



International tax

United Kingdom Highlights 2012

Investment basics:

Currency – Pound Sterling (GBP)

Foreign exchange control – No

Accounting principles/financial statements – U.K. GAAP/IAS. Financial statements must be filed annually.

Principal business entities – These are the public and private limited liability company, Real Estate Investment Trust (REIT), limited liability partnership, limited partnership, partnership and branch of a foreign corporation.

Corporate taxation:

Residence – A company is U.K. resident if it is incorporated in the U.K. or its place of central management and control is in the U.K.

Basis – A U.K. resident company is subject to corporation tax on worldwide profits and gains (see "Taxable income," below), with credit given for overseas taxes. With effect from Finance Act 2011, foreign profits (and losses) (including those from certain capital assets) arising from all (but not some) of the permanent establishments (PE) of a U.K. resident company may be excluded, by irrevocable election. The effect of the election may be deferred where there have been losses in any of the PEs, and is subject to a motive test where the foreign tax paid is less than 75% of the U.K. corporation tax that would have been paid on the income profits of the PE. A non-U.K. resident company is only subject to tax in respect of U.K.-source profits, which include the income of a U.K. PE, income from U.K. real estate, certain U.K.-source interest income and gains on assets used for purposes of the PE's trade.

Taxable income – For a U.K. resident company, corporation tax is imposed on trading income, several baskets of non-trading income and capital gains. Normal business expenses may be deducted in computing taxable income provided that these are not capital expenditure. No deduction is available for the depreciation or amortization of land, buildings or other

tangible fixed assets. Instead, tax relief is available for qualifying capital expenditure on plant and machinery (including certain integral features in buildings) at an annual writing down allowance of 10%/20% (8%/18% from 1 April 2012) on a reducing balance basis depending on the type of asset. Full relief is available for the first GBP 100,000 (GBP 25,000 as from 1 April 2012) of expenditure (excluding automobiles) per annum per business/group of companies. There is a limit on deductions that can be taken for financing costs where U.K. companies are members of a large group (IAS-defined). These debt cap rules apply broadly where the aggregate tax deductions for net financing costs of U.K. group companies exceed the worldwide group's gross accounting financing costs.

Taxation of dividends – A dividend exemption applies to most dividends (and distributions) unless received by a bank, insurance company or other financial trader. Dividends received by a non-small U.K. company on most ordinary shares and many dividends on non-ordinary shares from another company (U.K. or foreign) will be exempt from U.K. corporation tax, with no minimum ownership period or minimum ownership level. The exemption can also apply to small companies receiving dividends (and distributions) from U.K. or foreign companies, resident in a jurisdiction that has concluded a tax treaty with the U.K. that includes a non-discrimination provision. (A small company is a "micro or small enterprise" as defined by the EU)

Capital gains – Capital gains form part of a company's taxable profits. Gains (or losses) on the disposal of substantial shareholdings in both U.K. and foreign companies can be exempt. The main conditions broadly require the selling company to have continuously owned at least 10% of the shares of the company being sold for at least 12 of the 24 months before disposal and the selling company/company being sold must be trading or members of a trading group (without, to a substantial extent, any non-

trading activities) throughout a period of at least 12 months prior to disposal (in some cases this may have to be 24 months before the disposal) and immediately after the disposal. Where an election has been made to exclude the profits of PEs (see "Basis" above) the exclusion also may apply to gains and losses of certain capital assets of the PE unless the company is a close company. A non-U.K. resident company is not subject to tax on its capital gains unless the asset is held through a U.K. PE.

Losses – Trading losses generally can offset total profits of the year (including capital gains) with carryback of the excess to the preceding year permitted. Trading losses can be carried forward indefinitely (unless there is a change of ownership of the company and a major change in the nature and conduct of the trade within 3 years), but can only be offset against trading income. Capital losses can only be set against capital gains and can only be carried forward.

Rate – The main rate of corporation tax prior to 1 April 2012 is 26%. From this date, the rate is 24% (rather than the previously announced decrease to 25%).

The main rate does not apply to ring fence profits from oil rights and extraction. The small profits rate applied to companies with taxable profits of less than GBP 300,000 per annum is 20%. Companies with taxable profits between GBP 300,000 and GBP 1.5 million are effectively taxed on a sliding scale at an average rate between the main rate and the small profits rate. The GBP 300,000 and GBP 1.5 million limits are reduced if the company has any associated companies or the accounting period is less than 12 months.

