



P R E F A C E

This profile on Doing Business in the United Kingdom has been prepared by Baker Tilly, the independent member of Baker Tilly International in the United Kingdom (UK). The profile is designed to provide information on a number of subjects important to those contemplating investing or doing business in the UK.

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Doing Business in the UK has been designed for the information of readers. Whilst every effort has been made to ensure accuracy, information contained in this booklet may not be comprehensive and recipients should not act upon it without seeking professional advice.

Up-to-date advice and general assistance on UK matters can be obtained from Baker Tilly International's UK based member firm. Please see their details in the back cover of this booklet.

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1 INTRODUCTION

1.1 *Geography*

The United Kingdom (UK) covers an area of 94,246 square miles (244,100 square kilometres) and consists of England, Wales, Scotland and Northern Ireland. The Channel Islands and the Isle of Man are not included in this booklet as they have their own laws, governments and tax systems.

The climate is temperate with average temperatures of 4-6 C degrees in winter and 17-22 C degrees in summer and an annual average rainfall of 1100 mm. The south of England is significantly warmer than the North of England.

The country is mainly agricultural lowland with mountainous areas in Northern England, Wales and Scotland. Raw materials include coal and rich deposits of oil and gas under the North Sea.

A network of road and rail links radiates from London. The Channel rail tunnel provides fast rail and road access to Continental Europe. There are about 80 ports of commercial significance. London has the world's busiest international airport at Heathrow, and is also served by airports at Gatwick, Luton and Stansted. Other major international airports include those at Birmingham, Manchester and Glasgow in Scotland.

1.2 *Population*

The total population of the UK is 59.75 million. The main concentrations are in London (7.3 million), Birmingham, Manchester, Leeds, Bristol, Glasgow and Belfast in Northern Ireland.

1.3 *Political System*

The Queen is head of state but the country is governed by Parliament based at Westminster in London. Parliament comprises two houses, the House of Commons and the House of Lords. The Government is formed from the House of Commons by the political party winning the most seats in a general election. Elections must be held at least every five years.

Public services such as education, town planning, housing, refuse disposal and social and recreational facilities are provided by local authorities run by elected councillors.

The UK is one of 15 member states in the EU and is therefore subject to EU law.

1.4 Languages

English is the main language throughout the UK.

1.5 Currency

The monetary unit used throughout the UK is the pound, divided into 100 pence. Although it is a member of the EU, the UK is not part of the Euro area.

1.6 Economy

Britain has an open economy with international trade and investment forming a vital part. Exported goods and services account for one quarter of the gross domestic product. The economy is based on private enterprise with current government policy aimed at encouraging and expanding the private sector which now accounts for three quarters of gross domestic product and over two thirds of total employment. The only significant nationalised industry is Postal Services. Since 1993 the economy has grown at an annual rate of 2% to 3%.

The government's stated aim is that the markets operate with as little regulatory machinery as possible in order to stimulate competition. They are kept open and fair by bodies such as the Office of Fair Trading and the Competition Commission. In financial services, the Financial Services Authority is the regulator to protect the private investor.

The total workforce is approximately 28.5m, including 3.3m self-employed. 45% of employees are women. Unemployment ranges between 2% and 4%. There is a Government programme to revitalise inner cities and other areas where unemployment is high.

The rate of inflation has been in the range of 1% to 2% for the last few years.

2 BUSINESS ENTITIES AND ACCOUNTING

2.1 *Companies*

Commercial entities are usually limited liability companies with share capital. Companies may be limited by guarantee of their members rather than by shares, but generally it is only charities which operate in this way. A company may be incorporated either as a public or a private company. Only a public company ('plc') may offer shares or debentures to the general public. A public company must have an allotted share capital of at least £50,000. There is no minimum for a private company (Ltd). A public company must have at least two shareholders. A private company may have only one shareholder. There are no restrictions on the maximum number of shareholders for either type of company.

A private company need have only one director, but a public company must have at least two. There is no requirement that directors must be UK or EU nationals.

Where a foreign-based enterprise chooses to operate in the UK through a UK incorporated subsidiary company it will usually do so by means of a private company.

2.2 *Partnerships*

Partnerships can be either general partnerships, where the partners each have unlimited liability for the debts and obligations of the firm as a whole, or limited partnerships, where one or more of the general partners have unlimited liability and the limited partners have liability only up to the amount of their capital contributions. A partnership is defined in law as the 'relationship which exists between persons carrying on a business in common with a view to profit'. Except in Scotland, a partnership is not regarded as a separate legal entity distinct from its members.

The Limited Liability Partnerships Act 2000 came into effect on 6th April 2001 enabling all present unincorporated businesses and new businesses to operate through a new form of business structure: the Limited Liability Partnership (LLP). The LLP must have two or more members, and must conduct business with a view to profit. By

providing its members collectively with a form of limited liability, the LLP offers the prospect of asset protection to proprietors of unincorporated businesses for whom no such protection was previously available. The LLP is taxed in much the same way as a general (unlimited) partnership.

2.3 Sole Proprietorships

Many smaller businesses in the UK come into this category.

2.4 Branches

An overseas company can set up a place of business in the UK without forming a UK subsidiary company and in that case it is said to have a branch in the UK.

A branch is not a separate legal entity, but an extension of the foreign company, and the foreign company is therefore responsible for its liabilities.

