Tax Considerations for UK Technology Companies

Doing Business in the US

UKTI Trade Services
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Introduction

Your UK technology company is looking to enter the US market, whether by licensing or selling software to US customers, creating or modifying software for US customers or providing US customers with access to a cloud or software as a service (SaaS) solution. This publication highlights some US and UK tax considerations that you should take into account in determining how you will structure your UK company’s business with US customers.

A UK company conducting transactions with US customers may be subject to US taxes (directly or indirectly). This generally depends on the nature and extent of the UK company’s connections with the US, such as whether the UK company conducts transactions with US customers through US-based employees or agents or a US subsidiary, or directly from the UK.

If your UK company is eligible for benefits under the income tax treaty between the US and the UK, in some circumstances, the company may be wholly or partially exempt from certain US federal income taxes under this treaty.

US and UK tax matters are complex. The determination of tax consequences depends on the specific facts and circumstances of each particular situation. This publication provides very general information regarding some relevant US and UK tax matters. It is not tax advice and you should not rely on it in planning your business. You should consult a tax advisor concerning US and UK tax consequences if your UK company conducts activities in the US or transactions with US customers.

It is assumed that your UK company is a UK corporation taxpayer, whether at the main rate (currently 24%, reduced by marginal relief where appropriate) or the small companies’ rate (currently 20%). In either case, all of your UK company’s worldwide taxable profits will be subject to UK corporation tax. Special UK tax rules apply in relation to profits of a UK company from certain types of technology and other intellectual property, including significant tax depreciation allowances, on which we are happy to provide specific advice if requested.
Background – US Taxation of US Persons

The US federal government generally imposes income taxes on the worldwide income of individuals who are US citizens or US residents (as determined for US federal income tax purposes) and corporations organized under US law, regardless of where the corporation is managed or controlled. US federal income tax is imposed at graduated rates. The maximum US federal income tax rate for individuals and corporations currently is 35%. The maximum rate for individuals is scheduled to increase to 39.6% in 2013 absent amending legislation.

US states, counties and cities also may impose income taxes on resident individuals, income or business taxes on corporations and non-resident individuals engaged in business in the jurisdiction, as well as property taxes and sales and use taxes. The US does not have a value added tax.
Background – US Taxation of Non-US Persons

Individuals who are not US citizens or US tax residents and corporations not organized under US law may be subject to income taxes imposed by the US federal government on income from US sources and, in limited circumstances, on income from non-US sources. For this purpose, the “source” of income is determined under US federal income tax principles.

A non-US person engaged in business within the US (as determined for US federal income tax purposes) generally is subject to US federal income tax on the US source and, in limited circumstances, non-US source, net income earned, or deemed to have been earned, from that business (all such income sometimes referred to as income “attributable to” a US business). This tax is imposed on the US business income at the regular graduated income tax rates applicable to US persons.

The non-US person has to file a US federal income tax return reporting the US business income. The non-US person’s US business income also generally is subject to a US federal “branch profits” tax at a 30% rate to the extent the US business income is not reinvested in the US business. The US federal net income tax and branch profits tax may be reduced or eliminated under an applicable income tax treaty between the non-US person’s home country and the US, discussed below. In addition, a non-US person conducting a business within the US may be subject to US state and local income or business taxes, property taxes and sales and use taxes.

A non-US person’s US source income that is not attributable to a US business, if any, conducted by the non-US person (or, where a non-US person conducts a US business, that is not attributable to a US “permanent establishment”, as discussed below) may still be generally subject to US federal income tax imposed on a gross basis to the extent the income is so-called “fixed or determinable” income, a broad category that excludes most gains and certain types of interest income.

The US payor of the income is required to withhold this tax on the gross amount of the income at a 30% rate, or a lower rate under an applicable income tax treaty between the non-US person’s home country and the US, discussed below. The non-US person generally does not have to file a US federal income tax return reporting this type of income unless the tax was not properly withheld by the US payor. This type of income generally is not subject to US state or local taxes.

These US federal income taxes may be reduced or eliminated when the non-US person is eligible for benefits under an income tax treaty between the US federal government and the non-US person’s home country (for example, the UK). However, US state and local taxing authorities are not bound by these income tax treaties. For example, a non-US person conducting business within a US state may be subject to income tax imposed by that state, even though the non-US person is exempt from US federal income tax under an applicable US income tax treaty between the non-US person’s home country and the US.

There is an income tax treaty in effect between the US and the UK. Accordingly, it is important to determine whether or not your UK company is entitled to benefits under the US-UK income tax treaty.
Your UK company may decide to establish a presence in the US, for example, by opening a sales or marketing office in the US or by hiring employees or agents in the US. The specific facts and circumstances determine whether this results in the UK company being treated as engaged in business within the US for US federal income tax purposes — and, consequently, subject to US federal net income tax and tax return filing obligations. The relevant facts and circumstances include the nature, frequency and continuity of the activities conducted by the US-based employees or agents and whether your UK company is eligible for benefits under the US-UK income tax treaty.