Surtax – No

Alternative minimum tax – No

Foreign tax credit – A U.K. resident company is subject to corporation tax on its worldwide profits (including capital gains) with credit given for most overseas taxes. (A U.K. company may irrevocably elect to exempt the profits (and losses) of foreign PEs from U.K. corporation tax provided that

certain conditions are satisfied. Where such profits are excluded from U.K. taxation, no credit is available (see "Basis" above).

Participation exemption – Most dividends, including foreign dividends, are exempt (see above under "Taxation of dividends"). In addition, capital gains on the disposal of substantial (i.e. 10% or more) shareholdings in certain companies are not subject to corporation tax (see above under "Capital gains").

Holding company regime – See "Participation exemption", above.

Incentives – An enhanced tax deduction is available for certain R&D expenditure of 200% for small or medium-sized companies (increasing to 225% on 1 April 2012) and 130% for large companies.

Withholding tax:

Dividends – There is typically no withholding tax on dividends paid by U.K. companies under domestic law, although a 20% withholding tax generally applies to distributions paid by a REIT from its tax exempt rental profits (subject to relief under a tax treaty).

Interest – Interest paid to non-U.K. residents is subject to a 20% withholding tax, unless the rate is reduced under a tax treaty or exempt under the EU interest and royalties directive. This is not an automatic reduction and clearance must be granted by the U.K. tax authorities.

Royalties – Royalties paid to nonresidents are subject to a 20% withholding tax, unless the rate is reduced under a tax treaty or exempt under the EU interest and royalties directive.

Technical service fees – No

Branch remittance tax – No

Other – No

Other taxes on corporations:

Capital duty – No

Payroll tax – No

Real property tax – The national non-domestic rate is payable by occupiers of business premises. Local authorities collect the tax by charging a uniform business rate, which is deductible in computing income subject to corporation tax.

Social security – Employers are required to make pay-related social security contributions together with employee payroll deductions (see "Other taxes on individuals" below).

Stamp duty – A 0.5% rate applies on the transfer of U.K. shares and Stamp Duty Land Tax (SDLT) is charged on transfers of U.K. real property at rates between 1% and 4%, depending on the value of the property (e.g. the 4% rate is charged on the entire consideration if the consideration exceeds GBP 500,000). From April 2011, a 5% rate applies to residential property valued at more than GBP 1 million. In certain cases, transfers within a tax group may be free of stamp duty/SDLT.

Transfer tax – See "Stamp duty" above.

Other – Shipping companies may elect to pay tonnage tax in lieu of the normal corporation tax.

Anti-avoidance rules:

Transfer pricing – Comprehensive transfer pricing provisions apply to transactions with both domestic and foreign companies, following OECD principles. This includes a requirement to prepare documentation to demonstrate compliance with the arm's length standard. Advance pricing agreements are possible in certain situations.

Thin capitalization – The arm's length principle applies. There are no safe harbor provisions. Advance thin capitalization agreements are available. (See "Taxable income," above, for debt cap rules).

Controlled foreign companies – CFC provisions are applicable where, broadly, a U.K. company has an interest (direct or indirect) of at least 25% in a non-U.K. resident company that is controlled by U.K. residents and is subject to a lower level of taxation (generally less than 75% of the tax it would have paid if U.K. resident). There are several exemptions but where the CFC rules do apply very broadly all the profits of the CFC are computed as though it were U.K. resident and its U.K. shareholder is subject to tax accordingly.

Other – There are many specific anti-avoidance rules.

Disclosure requirements – Certain tax arrangements that result in a U.K. tax advantage and fall within prescribed hallmarks must be disclosed to the U.K. tax authorities by, for example, a promoter, and the user must note the use of such arrangements on the tax return. Separately, certain transactions valued at more than GBP 100 million, involving, for example, the issue of shares or debentures by, or the transfer or permitting the transfer of shares or debentures of, a foreign subsidiary of a U.K.

company, also have to be reported to the U.K. tax authorities within 6 months of the transaction. There is a list of excluded transactions that do not need to be reported.

Administration and compliance:

Tax year – The shorter of 12 months or the period for which the accounts are prepared.

Consolidated returns – All companies file separate tax returns. However, losses may be "group relieved" between U.K. group companies (broadly, where one is a 75% subsidiary of another or both are 75% subsidiaries of the same corporate parent in terms of share ownership, rights to income and rights on a winding up, taking account of direct and indirect holdings). There also are other group rules that apply to capital gains that allow, for example, assets to be transferred intragroup at no gain/no loss for tax purposes or gains/losses to be transferred between the members of the group.