2.5 Audit and Accounting Requirements

All businesses need to maintain proper books of account for taxation purposes and to retain the accounting records and associated documents for not less than 6 years. All Public companies, and LLP's and private companies with an annual turnover exceeding £1m must have their accounts audited by a qualified accountant.

2.6 Filing Requirements

All limited companies and LLP's must file accounts at a central registry (Companies House) but small companies may file in an abbreviated form. An annual return giving details of directors and shareholders must also be filed.

Branches of foreign companies must file details of the branch and its head office at Companies House within one month of setting up a branch. Abbreviated accounts of the foreign parent must also be filed annually although, depending on their nature, there is no requirement for them to be audited.

3.1 Exchange Control

There are no exchange controls in the UK on inward or outward investment. Foreign currencies can be bought and sold freely and there are no restrictions on the maintenance of foreign currency bank accounts in the UK.

There are no limitations on the repatriation of profits from the UK.

The UK, in common with the rest of the EU, has enacted laws to prevent the laundering of the proceeds of serious crime. Financial and some other institutions must obtain and retain satisfactory evidence of the identity of a potential customer before they do any business with that customer, even for relatively small sums. Failure to report suspicion of money laundering to the appropriate authorities can result in serious penalties.

3.2 Sources of Finance

3.2.1 Banking

The UK's central bank, the Bank of England, acts as banker to the Government. It is responsible, inter alia, for setting base interest rates through its Monetary Policy Committee.

Overdrafts with fluctuating interest rates are the most commonly used facility for financing working capital or to fund seasonally affected business. Technically, overdrafts are repayable on demand.

Banks also offer short, medium or long-term loans. The repayment terms are negotiable and the rate of interest may be fixed or variable. To obtain bank finance the business will normally be required to provide adequate security. Security will typically be in the form of a fixed or floating charge over the business assets, as well as, in certain circumstances, personal guarantees from the owners.

In addition to these traditional services the banks offer various other financing arrangements through subsidiaries or affiliates. These include instalment credit, leasing, factoring and invoice discounting and 'mezzanine' finance.

Branches of foreign banks in the UK will frequently arrange suitable finance for businesses from their own countries wishing to trade in the UK.

3.2.2 Stock Exchanges and Trading Facilities

The London Stock Exchange provides a market for shares and other securities issued by public companies. Admission to trading on the London Stock Exchange would normally be expected to make a company more attractive to private and institutional investors, and thus make it easier to raise new capital. To become and remain listed a company has to satisfy and abide by the extensive rules established by the London Stock Exchange and UK Listing Authority which is independent from the London Stock Exchange.

Within the main market, the London Stock Exchange has established techMARK for innovative technology companies.

For growing and fledgling companies the London Stock Exchange has established The Alternative Investment Market (AIM) which offers the benefit of potentially improved marketability of shares but with a more flexible regulatory environment. In addition, the OFEX market operated by OFEX plc provides a share-trading platform for companies and is often used by smaller and start-up companies to raise finance.

A company with securities that are not publicly traded may wish to enter these markets to raise new capital or to enable security holders to realise all or part of their investment.

The main methods of entering these markets are:

- admitting existing securities to trading
- an offer for sale - this involves an offer to the public of securities at a fixed price or by way of a tender for which a minimum price is stated. The offer is made by a third party such as a merchant bank or stockbroker
- a placing - this involves the marketing of securities to a more restricted group of investors.

For a company already listed on an overseas stock exchange an introduction can be made by a broking firm to allow its securities to be traded on the London Stock Exchange.

Once a company's securities are traded on the Stock Exchange further capital can be raised by rights issues, tender placings or by further offers for sale.

3.2.3 Venture Capital Companies

For businesses that are not large enough to consider Stock Exchange entry but which require finance, Venture Capital Companies can provide equity for start-ups, for development or for management buy-outs. Venture capital companies may also be a source of finance for a business that does not have sufficient security to borrow from a bank. But they may require a higher return than a traditional bank.

3.2.4 Enterprise Investment Scheme

The Enterprise Investment Scheme (EIS) is a government scheme designed to encourage UK resident individuals, through tax incentives, to invest in entrepreneurial unquoted companies. To be eligible for the EIS the company must be incorporated and reside for tax purposes in the UK and it must carry on a qualifying trade, largely within the UK.

Individual investors subscribing for not more than 30% of a qualifying company get tax relief at 20% on up to £150,000 per annum invested. EIS also provides a means of deferring capital gains.

EIS is not available for companies with a Stock Exchange Listing but may be available for AIM or OFEX companies.

3.3 Investment Incentives

The UK offers an attractive package of grants and incentives to encourage industrial development.

Foreign owned companies are eligible for the same incentives as UK owned companies.

References should be made to the British Government's Invest UK website www.invest.uk.com

3.3.1 Assisted Areas

The Assisted Areas are those parts of England, Scotland and Wales that are designated as Development or Intermediate areas. There are no Assisted Areas within 100 miles of London.

Regional Selective Assistance (RSA) is only available for projects within the assisted areas. Most manufacturing and some service industry projects are eligible.

RSA is given in the form of a grant of up to 15% of the capital expenditure costs of a project, depending on a number of jobs to be created or maintained.

3.3.2 Enterprise Zones

Since 1981, a number of Enterprise Zones have been created throughout the UK, offering various benefits to companies.

