An Overview of UK Taxation

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1. Corporation Tax

In each accounting period, the Annual Investment Allowance gives a 100% writing down allowance on the first £500,000 spent on general plant and machinery. After this initial allowance, the rate of capital allowances for plant and machinery is 18% a year on the reducing balance basis.

There is only one major tax on a company's profits, which is Corporation Tax, currently levied at a rate of 20%. The rate will be reduced to 18% by 2020.

1.1 The charge to Corporation Tax

Corporation Tax is assessed on total taxable profits and chargeable gains in respect of each accounting period. Profits charged to Corporation Tax are calculated by adding together income from various sources. These will principally include trading profits, rents, investment income, deposit interest and chargeable gains.

1.2 Capital allowances

Capital allowances allow the cost of the capital assets to be written off against the taxable profits of a business. These allowances fulfil the role of commercial depreciation charged in accounts. In each accounting period, the Annual Investment Allowance gives a 100% writing down allowance on the first £500,000 spent on general plant and machinery. After this initial allowance, the rate of capital allowances for plant and machinery is 18% a year on the reducing balance basis. Although there are some specific exceptions, most assets qualifying as plant and machinery are pooled together and the value of the pool is written down accordingly.

1.3 Dividends

Distributions received by small companies will be exempt where the payer is resident in the UK or a territory which has concluded a double taxation treaty with the UK.

1.4 Chargeable gains

UK resident companies pay Corporation Tax on their chargeable gains at the relevant Corporation Tax rate. Foreign companies which are established in the UK are also liable to pay Corporation Tax on chargeable gains arising from the disposal of assets situated in the UK and used for the purposes of the UK establishment or its trade. This chargeable gain is calculated as the difference between the net proceeds of the sale of a chargeable asset and its purchase price, together with any allowable expenditure incurred on that asset.

There is an exemption for capital gains and losses on substantial shareholdings in trading companies disposed of by corporate shareholders. This is commonly referred to as the "substantial shareholdings exemption". A non-UK company disposing of shares in a UK company will not generally be subject to UK taxation, unless it has a permanent establishment in the UK.

1.5 Transfer pricing

A small enterprise is exempt from the transfer pricing rules unless it has transactions with a resident of a non-qualifying territory – broadly a tax haven.

Companies which are part of a medium-sized enterprise are similarly exempt unless HMRC issues a direction that the transfer

1. Corporation Tax (cont.)

pricing rules should apply in the specified circumstances. Such an issue is likely to require HMRC to undertake a transfer pricing audit and establish a prima facie case that transactions are not independent and impartial.

1.6 Enterprise Investment Scheme

The Enterprise Investment Scheme (EIS) is designed to assist companies in the UK to raise finance. The UK offers generous tax reliefs to UK taxpayers who subscribe to ordinary shares in independent and unlisted trading companies which meet certain criteria. This relief is also offered for investment in companies that conduct research and development. The company is only required to have a permanent establishment in the UK and does not have to be incorporated or trading in the UK for the relief to be offered.

Most trades conducted by a company, or within a group of companies will qualify for EIS purposes. Legislation specifies trades which will not qualify, including those with an element of asset backing – the tax relief is given because the investments are expected to be high risk. There are many complex conditions which must be met in order to both obtain and retain the income tax relief. However, the upfront income tax relief and disposals not subject to capital gains tax make subscription for shares in an EIS qualifying company a risk that some investors are willing to take.

1.7 Patent Box

In order to encourage innovation and increase tax competitiveness in the UK, a lower Corporation Tax rate of 10% will apply to profits arising from patented technology. This relief applies to worldwide profits from patented inventions protected by UK Intellectual Property Office (IPO) or European Patent Office (EPO) patents.

Besides the royalties and income from the sale of intellectual property, profits from sales of products which incorporate a patented invention may qualify. In addition to this, it is not necessary for the UK company to own the patent rights entirely; an exclusive licence to exploit the patent is sufficient. Where the development of a patent has been undertaken elsewhere in the group, the UK company will be able to claim Patent Box relief, provided that the UK business has sufficient management activity in relation to the intellectual property.

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VAT is applied by means of an input/output system. When a business buys goods or services, it pays VAT to the supplier (input tax) and when goods or services are sold, whether to another business or to a final consumer, it is required to charge VAT (output tax).

2. VAT

VAT is charged on the supply of goods and services in the UK made by a taxable person in the course of furtherance of a business, unless the supplies are an exempt supply. A UK taxable person is anyone registered or liable to be registered for UK VAT. The standard rate for VAT in the UK is 20%.

VAT is applied by means of an input/output system. When a business buys goods or services, it pays VAT to the supplier (input tax) and when goods or services are sold, whether to another business or to a final consumer, it is required to charge VAT (output tax). The total of input tax incurred by a business must be totalled periodically and deducted from the output tax charged. The balance of these amounts is paid to HMRC. As a result, the final consumer bears the cost of VAT on the final price of the goods or services they purchase.

A taxable person is required to register for VAT if their combined value of taxable supplies in the UK exceeded the registration limit in the preceding 12 months or if there are reasonable grounds for believing that the value of taxable supplies to be made in the next 30 days alone will exceed the registration limit. A business may also de-register if the anticipated value of the taxable supplies in the next 12 months is less than the registration limit.