Accordingly, it is important to consult with a US tax advisor concerning the tax consequences of establishing a US office or hiring US-based employees or agents.

For example, assume your UK company’s US-based employees or agents have (1) the authority to solicit, negotiate and conclude license or sales agreements with US customers that bind the UK company or to perform other significant services necessary to complete license or sales transactions with US customers, and/or (2) a stock of software from which orders are filled on behalf of the UK company. These activities may well result in the UK company being treated as engaged in business within the US for US federal income tax purposes — and, therefore, subject to US federal net income tax — unless the UK company is exempt from this tax under the US-UK income tax treaty, as discussed below. Whether or not the UK company is treated as so engaged may depend on the scope of the employees’ or agents’ authority, the frequency and continuity with which that authority is exercised and whether the agents are independent agents (discussed below). If the UK company is so engaged, it generally will be subject to the US federal branch profits tax referred to above at a 30% rate. If the UK company is eligible for benefits under the US-UK income tax treaty, it may be completely exempt from the US federal branch profits tax or may be subject to this tax at a reduced rate of 5% under the treaty.

If your UK company is eligible for benefits under the US-UK income tax treaty and does not have a US “permanent establishment” (as defined in the treaty), generally it should be exempt from US federal net income tax on its US business income and the US federal branch profits tax. Accordingly, consideration should be given to whether or not it is commercially feasible to conduct
the UK company’s transactions with US customers in a manner that avoids a US “permanent establishment.” Your UK company may avoid having a US “permanent establishment” under the treaty by conducting transactions with US customers inside the US through brokers, general commission agents or other independent agents (e.g., independent sales agents or distributors) acting in the ordinary course of their business in their capacity as such. This should be the case even if these agents have the authority to solicit, negotiate and complete transactions with US customers that bind the UK company or have a stock of software from which orders are filled on behalf of the UK company, and these agents conduct these activities with some frequency over a continuous period of time. Of course, any decision to act in the US through independent agents, rather than through employees or a dedicated, dependent agent, could present significant non-tax issues that should be carefully considered.

Also, your UK company may avoid having a US “permanent establishment” if it uses a US office solely for the purpose of storing, displaying or delivering software and storing software to be used solely for those purposes and certain other US-based activities which are described in the US-UK income tax treaty.

In analyzing whether or not your UK company has a US office or “permanent establishment”, a US-based website or server used to conduct business with customers should be taken into account as it is uncertain whether such a website or server could be viewed as a place of business or a “permanent establishment” in the US.

If your UK company does not have US “permanent establishment” and thus is exempt from US federal net income tax, the UK company still may be subject to withholding of US federal income tax on a gross basis – discussed below under “Conducting Business Directly from the UK”.

If your UK company has a “permanent establishment” in the US and your UK company is eligible for benefits under the US-UK income tax treaty, credit will generally be allowed by HM Revenue & Customs (HMRC) in respect of any US federal income tax and US federal branch profits tax paid by the UK company on the same profits; the credit will be capped at the applicable rate of UK corporation tax in respect of any profits deemed attributable to that permanent establishment (as determined for UK tax purposes) in calculating the amount of the credit. Should your UK company not be eligible for benefits under the US-UK income tax treaty, as an alternative strategy it is now possible under UK tax law to elect for an exemption from UK corporation tax with respect to such foreign branch profits in order to avoid double taxation, although further advice should be taken on the consequences of making this election.
Conducting Business through a US Subsidiary

If your UK company’s US activities rise to the level of conducting business in the US for US federal income tax purposes – and having a US “permanent establishment” under the US-UK income tax treaty, if applicable – you should consider whether the UK company should conduct transactions with US customers through a subsidiary that is a US corporation or a US limited liability company (LLC) that is taxed as a corporation for US federal income tax purposes (if a US LLC is used, UK tax advice should be taken concerning any potential adverse or uncertain UK tax consequences). This should enable your UK company to avoid having to file US federal income tax returns itself. Instead, the US subsidiary would be subject to US federal income tax on its worldwide income and applicable US state and local taxes, and it would have to file US federal income tax returns and other applicable US tax returns. Distributions of the US subsidiary’s earnings to the UK company generally would be subject to withholding of US federal income tax at a 30% rate. If your UK company is eligible for benefits under the US-UK income tax treaty, these distributions may be completely exempt from this withholding tax or subject to this withholding tax at a reduced rate of 5% under the US-UK income tax treaty. Any distribution or dividend paid by the US subsidiary to your UK company generally will be exempt from UK corporation tax. However, the UK tax rules on distributions are complex, and specific UK tax advice should be sought.
Conducting Business Directly from the UK

Your UK company may decide to act from the UK in its transactions with US customers and otherwise have no presence (e.g., no office, server, website, employees or agents) in the US or, if it is eligible for benefits under the US-UK income tax treaty, operate so as to avoid having a US “permanent establishment” under the treaty, as discussed above.