The benefits include 100 per cent tax allowances for commercial buildings and exemption from local property taxes. They are given for ten years from the date of the designation of the Zone. Most forms of development are also exempt from planning controls.

There are 10 Enterprise Zones still extant, mainly in the East Midlands and Northern England.

3.3.3 Free Zones

There are a number of Free Zones at selected UK ports and airports within which imported goods may be stored or processed duty free for re-exportation.

3.3.4 Local Authority Assistance

Regional government in the UK is conducted through local authorities. Local authorities are empowered to promote the economic development of their particular areas and have considerable discretion in how they go about this.

The assistance includes grants, loans or guarantees of borrowing and the provision of property and services.

Different circumstances apply to England, Scotland, Wales and Northern Ireland.

England

In England, the local authorities mainly work through a body known as 'English Partnerships'. This body supports projects that create or safeguard jobs and develop derelict land in the inner cities or Assisted

Areas. The assistance provided by this body mainly takes the form of rental guarantees and soft loans. Much of the funding comes from Europe.

Wales

The Welsh Development Agency provides generous assistance to major inward investment projects.

Scotland

Within Scotland, development of funding in the form of low interest loans and equity participation is provided through Local Enterprise Companies. Funding is normally in the region of £15,000 to £50,000.

Northern Ireland

The highest levels of local authority assistance are available in Northern Ireland. The principal features include tax-free grants of up to 50% of the cost of new factory buildings and machinery and equipment, employment grants, interest relief grants and rent grants. Other benefits include a contribution of up to 50% for training, product and research and marketing development grants for up to 40% of approved costs.

3.4 New Towns

There are 21 New Towns throughout the UK. New Towns offer a number of advantages for industrial development, including good location, a variety of factory units available for letting or purchase, space for expansion and readily available high-standard housing for employees.

The Commission for New Towns will provide, free of charge, detailed information on the availability of sites for purchase.

3.5 Research and Development Support

Known as Smart the scheme provides grants to small and medium sized enterprises for feasibility studies into innovative technology and development up to pre-production proto-type stage of new products and processes.

Financial support is also available for research programmes through Link.

3.6 *The Law and Money Laundering*

No assistance to money launderers

It is an offence to provide assistance to a money launderer to obtain, conceal, retain or invest funds.

No Tipping Off

It is an offence to inform the person that they are under suspicion of money laundering and that a report has been made.

Failure to Report

It is an offence for a person who knows or suspects that another is engaged in money laundering not to report such knowledge or suspicion as soon as practical.

You should appreciate that financial institutions and professionals, who may assist you in setting up in the UK, will be required to verify your identity and background and to monitor your institutions in the light of this legislation.

3.7 *Inward Investment*

The EU's Customs rules apply uniformly to all goods imported into its territory. However, the myriad of its trading arrangements with world producers has resulted on complex rules which change frequently and has introduced compliance issues for the unwary or ill advised importers. The risks can include seizure of incorrectly declared goods, severe penalties for non compliance under criminal law in many Member States and duty overpayments. Not withstanding this, there are many opportunities to use the facilitory arrangements (for example Customs Warehousing and information technology to streamline procedures). Intending investors considering setting up distribution or manufacturing sites in the UK who wish to remain competitive in the EU must therefore ensure that the real cost of importing is well researched prior to finalising their plans.

4 EMPLOYMENT REGULATIONS AND SOCIAL SECURITY CONTRIBUTIONS

4.1 *Work Permits*

The following do not need work permits.

- (a) EU area nationals. The member countries are Austria, Belgium, Denmark, Ireland, Finland, France, Germany, Greece, Holland, Iceland, Italy, Liechtenstein, Luxembourg, Norway, Portugal, Spain and Sweden.
- (b) People born in Gibraltar.
- (c) Commonwealth citizens who were allowed to enter or to remain in the UK on the basis that a grandparent was born here.
- (d) Husbands, wives and dependent children under 18 of people who hold work permits or who qualify under the above categories.

Representatives of overseas firms who are seeking to establish a UK branch or subsidiary, and persons coming to the UK to set up a new business or takeover or join an existing business as a partner or a director, will not normally need a work permit but may have to obtain prior entry clearance at a British diplomatic post abroad.

A simplified procedure is available for employees of multi-national companies transferring to a senior post in the UK or transferring for up to three years to develop their career.

4.2 *Engagement and dismissal*

No employee may be taken on without a contract of employment although this may take the form of a letter. The contract of employment must state as a minimum the following:

- Rate of pay and hours worked
- Paid holiday entitlement (minimum 4 weeks)
- Paid sick leave entitlement

- Minimum notice of termination of employment
- Details of any pension scheme
- Clauses relating to health and safety
- Disciplinary procedures
- Grievance procedures
- National Minimum Wage

An employee's contract of employment may be terminated for any reason within the first year, but thereafter termination without good reason and without following the statutory disciplinary procedures may result in a claim by the employer for unfair dismissal subject to a maximum of £50,000. Larger employers must consult the workforce before making anyone redundant. Employees made redundant are entitled to redundancy payment in addition to any payment in lieu of notice, according to a laid down scale.

4.3 *Trade Unions and Worker Councils*

There is no legal requirement for employers to recognise any trade union unless a majority of the work force vote in favour. Agreements between employers and trade unions over pay and conditions are not binding by law and unions may not take industrial action without first securing a majority vote in a secret ballot of their members.

