efficient service from HMRC and in addition, this extends the filing deadline to 31 January following the end of the tax year.

If the tax return is filed late, an automatic penalty of £100 will be charged which may be increased if the delay in filing is extended beyond 3 months.

Any additional tax liability will need to be paid to HMRC by 31 January following the end of the tax year. Provided the return has been processed by this time the taxpayer should receive a reminder from HMRC, providing details of how to pay and a payslip to use when making the payment.

If the individual’s return has not been processed by this time, he is still liable to pay his tax by 31 January.

If the tax is paid late, interest will be charged from the day after the due date. In addition, if the tax has not been paid within a month of the due date, a surcharge of 5% of the outstanding balance will be levied. Further charges may be raised if the tax liability remains unpaid after this date.

For an individual coming to the UK, the date of arrival and some brief details on the individual intentions should be disclosed in the annual income tax return for the tax year of arrival.

**OTHER TAXES**

**Capital Gains Tax**

Mention has been made earlier of CGT with regard to the annual allowance and the tax rates at which it is charged. CGT is broadly charged on any gain made on holding an investment, such as shares or property.

There are several valuable exemptions, the most important one being an exemption for an individual’s main residence. In addition, there are certain tax breaks which are available to encourage investment. One of those is
Entrepreneurs’ Relief, described below.

**Entrepreneurs’ relief**
Entrepreneurs’ Relief (ER) is available for “qualifying business disposals”. The effect is to reduce the rate of Capital Gains Tax from 18% or 28% to 10%, for total lifetime gains of £10 million.

A claim for ER can be made more than once, but the total cumulative gains cannot exceed £10 million. If this is the case, any gains over this limit will be subject to the higher rates of CGT.

A “qualifying business disposal” includes a disposal of shares in a trading company, or the holding company of a trading group.

ER is normally available provided that, for a period of 12 months ending with the date of the sale, the individual holds at least 5% of the ordinary share capital; can exercise at least 5% of the voting rights and is an officer or employee of the company or of one or more of the companies which are members of the trading group.

Compliance with the rules should be checked carefully.

**Inheritance tax**
The charge to Inheritance Tax (“IHT”) is based on where the asset is situated and the domicile of the person concerned, residence is irrelevant.

**Deemed domicile**
The concept of deemed domicile only applies for IHT purposes, and is essentially an anti-avoidance provision.

If an individual comes to the UK he will be deemed domiciled in the UK once he has been resident in the UK for seventeen out of twenty years. Certain Double Taxation Treaties may override these rules and should be checked carefully.

**Basis of taxation**
IHT is an integrated lifetime transfer and estates tax, and is a tax on capital transfers of value by an individual on certain lifetime gifts which are taxed immediately, lifetime gifts where the donor dies within seven years from the date of the gift and the chargeable estate upon the individual’s death.

Each individual is entitled to a nil rate band (NRB) (currently £325,000 for 2012/13). Only transfers of value exceeding this band are liable to IHT. Any unused NRB can now be shared by spouses/civil partners on second death. The NRB is not an annual exemption. It is a seven year cumulative band which takes
into account the previous seven years’ chargeable transfers when determining whether a transfer has exceeded the NRB.

IHT is currently charged at rates of: 20% for lifetime transfers and 40% on death.

There are three types of lifetime gift, exempt transfers, potentially exempt transfers and chargeable lifetime transfers.

Upon death an individual is deemed to have made a transfer of value equal to the whole of their chargeable estate, which is the total value of all their capital assets less any amounts owing at the date of death.

Examples of the most common exempt transfers are transfers between spouses and civil partners, gifts to UK registered charities, the annual exemption – the first £3,000 of gifts made each tax year – and small gifts up to £250 de minimis. There are other valuable exemptions available.

The most common chargeable lifetime transfers (CLTs) are gifts to trusts. All gifts to trusts (except charitable trusts or trusts for the disabled) are CLTs.

Potentially exempt transfers are all lifetime gifts between individuals. During the donor’s lifetime the transfers are treated as exempt from IHT and if the donor survives seven years from the date of the gift the transfer is completely exempt.

If the donor dies within seven years of the date of the gift the transfer becomes chargeable, although the amount chargeable depends on how many years have passed between the date of the gift and the date of death.

OTHER CONSIDERATIONS

Remuneration packages
Any benefits provided to an employee, either in the UK or in their home country, will need to be considered when calculating the UK tax position and some of the more popular benefits are mentioned briefly below.

It is also possible to use share schemes and incentives to remunerate in a tax efficient manner and these are discussed elsewhere in the book.

Common benefits
If accommodation is provided rent free or at a subsidised rate, the relevant benefit of that will be chargeable to both tax and NI. If the value of the property provided is in excess of £75,000, the tax benefit is particularly high and there are ways of minimising the tax liabilities.

If the employer helps with the move to the UK, there are some valuable reliefs worth up to £8,000 but it is important that advice and planning is undertaken before the move takes place.
If an employee is sent to the UK on a temporary secondment for less than 24 months it may be possible to claim tax relief in respect of the expenses in attending the “temporary workplace” in the UK. These expenses would include, but not restricted to accommodation costs, utilities, ordinary commuting to the temporary workplace and subsistence. This relief may extend to cover travel between the UK and their home country.

The taxable benefit of a car is generally calculated on its CO2 emissions and the list price before discounts. This has led to a move towards more fuel efficient cars and can make a difference to the overall taxable benefit.

**Double taxation**

It is always worthwhile to remember that there is a guiding principle that no one should suffer double taxation on the same income, gains or assets in more than one country. However, how this relief is given depends on the country of origin and any double taxation treaty which may be in force with the UK.

Taxation could be due in both countries, the country of origin only, or the country where the source is “arising”. This changes depending on the type of income or gains and whether there is an old treaty, a new treaty or even no treaty at all.

Once again, the interaction between the countries should be checked before the foreign national arrives in the UK if at all possible.