Even if your UK company is not engaged in business in the US or does not have a US “permanent establishment” under the US-UK treaty, your UK company may be subject to gross basis withholding of US federal income tax on so-called US source “fixed or determinable” payments it receives in respect of transactions involving computer software. The payments that may be subject to this US withholding tax include (i) royalties for the license of a copyright in a computer program or other intellectual property, (ii) rents for the lease of a copy of computer program or other intellectual property, and (iii) payments from a sale of a copyright in a computer program or sale of other intellectual property that is contingent on the productivity, use or disposition of the copyright or other intellectual property. However, to the extent your UK company is eligible for benefits under the US-UK income tax treaty, the rate of US withholding tax imposed on most, if not all, of these items may be reduced to zero. Absent benefits under the US-UK income tax treaty, the general rate of US withholding tax on these items would be 30%. Note that there are complex US federal income tax rules and judicial decisions that determine how various types of transactions in intellectual property are to be characterized for US federal income tax purposes; these authorities are uncertain in scope and may result in payments being subject to US withholding taxes even if they are not labeled as “royalties”, for example, or even if the payor is not a US person. Accordingly, it is important that you consult a US tax advisor concerning the US tax consequences of your UK company’s transactions in intellectual property.

If the UK company is eligible for benefits under the US-UK income tax treaty, in order to claim an exemption from US federal withholding tax under the treaty, the UK company would have to provide to its US customer a US tax form, a W-8BEN, that indicates the UK company’s US taxpayer identification number (for a company, generally its US employer identification number). The UK company would obtain a US taxpayer identification number by filing a form SS-4 with the US Internal Revenue Service. The UK company’s obtaining a US taxpayer identification number, in and of itself, should not result in the UK company being subject to US federal income tax or withholding of such tax. A filled in sample of a W-8BEN form is provided in Exhibit 1 on the next page.

This W-8BEN form generally is valid for three calendar years following the year in which it is signed by the UK company, unless information provided on the form materially changes during that time period. This form is not filed with the US Internal Revenue Service, but rather must be retained by the US customer.
**Exhibit 1:**

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**W-8BEN**

**Certificate of Foreign Status of Beneficial Owner for United States Tax Withholding**

- Section references are to the Internal Revenue Code. ➤ See separate instructions.
- ➤ Give this form to the withholding agent or payer. Do not send to the IRS.

**OMB No. 1545-1621**

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**Do not use this form for:**
- A U.S. citizen or other U.S. person, including a resident alien individual.
- A person claiming that income is effectively connected with the conduct of a trade or business in the United States.
- A foreign partnership, a foreign simple trust, or a foreign grantor trust (see instructions for exceptions).
- A foreign government, international organization, foreign central bank of issue, foreign tax-exempt organization, foreign private foundation, or government of a U.S. possession that received effectively connected income or that is claiming the applicability of section(s) 115(2), 501(c), 892, 895, or 1443(b) (see instructions).
- A person acting as an intermediary.

**Instead, use Form:**
- W-9
- W-8ECI or W-8EXP
- W-8ECI or W-8IMY
- W-8ECI or W-8EXP

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**Part I  Identification of Beneficial Owner (See instructions.)**

<table>
<thead>
<tr>
<th>1 Name of individual or organization that is the beneficial owner</th>
<th>2 Country of incorporation or organization</th>
</tr>
</thead>
<tbody>
<tr>
<td>UK Company</td>
<td>United Kingdom</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>3 Type of beneficial owner:</th>
<th>4 Permanent residence address (street, apt. or suite no., or rural route). <strong>Do not use a P.O. box or in-care-of address.</strong></th>
</tr>
</thead>
<tbody>
<tr>
<td>Individual</td>
<td>100 Main Street</td>
</tr>
<tr>
<td>Corporation</td>
<td>London</td>
</tr>
<tr>
<td>Disregarded entity</td>
<td>City or town, state or province. Include postal code where appropriate.</td>
</tr>
<tr>
<td>Partnership</td>
<td>Country (do not abbreviate)</td>
</tr>
<tr>
<td>Simple trust</td>
<td>United Kingdom</td>
</tr>
<tr>
<td>Central bank of issue</td>
<td></td>
</tr>
<tr>
<td>Tax-exempt organization</td>
<td></td>
</tr>
<tr>
<td>Private foundation</td>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>5 Mailing address (if different from above)</th>
<th>6 U.S. taxpayer identification number, if required (see instructions)</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>XX-XXXXX</td>
</tr>
</tbody>
</table>