There is no legal requirement for employees to be represented on the board of directors of companies.

4.4 *Social Security Contributions*

All employers are liable for social security contributions in relation to their employees. Rates of contributions for employers and employees are set out at Appendix 6.

5 TAXATION

5.1 *Companies*

5.1.1 *Scope*

Companies that are incorporated under UK law, and other companies which are managed and controlled from the UK, are liable to corporation tax on their worldwide profits.

Companies not incorporated under UK law, and not managed and controlled from the UK, are liable to corporation tax on any trading profits that they derive from a UK branch or agency. Where there is a double tax treaty between the UK and the country in which such a company is based then its terms may modify the extent to which the company is liable to corporation tax.

Foreign companies are also liable to UK tax on other sources of income derived from the UK, subject again to the terms of any relevant double tax treaty.

5.1.2 *Taxable profits*

Corporation tax is charged on a company's income and capital for each of its accounting periods. An accounting period is normally the period for which accounts are produced to comply with company law, but special rules apply where such accounts cover a period of more than 12 months.

Dividends received from other UK companies are generally exempt from corporation tax.

The principal part of a trading company's corporation tax computation is the adjustment of its profits for tax purposes. The starting point in the company's profit before tax is as shown by the statutory accounts. Disallowable expenses are then added back.

Depreciation is also added back as disallowable, and capital allowances (see 5.1.3) are deducted instead. Capital receipts and expenses are generally excluded.

The general rule for deductible expenses is that they must be 'wholly and exclusively' incurred for the purposes of the trade. There are also specific rules disallowing entertaining expenses (except those relating to their staff), improvements to premises (as opposed to repair) and general bad debt provisions (as opposed to provisions for specific debts).

Special reliefs, or tax repayments for certain loss making companies, are available in respect of revenue expenditure on research and development.

Companies are also liable to corporation tax on their capital gains. Generally these are computed as the excess of the proceeds of sale of an asset over its original cost, but for assets acquired prior to 31 March 1982, the market value of the asset at that date may be substituted if it produces a smaller gain. There is an 'indexation relief' to ensure that tax is levied only on real gains and not on any proportion that is attributed to inflation. Tax on the sale of real property which is used in a trade and of certain other business assets can be deferred if the sale proceeds are used to purchase replacement assets within specified categories.

New rules exempt gains or losses on the disposal of substantial shareholdings (10% or more) where certain conditions are satisfied.

5.1.3 Capital Allowances

Capital allowances are deductible from trading profits as a replacement for the depreciation charged in the statutory accounts. The principal classes of assets eligible for allowances are:

- Industrial buildings
- Hotels
- Agricultural buildings
- Machinery and plant
- Patent rights
- Know-how
- Mines and oil wells
- Scientific research expenditure

A different set of rules and method of calculation applies to each of these categories.

Allowances in respect of industrial buildings and machinery and plant are the most commonly claimed. There is an elaborate statutory definition of an 'industrial building'. Broadly speaking, building costs incurred on a

building used for industrial manufacturing, processing or repair will usually qualify, and allowances are also available for certain storage facilities. In general, allowances are not given on the cost of retail premises or office buildings.

The rate of allowance on industrial buildings is generally 4% per annum. Expenditure on constructing a building in a designated Enterprise Zone, however, qualifies for an allowance of 100% in the year in which it is incurred.

There is no statutory definition of 'machinery' or 'plant'. While 'machinery' presents no problems, a considerable amount of case law has developed to define 'plant'. Generally speaking, any apparatus that performs a function in the business will qualify, while any items forming part of the premises will not. Examples of qualifying plant include shop fittings, air conditioning installations, special lighting and moveable partitions. Non-qualifying items include general light fittings and wiring, prefabricated buildings and shop fronts. The Inland Revenue have published a list of items that, in their opinion, qualify.

For capital expenditure on assets used in research and development the rate of allowance is 100%.

5.1.4 Interest Payments

Interest payable is usually deductible from profits for tax purposes in the same way as any other trading expense.

Companies must generally deduct income tax at 20% from interest that they pay to lenders other than banks and pay the tax over to the Inland Revenue with the exception of payments to other UK resident companies.

However, most of the UK's double tax treaties with other countries provide for a reduced rate of withholding tax, or in some case no withholding tax at all. Some examples are given in Appendix 1.

Care is needed with interest payable to an overseas parent company. In some circumstances the interest will not qualify for tax relief and will be treated as a dividend payment.

5.1.5 Royalty Payments

Deductions for royalties paid or to be paid are available; historically some types of royalties, for example patent royalties, were deductible

only on the basis of the amount actually paid, others on a normal accounting basis. However, following the introduction of new rules to deal with the taxation of intangibles, royalties are now deductible on an accounts basis.

Companies must in some cases deduct income tax at 20% from royalties paid, and pay the tax over to the Inland Revenue. Where the licensor is resident abroad, the appropriate double tax treaty may provide for a reduced or a nil rate of withholding tax. Some examples are given in Appendix 2.

5.1.6 Dividend Payments

No tax or withholding tax is payable when a UK company pays a dividend to an individual or another company including non-residents.

Depending on the terms of particular double tax treaties the recipient may receive a partial tax credit and, in cases, a right to a small tax repayment.