Filing requirements – The U.K. operates a self-assessment regime. Large companies pay tax in quarterly installments starting in month 7 of their financial year. The tax return is due to be filed within 12 months of the period end. Mandatory online filing of all company tax returns applies from 1 April 2011.

Penalties – Companies are liable to a fixed penalty of GBP 100 for failure to file a tax return by the due date, plus an additional GBP 100 if the return is not submitted within 3 months of the due date. Further penalties may apply to returns filed at least 6 months late. Tax geared penalties can be sought for matters such as tax returns that are carelessly or deliberately incorrect, although such penalties can be reduced depending on the taxpayer's behavior (e.g. voluntary disclosure, cooperating with tax enquiries, etc.). Interest is paid on late paid tax.

Rulings – U.K. tax legislation includes a number of anti-avoidance provisions for which advance statutory clearance may be sought. Also, under a non-statutory clearance procedure, the U.K. tax authorities' view of the tax consequences of specific transactions can be sought, on a named basis, with full disclosure, where there is both commercial significance and material uncertainty.

Personal taxation:

Basis – Individuals who are resident, ordinarily resident and domiciled in the U.K. are subject to tax on their worldwide income

and gains. Different treatment may apply where a person, although resident, is not ordinarily resident or not domiciled in the U.K.

Residence – Generally, an individual is resident if present in the U.K. for 183 days or more in a tax year, or if the resident makes visits to the U.K. that average 91 days or more for 4 consecutive tax years (which also can constitute “ordinary residence”). An individual is ordinarily resident if, for example, resident for 3 tax years or if he/she has moved to the U.K. with the intention of staying for the next 3 years. An individual's domicile status may be determined by his/her parents' domicile or can be acquired.

Filing status – Individuals file tax returns separately, irrespective of marital status.

Taxable income – Individuals who are resident, ordinarily resident and domiciled in the U.K. are subject to U.K. tax on their worldwide income. Residents who are not ordinarily resident or not domiciled in the U.K. may make a claim for the remittance basis of taxation to apply to overseas income. For those taxpayers who have been U.K. resident for 7 out of the past 9 years, a claim will lead to an additional tax liability of GBP 30,000 per annum. The remittance basis may also apply, but without a claim, if (broadly) the unremitted overseas income (and overseas capital gains) is less than GBP 2,000.

Capital gains – Individuals who are domiciled and either resident or ordinarily resident in the U.K. are subject to capital gains tax on all chargeable assets, regardless of where they are situated. Similar to the rules for overseas income, an individual who is not domiciled may make a claim for the remittance basis of taxation to apply to any capital gains on non-U.K. assets (see “Taxable income”, above). An annual exemption is available to reduce capital gains (GBP 10,600 for 2011/12 and 2012/13) except in tax years where a claim for the remittance basis is made. Those who are neither resident nor ordinarily resident when a gain is realized are not chargeable to U.K. capital gains tax, unless they are absent from the U.K. for less than 5 years and they acquired the asset before they left.

Deductions and allowances – Individuals are given a personal allowance deduction from total income before it is subject to tax (GBP 7,475 for 2011/12 and GBP 8,105 for 2012/13). A higher allowance is available to individuals aged 65 and over. The basic personal allowance for income tax is

gradually reduced to nil for individuals with “adjusted net income” above GBP 100,000.

Rates – Income tax is charged at progressive rates. Income in excess of GBP 150,000 is charged at 50% (the “additional rate,” charged on all income except dividends) or 42.5% (the “dividend additional rate” charged on dividends). For 2011/12, income between GBP 35,001 and GBP 150,000 is charged at 40% (for 2012/13, the limits are GBP 34,371 and GBP 150,000) (the “higher rate”) or 32.5% (the “dividend upper rate”). Income below GBP 35,001 (for 2012/13, GBP 34,371) is charged at rates between 10% - 20% depending on the type and amount of income. Dividends from U.K. companies and many non-U.K. companies attract a non-payable tax credit. (Credit is not available where the individual's holding in a non-U.K. company is 10% or more and the company is in a territory with which the U.K. does not have an appropriate double tax treaty.)

The rate of capital gains tax is determined by the total of capital gains and income. Capital gains tax is payable at a rate of 28% where an individual is liable to pay income tax at the higher rate or the dividend upper rate. For 2011/12, if taxable income is less than GBP 35,001 (for 2012/13, GBP 34,371), the rate of capital gains tax is 18%, except insofar as the gains, when added to income, would be in excess of the GBP 35,000 (GBP 34,370) limit. In that case the excess is taxed at 28%.