3. Personal taxation

UK income tax is chargeable on any UK source income received by an individual in the UK if they are UK resident. Foreign income is subject to UK tax where the individual is either domiciled in the UK, or where the individual is not domiciled in the UK but their income is remitted there or they choose to be taxed on it on an arising basis. The starting rate for income tax is 20%.

If an individual elects to be taxed on an arising basis, they will be assessed on their worldwide income and gains as they arise. Where a person elects to be taxed on the remittance basis, they will be subject to UK tax on all income and proceeds from gains on assets situated within the UK. In contrast to the arising basis, remittance taxation only causes non-UK income or proceeds to be taxed where they are remitted to or used in the UK. A remittance basis charge must be paid by all individuals who have spent seven of the past nine tax years in the UK and elect to be taxed on a remittance basis. This charge is £30,000 per annum.

Under existing concessionary rules an individual may, in certain circumstances, split a tax year when entering or leaving the UK. A new statutory split year treatment is suggested to split tax years in to periods of residence and non-residence. This will broadly put the concessionary treatment onto a statutory basis.

In terms of capital gains tax (CGT), individuals who are resident in the UK are entitled to an annual personal allowance and CGT exemption. This means that an individual will not be taxed on income or capital gains which fall below these thresholds. It should be noted that individuals who elect for the remittance basis to apply and are resident in the UK but are not domiciled there are not entitled to the personal allowance or the capital gains tax exemption.

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4. Entrepreneurs' Relief

Entrepreneurs' Relief is available for individuals who make a material disposal of a business asset. Included in this category are shares or securities of the individual's "personal" company. These include trust business assets as well as assets owned by individuals which were used in a business where the individual was a partner or the entity was their personal company.

There are qualifying conditions attached to each category, for example in the case of the personal company the requirements are that for at least 12 months prior to the disposal the individual held at least 5% of the ordinary share capital and, by virtue of that holding, 5% of the exercisable voting rights. The company must be a trading company or a holding company of a trading group and the individual must be an officer or employee thereof.

The rate of tax on gains qualifying for Entrepreneurs' Relief is 10%. The maximum amount of gains which qualify for Entrepreneurs' Relief during an individual's lifetime is £10 million.

5. Payroll taxes

All UK employers must operate a Pay As You Earn (PAYE) payroll system. Over each UK tax year, an employer must account to HMRC for the full amount of any tax and National Insurance contributions that it must deduct from payments made to employees. UK employers are required to operate the system without exception and to keep appropriate records and complete the necessary filings. Employers are required to submit their PAYE information when paying their employees each month.

6. Research and development

Relief for expenditure of revenue on research and development that is related to a company's trade and is undertaken by the company or on its behalf is wholly allowable as a tax deduction. In certain circumstances, enhanced relief is available.

Expenditure of a capital nature on research and development related to a company's trade is also wholly allowable as a tax deduction. However, no allowance is available for expenditure on land. If any proceeds are received from the disposal of the capital assets, the receipt is taxed as a trading receipt.

A small or medium-sized enterprise may undertake research and development which is related to the company's trade. In addition to this, they may claim their expenditure on staffing costs as well as software and consumable items. In certain circumstances, companies incurring research and development expenditure of a specific nature are entitled to claim research and development tax relief. Expenditure for which state aid is received is excluded. Research and development which is deemed to be funded or subcontracted to the company may only be claimed under the large companies scheme.

As is the case with small and medium-sized enterprises, large companies may claim tax relief for research and development, staffing costs and software development. In addition to this, large companies may include expenditure on any outsourced staff in respect of research and development carried out by it. Subcontracting of research and development to a research organisation, university or other third party, as well as contributions to such persons for such research and development, may also be deducted from their tax liability provided that the expenditure is relevant to the company's activities.

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7. Contact us

We welcome the opportunity to discuss any of the issues raised in this guide or any other questions you might have. If you would like to know more, please get in touch with us.

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Thinking about international expansion?

Working out what's important to your business plan

In any international expansion there are factors you need to address; make sure you have dealt with all local formalities and are operating in a fully compliant manner. Use this chart to consider the questions you need to answer when thinking about expansion.

1. What type of business will you establish?	2. Where will this business fit into your existing structure?	3. How do you establish an entity?	4. How will the entity be funded?	5. What do you need to do to start activities?
▪ PLC ▪ Limited company ▪ Partnership	▪ Branch ▪ Subsidiary ▪ Separate entity	▪ Incorporators ▪ Registration ▪ Founding documents ▪ Trading name	▪ Foreign investment ▪ Equity investment ▪ Loans and securities	▪ Bank account ▪ Business insurance ▪ Property ▪ Work permits

6. Which tax structures apply?	7. Will you have employees?	8. Which legal system applies?	9. Which organisational matters should you consider?	10. How can Sable help you?
▪ Corporation Tax ▪ Tax on dividends ▪ Customs and import duty ▪ VAT	▪ Contracts ▪ Benefits ▪ Dismissal	▪ Employment ▪ Intellectual property ▪ Land ownership	▪ Cash management ▪ Preparation of annual accounts and annual reporting ▪ Payroll ▪ Auditing	▪ Relocation ▪ Company set up ▪ Manage business operations