5.1.7 Calculation of Liability

Corporation tax rates (see Appendix 4) are specified for 'financial years', commencing on 1 April. The financial year 2002, for example, will run from 1 April 2002 to 31 March 2003. If an accounting period ends on some other date, chargeable profits are time-apportioned to financial years.

There are different rates of corporation tax depending on the level of profit. A reduced rate applies if profits for a year do not exceed a 'lower limit'. The full rate applies if profits exceed a 'higher limit'. If profits fall between the lower and higher limits the rate of tax is calculated by a sliding scale formula which gives an overall rate somewhere between the reduced rate and the full rate. The formula produces an effective rate of tax on profits in excess of the lower limit which is higher than the full rate.

The higher and lower limits are reduced if the company has 'associates' i.e. if there are other companies anywhere in the world under the same control. If, for example, a company has a parent company and two fellow subsidiaries, the limit must be divided by four, being the total number of companies in the group.

5.1.8 Due Dates for Payment

Except for large companies, corporation tax is payable nine months after the end of the accounting period. For companies which make profits in excess of £1.5m per annum (divided by the number of associates), corporation tax is payable by quarterly instalments, commencing in the middle of the seventh month of the company's accounting year. The tax payable is based on the estimated taxable profit for the year.

5.1.9 Relief for Losses

Trading losses incurred in an accounting period may be offset against other sources of income in that period or in the preceding accounting period, or carried forward indefinitely against future trading income. They may also be surrendered to the other UK group companies for relief in the same accounting period.

The losses of investment companies can generally be set off against general profits in the year that the loss was incurred and the excess carried forward.

Other types of loss may in general be offset only against future income from the same activity.

5.1.10 Administration

A system of self-assessment operates. Interest is payable or receivable on any under/overpayments of tax subsequently agreed. A corporation tax return is required from companies in respect of each accounting period. A penalty is levied if the return is not delivered, together with the company's accounts, within twelve months of the end of the accounting period.

5.1.11 Tax Planning

An overseas organisation intending to set up operations in the UK should give early consideration to the manner in which its investment will be structured, in order to avoid excessive taxes both in the home country and in the UK.

5.2 Individuals

5.2.1 Overview

Individuals who are resident and domiciled (see 5.3.1 below) in the UK are subject to UK tax on the aggregate of their worldwide income and capital gains. Individuals are taxed at source at basic and higher rates on their employment income and benefits after allowances. The highest marginal rate of tax is 40%. Individuals are taxed at various rates. The thresholds, tax rates and allowances are set out in Appendix 5. On death or gifts made within 1 year of death, inheritance tax is payable on the value of the deceased's assets at 40% on the value in excess of £250,000. The UK does not have a wealth tax.

5.2.2 Sole Traders

The self-employed are liable to income tax on their profits as adjusted for tax purposes in broadly the same way as profits are adjusted for corporation tax. Interest on loans to provide capital for the business is an allowable deduction.

The UK fiscal year runs from 6 April to 5 April but an individual may draw up his accounts for a year ended on any date. The accounts of the business for the year ended on or prior to 5 April form the basis of assessment for the fiscal year. There are special rules for commencement and cessation and changes in accounting date, giving rise to some scope for tax planning.

5.2.3 Partnerships

Partnerships are taxed in the same way as the self-employed, so that the individual partners are taxed on their share of the profits as adjusted for tax purposes. A partner is not liable for the unpaid tax of another partner.

A partnership controlled and managed in the UK is liable to income tax on both its UK and overseas profits. This includes any profits due to partners not resident in the UK. In practice however, the Inland Revenue will not assess a non-resident's share of overseas profits.

A partnership managed and controlled abroad which carries on part of its business in the UK through a branch or agency will be subject to income tax on the profits of the branch. The branch will be taxed as a non-resident carrying on a trade in the UK even though some of the partners may be resident in the UK.

Profits attributable to a corporate partner are assessed separately on the company, broadly under corporation tax rules.

5.2.4 Taxation of employees

Employees resident in the UK are subject to income tax and social security contributions (see 5.4) on all earnings and most benefits provided by an employer. Benefits include cars, accommodation, cheap loans and health care insurance.

5.2.5 PAYE

Income tax and social security contributions are deducted at source by the employer under the PAYE (pay as you earn) system. It is the employer's responsibility to ensure that the PAYE system is operated correctly and, particularly, to distinguish between those who are employed and those who claim to be self-employed. Employers are subject to regular inspections by the Inland Revenue, and failure to operate properly the rules governing PAYE can lead to penalties and interest on unpaid tax.

5.2.6 Taxation of savings income

Savings income from sources such as shares and cash deposits are added to the individual's other income and are normally taxed at the rates set out in Appendix 5. There are some exemptions to this general rule:

Interest on bank and building society accounts, etc is taxed at 20% if it would otherwise fall into the basic rate band. Generally tax at 20% is deducted at source.

Gross dividends are taxed at 10% if they would otherwise fall into the lower or basic rate bands. Generally tax at 10% is treated as having been deducted at source from UK dividends. Tax at 32.5% is due on gross dividends where the dividend falls into the higher rate band, with relief available for the 10% tax treated as deducted at source (the tax credit). This gives a tax liability equivalent to 25% of the net dividend for a higher rate tax payer. The deemed 10% tax credit generally cannot be repaid if the actual tax liability is lower.