Entrepreneurs' relief reduces the rate of capital gains tax to 10% for certain business assets, subject to a lifetime limit of GBP 10 million of gains per individual with effect from 6 April 2011. No tax is payable on gains up to the annual exempt amount (GBP 10,600 for 2011/12 and 2012/13).

Other taxes on individuals:

Capital duty – No

Stamp duty – The charge is imposed at 0.5% on the transfer of U.K. shares and Stamp Duty Land Tax is charged on transfers of U.K. real property, at rates of 1%-4% depending on the value of the property. For example, the 4% rate is charged (on the entire consideration) if the consideration exceeds GBP 500,000. From April 2011, a 5% rate applies to residential property valued at more than GBP 1 million.

Capital acquisitions tax – No

Real property tax – Council tax applies to the occupation of domestic property.

Inheritance/estate tax – Inheritance tax is charged on property passing on death, certain gifts made within 7 years of death and some lifetime transfers (e.g. to a discretionary trust). Where due, inheritance tax is payable on assets in excess of GBP 325,000 (2011/12 and 2012/13) at a rate of 40% (20% for certain lifetime transfers).

Net wealth/net worth tax – No

Social security – National Insurance Contributions (NIC) are payable by employers, employees and self-employed individuals. For example, for 2011/12, weekly paid employees pay NIC at a rate of 12% on weekly income between GBP 139 and GBP 817 (for 2012/13, the limits are GBP 146 and GBP 817) and 2% on income exceeding this amount. For employers, NIC is payable at a rate of 13.8% on all income in excess of GBP 136 per week (for 2012/13, GBP 144 per week). For 2011/12, self-employed individuals pay NIC at a rate of 9% on annual income between GBP 7,225 and GBP 42,475 (for 2012/13 the limits are GBP 7,605 and GBP 42,475) and 2% on the excess, together with a fixed charge of GBP 2.50 per week (GBP 2.65 for 2012/13).

Administration and compliance:

Tax year – The tax year is 6 April to 5 April of the following year.

Filing and payment – Tax on employment income is withheld by the employer under the Pay As You Earn (PAYE) system and remitted to the tax authorities. Income not subject to PAYE and capital gains tax are self-assessed. If an individual is required to file a tax return, it must be filed by 31 October (or 31 January if filing online) after the tax year. Payment of tax is due by 31 January after the tax year. Payments on account of tax may be required (on 31 January in that tax year and 31 July in the following tax year).

Penalties – Individuals are liable to a penalty of GBP 100 for failure to file a tax return by the due date. The penalties escalate if the return is filed more than three months after the due date. For example, for returns filed more than three months after the filing date, the penalty is GBP 10 per day for a maximum of 3 months, and for returns filed more than 6 months and 12 months after the filing date, further penalties of the greater of 5% of the tax liability or GBP 300 may be due. Tax geared penalties can also be sought for matters such as late payment of tax and tax

returns that are carelessly or deliberately incorrect. Interest is paid on tax paid late.

Value added tax:

Taxable transactions – VAT applies to most sales of goods, the provision of services and imports.

Rates – The standard VAT rate is 20%, with a reduced rate of 5% for certain items. There also are some specific zero-rated reliefs and exemptions.

Registration – Registration is compulsory for businesses whose taxable supplies exceed GBP 73,000 (2011/12) in any given year or where a business expects that its taxable supplies will exceed this threshold within the next 30 days. Voluntary registration is

possible for businesses making taxable supplies below this threshold. Deregistration is possible if taxable supplies fall below GBP 71,000 (2011/12).

Filing and payment – VAT returns are generally due on a quarterly basis (taxable persons are allocated one of 3 VAT return periods). A taxable person may also be allowed to complete returns on a monthly basis (which is advantageous where the company is in a regular repayment position).

If the VAT return is not filed by the due date or the VAT due is not paid, a taxable person is liable to a surcharge.

Source of tax law: Income and Corporation Taxes Act 1988, Taxation of Chargeable Gains Act 1992, VAT Act 1994,

Income Tax (Earnings and Pensions) Act 2003, Income Tax (Trading and Other Income) Act 2005, Income Tax Act 2007, Corporation Tax Act 2009, Corporation Tax Act 2010, Taxation (International and Other Provisions) Act 2010, Inheritance Tax Act 1984 and annual Finance Acts

Tax treaties: The U.K. has concluded 125 tax treaties.

Tax authorities: HM Revenue & Customs

International organizations: OECD, EU, WTO

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