5.2.7 Income from land and property

The net income from these sources is added to the individual's other income and taxed according to the rates and thresholds set out at Appendix 5. Interest on loans relating to land or property that is let may be deducted for tax purposes. Where the income is paid to an overseas resident it is subject to a withholding tax of 22%. The withholding tax can be avoided if the overseas resident registers with the UK tax authorities.

5.2.8 Capital Gains

With some minor exceptions, tax is payable on all assets on which a gain is made. The gain is normally calculated by taking the cost plus indexation (using the retail price index) up to 5 April 1998 and comparing that with the sales proceeds. If the asset was held before 31 March 1982, the 31 March 1982 market value may be substituted for the cost. The resultant gain is then reduced by 'taper relief' which is calculated by reference to the number of complete years the asset has been owned after 6 April 1998. The relief is different for business and non-business assets. A maximum reduction for non-business assets is available at 40% if the asset is owned for 10 years. Non-business assets acquired prior to 17 March 1998 are treated for this purpose as having already been owned for one year.

For business assets a maximum reduction of 75% is available if the asset is owned for 2 years. Assets qualifying as business assets from 6 April 2000 include:

- All shareholdings in unquoted trading companies (including those traded on AIM)
- All shareholdings held by officers and employees in quoted trading companies
- All employee shareholdings of less than 10% (irrespective of quoted or trading status)
- Shareholdings in quoted trading companies where the holder is not an officer or employee but can exercise at least 5% of the voting rights.

Special apportionment rules apply when an asset changes status between a non-business and business asset.

There is an annual allowance to exempt a small amount of the gain in each year. Gains are usually taxed using income tax rates, treating the gain as the top slice of income (see Appendix 5).

5.2.9 Inheritance Tax

Inheritance tax is payable on death by the deceased's personal representatives on the net value of the deceased's assets and liabilities at the date of death. Gifts within seven years of death are included in whole or part in the deceased's estate for inheritance tax purposes. Transfers between spouses are exempt although a restriction applies where the donor spouse is UK domiciled but the donee spouse is not. Some business assets qualify for exemption in whole or in part.

The rate of tax and level of exemption for small estates is set out in Appendix 5.

5.2.10 Administration

The UK operates a system of self-assessment for tax on income and capital gains. A tax return for the year ended 5 April must be filed annually normally by 31 January in the following year, together with a payment of the balance of any tax due for the relevant year. Payments on account of the liability for the relevant year are due as to 50% on 31 January in the relevant year and 50% six months later. Payments on account are calculated by reference to the liability for the previous year.

5.3 Expatriates

5.3.1 Scope of UK Taxation

Most people who come to the UK for employment will be in a position to claim that they are 'domiciled'* outside the UK. Domicile is a concept in Anglo-Saxon law meaning, broadly, one's natural home country, the country to which, if absent, one intends eventually to return. Living as a foreign domicile in the UK can bring significant tax advantages. In particular, investment income and capital gains arising outside the UK are not taxed in the UK if the funds concerned are not 'remitted' to the UK, meaning that they are not brought into or otherwise enjoyed in the UK. Foreign domicile status should not however be taken for granted. A claim must be made to the Inland Revenue and they have the right to challenge it. In practice, they will usually accept that a person who comes to the UK solely for employment purposes has retained a foreign domicile, provided an actual intention to return to the country of origin is retained.

Unless their visit to the UK is very short, people who come to the UK for employment purposes will generally be treated as resident in the UK in a tax context. Residence is an entirely separate concept from domicile.

*At the time of writing a review of these rules is proposed.

If they intend to stay for less than three years they can generally claim that they are resident but not ordinarily resident in the UK. The chief significance of this is that if their work is partly in the UK and partly overseas, then they will not be taxed in the UK on the part of their salary which relates to the overseas work, if that part is paid to them abroad and is not brought into the UK.

Longer term employment in the UK will result in a resident and ordinarily resident status from arrival. On this basis the whole of the salary is taxed even though part of it may be earned outside the UK. For those who can claim a foreign domicile there may be scope for having two separate contracts of employment, for respectively their UK and their foreign duties. A person who is not domiciled in the UK and who is employed by a company which is not resident in the UK or the Republic of Ireland for duties which are performed entirely outside the UK is not taxed on the salary therefrom provided it is not brought into the UK.

The current rates of income tax and personal allowances are listed in Appendix 5.

5.3.2 Accommodation provided by the employer

Accommodation provided by the employer is taxable unless it is temporary accommodation (i.e. less than 24 months) connected with the employee's relocation. The tax charge is on the utilities paid by the employer, plus the 'annual value' if it is owned or the rent paid if it is leased. There is an additional tax charge on employer owned accommodation costing over £75,000, which is broadly equivalent to a tax on the notional interest on the excess.

5.3.3 Social Security Contributions

The UK has reciprocal social security agreements with many countries under which employees may continue to pay the home country contributions for a specified period of time. The agreements can also provide for protection of benefits.

Under European Union regulations a national of a member state who is posted by their employer to another member state is liable to pay contributions to the state in the period that they are working provided the assignment is for a period of at least 12 months. Employees who have assignments of less than 12 months continue to pay home country contributions.

5.4 Indirect Taxes

5.4.1 Value Added Tax

In common with other states of the EU the UK imposes value added tax (VAT) on the consumption of goods and services.

In general terms businesses do not themselves suffer VAT, as it is a tax payable by the ultimate consumer, the man in the street, but businesses are responsible for the administration and collection of tax.

Businesses with an annual sales turnover in excess of the registration limit, currently £55,000, are required to register with HM Customs & Excise. In general terms they must then add VAT to the price they charge for their goods and services, and periodically pay over to HM Customs and Excise the VAT they have charged. In doing so they may deduct the VAT with which they have themselves been charged on their purchases of goods and services.

Voluntary registration is permitted for businesses with an annual sales turnover below the registration limit and which wish to be in a position to recover the VAT that they incur on their purchases.

For most categories of goods and services, VAT must be added at the standard rate, currently 17.5%.

A reduced rate of 5% applies to fuel and power, other than fuel for transport, some property construction services and childrens' car seats.

Some categories are 'zero-rated'. This means that a nil rate of tax is to be charged, but the business supplying the goods or services is nevertheless entitled to a refund of the VAT it has incurred on its purchases. Businesses making only zero-rated supplies will therefore be in a position to obtain periodic refunds from HM Customs & Excise.

Some services are 'exempt'. Again there is no VAT to be charged, but in contrast to the position on zero-rated supplies the supplier is not entitled to a refund of the VAT paid on purchases. Businesses that make exempt supplies in addition to either standard-rated or zero rated supplies may be able to recover part of the VAT they incur on their purchases.

The principal categories of main goods and services classed as zero-rated or exempt are listed in Appendix 4.

Exports are generally zero-rated except where they are made to a person in the EU in a private rather than a business capacity.

VAT must be paid on the import of goods, and of some services, into the UK.

Whilst VAT is perceived as a simple transaction tax, there are numerous complications, particularly in the property and finance sectors. For instance, property transactions can be standard rate, reduced rate, zero rate or exempt (but with the options to charge VAT). In addition there are complex anti-avoidance issues that can effect non-avoidance transactions.

The VAT compliance regulations are strict and penalties are imposed for the late submission of periodic returns and for errors in returns. Businesses need to avoid potential problems by implementing an efficient accounting system at an early stage.

5.4.2 Customs Duty

In addition to VAT there are sales taxes on particular items notably cars, fuel for motor vehicles, tobacco, and alcoholic drinks.

The EU has a harmonised system of Customs Duties. Goods can move freely within the EU if they originate in the EU or once they are duty paid in any jurisdiction.

Duty is a one-off absolute cost. To pay the current duty accurate classification and valuations accordingly to customs rules is vital. This valuation may differ markedly from the direct tax valuation or the VAT valuation. In correct valuations a classification will either mean too much duty is paid or too little. The former will add an irrecoverable cost, the latter will leave a business open to penalties, criminal proceedings (there is no civil penalty regime) and disruptions to the business (for instance wrongly declared goods can be seized bringing production to a halt).

There are many reliefs that can reduce the burden of customs duties. These can significantly reduce the duty cost. These reliefs are not available retrospectively and authorisation must be obtained in advance from Customs & Excise.

5.4.3 Other Indirect Taxes

These include;

Excise Duty – high levels of duty are applied to motor fuels, alcohol & tobacco products. Excise duty also applies to gaming.

Insurance Premiums Tax (IPT) – Levied at 5% on most insurance visits in the UK (even if insured by an offshore company). IPT is charged at 17.5% on domestic appliances & motor car warranties & travel insurance. Exemption is available for certain long term contracts (life assurance) re-insurance and other specified risks.

Landfill Tax (LFT) – This is a levy on waste dumped at landfill sites. It is charged at £13 a tonne and this increase on 1 April 2003 to £14 and then on 1 April 2004 to £15 a tonne. Inert waste (stone, slag, ash, water, soil, etc) is subject to a LFT at £2 a tonne. Exemption is available for waste from a continental side if a certificate is obtained.

Climate Change Levy – Is a tax on fuel costs. The tax varies accordingly to the type of fuel. No levy's charged to domestic properties or qualifying charitable uses.

Aggregate Levy – This is a charge of £1.60 a tonne on sand, gravel and rock commercially exploited in the UK. A number of exemptions apply.

Air Passenger Duty – This is a levy on the carriage of a passenger from most UK airports. The duty rates are £10 for European Economic Area destinations and £40 for other destinations with reduced rates of £5 and £20 respectively for the lowest class of travel. The European Economic Area is the EC plus some assorted territories such as Gibraltar, the Faroe Islands, Madeira, etc.

5.5 Other Taxes

5.5.1 Stamp Duty

Stamp duty is payable by UK or foreign purchasers of land and shares in UK incorporated companies.

The rate of duty on shares is 0.5% of the consideration. On other assets a scale of 1% to 4% applies on transfers between £60,000 and £500,000 at which point the highest rate applies.

5.5.2 Businesses

There are no local taxes levied on company profits. However, local authorities levy a tax, known as the uniform business rate, on the occupiers of commercial property. The amount paid depends upon the annual rental value of the property which takes into account its location and size. The rate of the tax is set by central government.

5.5.3 Individuals

Individuals pay local taxes by reference to the market value of domestic houses which they occupy as owners or lessees. The tax is typically between £500 and £2,000 per annum.

5.5.3 Tax Planning

There are significant advantages built into the UK tax system for those who can claim successfully that they are 'domiciled' outside the UK covering not only income tax and tax on capital gains but also inheritance tax on death or lifetime gifts. Detailed advice is necessary for the maximum benefit to be obtained. Companies which plan to send employees to the UK are recommended to arrange for them to consult Baker Tilly before their arrival or as soon as they arrive, so that prompt action can be taken where appropriate to minimise their UK tax liabilities.

1 APPENDIX 1

Withholding taxes on interest payments

Interest payments to overseas lenders are generally subject to the deduction of withholding tax at 20% but the following table shows by way of example the reduced rates which are specified in some of the UK's double tax treaties with other countries. Prior authorisation must be obtained from the Inland Revenue before applying the reduced rate provided for by treaty.

	%		%
Australia	10	Japan	10
Austria	nil	Luxembourg	nil
Belgium	15	Netherlands	nil
Canada	10	New Zealand	10
China	10	Norway	nil
Cyprus	10	Pakistan	15
Denmark	nil	Portugal	10
France	nil	South Africa	10
Greece	nil	Spain	12
India	15	Sweden	nil
Ireland	nil	Switzerland	nil
Italy	10	United States	nil

Withholding taxes on royalty payments

Royalty payments for the use of patents granted under the laws of the UK are generally subject to the deduction of withholding tax at 20% but the following table shows by way of example, the reduced rates which are specified in some of the UK's double tax treaties with other countries.

	%		%
Australia	10	Luxembourg	5
Austria	nil	Netherlands	nil
Belgium	nil	New Zealand	10
Canada	10	Norway	nil
China	10	Pakistan	12.5
Cyprus	nil	Portugal	5
Denmark	nil	South Africa	nil
France	nil	Spain	10
Greece	nil	Sweden	nil
Ireland	nil	Switzerland	nil
Italy	8	United States	nil
Japan	10		

Rates of corporation tax

Year to 31 March 2003

Profits £	Tax %
0 - 10,000	0
10,001 - 50,000	23.75*
50,001 - 300,000	19
300,001 - 1,500,000	32.75*
Over 1,500,000	30

*effective rate

VAT: Zero-rating and exemptions

The principal categories of goods and services classed as zero-rated or exempt are as follows:

Zero-rated	Exempt
Food	Land
Water	Insurance
Books	Postal services
Housebuilding (new build)	Betting
Protected buildings	Finance
Some international services	Education
Transport	Health and welfare
Medicines	Sports and cultural services
Charities	Exports of goods
Clothing and footwear (for children)	

5 APPENDIX 5

Rates of income tax

Year to 5 April 2003		
	Taxable income £	Tax %
Lower rate	1 - 1,920	10
Basic rate	1,921 – 29,990	22
High rate	Over 29,990	40

Some savings and investment income is taxed at lower rates

Income Tax allowances

Year to 5 April 2003			£
Personal			4,615
Age allowances:			
Personal	65-74		6,100
Personal	75 and over		6,370
Married	65 before 6 April 2000		5,465*
Married	75 and over		5,535*
	income limit for full relief		17,900
Blind person			1,480

*Relief restricted to 10%

Capital Gains

Year to 5 April 2003	£
Annual exemption:	
Individuals	7,700
Personal Representatives	7,700
Trusts	3,850

Inheritance tax

Year to 5 April 2003	
7 year cumulative transfers	
£1 - £250,000	Nil
Over £250,000	40%
Some lifetime gifts are taxed at 20%	
Main exemptions	
Annual gifts per donor	£ 3,000
Small gifts per donee	250
Certain exemptions apply to gifts on marriage	
Parent	5,000
Grandparent	2,500
Other	1,000

6 APPENDIX 6

Rates of social security contributions

Year to 5 April 2003

Class I (employed)	Contracted in rates		Contracted out rates		
	Employer	Employee	Employers		Employee
	Payable on		Payable on		
	all earnings band		all earnings band		
Earnings per week	%		%	%	%
£0 - £89.00	nil		nil	nil	nil
£89.01 - £585.00	11.8		10	8.3+	8.4
Over £585.00	11.8		-	11.9	-

+Rate increased by 2.5% for money purchase schemes

Class 1a (employers only)	11.8% of most taxable benefits
Class 2 (self-employed)	£2.00 per week
Annual small earnings exemption	£4,025
Class 3 (voluntary)	£6.85 per week
Class 4 (self-employed)	7.0% on profits between £4,615 and £30,420

Maximum £1,806.35 p.a.



NOTES

Doing business in the UK



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MEMBER FIRM CONTACT DETAILS

Baker Tilly is a leading independent firm of chartered accountants and business advisers that specialises in providing an integrated range of services to the owner managed business. We provide our growing and established business clients with audit, accountancy, personal and corporate taxation, VAT, consultancy, corporate finance, financial services and business recovery. The firm has national coverage through its network of over 30 offices and is represented internationally through its independent membership of Baker Tilly International.

Contact: Geoff Barnes
Baker Tilly
2 Bloomsbury Street
London WC1B 3ST

Tel: +44 20 7413 5100
Fax: +44 20 7413 5101
Email: geoff.barnes@bakertilly.co.uk
www.bakertilly.co.uk

Baker Tilly International World Headquarters
2 Bloomsbury Street
London WC1B 3ST

Tel: +44 20 7314 6875
Fax: +44 20 7314 6876
Email: info@bakertillyinternational.com
www.bakertillyinternational.com