**Part II  Claim of Tax Treaty Benefits (if applicable)**

9 I certify that (check all that apply):

a [ ] The beneficial owner is a resident of the United Kingdom, within the meaning of the income tax treaty between the United States and that country.

b [ ] If required, the U.S. taxpayer identification number is stated on line 6 (see instructions).

c [ ] The beneficial owner is not an individual, derives the item (or items) of income for which the treaty benefits are claimed, and, if applicable, meets the requirements of the treaty provision dealing with limitation on benefits (see instructions).

d [ ] The beneficial owner is not an individual, is claiming treaty benefits for dividends received from a foreign corporation or interest from a U.S. trade or business of a foreign corporation, and meets qualified resident status (see instructions).

e [ ] The beneficial owner is related to the person obligated to pay the income within the meaning of section 267(b) or 707(b), and will file Form 8833 if the amount subject to withholding received during a calendar year exceeds, in the aggregate, $500,000.

10 **Special rates and conditions** (if applicable—see instructions): The beneficial owner is claiming the provisions of Article of the treaty identified on line 9a above to claim a, % rate of withholding on (specify type of income): .

**Part III  Notional Principal Contracts**

11 [ ] I have provided or will provide a statement that identifies those notional principal contracts from which the income is not effectively connected with the conduct of a trade or business in the United States. I agree to update this statement as required.

**Part IV  Certification**

Under penalties of perjury, I declare that I have examined the information on this form and to the best of my knowledge and belief it is true, correct, and complete. I further certify under penalties of perjury that:

1 I am the beneficial owner (or am authorized to sign for the beneficial owner) of all the income to which this form relates.

2 The beneficial owner is not a U.S. person.

3 The income to which this form relates is (a) not effectively connected with the conduct of a trade or business in the United States, (b) effectively connected but is not subject to tax under an income tax treaty, or (c) the partner’s share of a partnership’s effectively connected income, and

4 For broker transactions or barter exchanges, the beneficial owner is an exempt foreign person as defined in the instructions.

Furthermore, I authorize this form to be provided to any withholding agent that has control, receipt, or custody of the income of which I am the beneficial owner or any withholding agent that can disburse or make payments of the income of which I am the beneficial owner.

**For Paperwork Reduction Act Notice, see separate instructions.**

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**Cat. No. 25047Z Form W-8BEN (Rev. 2-2006)**

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**Form W-8BEN (Rev. February 2006)**

**Department of the Treasury Internal Revenue Service**

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For information on the services available to you, or to locate your nearest International Trade Team, please visit our website: www.ukti.gov.uk

UK Trade & Investment has teams located in the British Embassy in Washington DC and eight British Consulates around the United States. For more information on our offices, please visit: www.ukinusa.fco.gov.uk

U.S. States
If you are looking for advice on establishing a presence in the United States, Select USA is a programme under the US Department of Commerce that explains the benefits and puts you in touch with relevant US Economic Development Agency contacts: selectusa.commerce.gov

In addition, many US States maintain offices in the UK or elsewhere in Europe. The US state governments are a good source of advice and information about business conditions in their states. Please visit the Council of the American States in Europe website for more information: www.case-europe.com

U.S. Lawyers
A list of American attorneys based in the UK is available on the US Embassy website: www.usembassy.org.uk

The American Bar Association website provides extensive lists of law firms across the United States. You can search by geography, area of practice or just browse the list of law firms to search for ABA-certified lawyers by state and by specialty: apps.americanbar.org/legalservices/iris/directory
Select U.S. Government Resources

All US federal agencies
www.usa.gov/directory/federal/index.shtml

Alcohol and Tobacco Tax and Trade Bureau (TTB)
www.ttb.gov/index.shtml
Regulates Alcohol & Tobacco

American Embassy, London
london.usembassy.gov
Represents US diplomatic interests abroad

Consumer Product Safety Commission (CPSC)
www.cpsc.gov
Regulates Consumer Products

Customs & Border Protection (CBP)
www.cbp.gov
Regulates and facilitates international trade, collecting import duties, and enforcing US regulations, including trade, customs and immigration

Federal Trade Commission (FTC)
www.ftc.gov
Presides over Dissatisfaction with Business Practices

FedWorld
www.fedworld.gov
Online locator service for a comprehensive inventory of information disseminated by the US Federal Government

Food & Drug Administration (FDA)
www.fda.gov
Regulates Cosmetics & Drugs, Food, Medical Devices, Veterinary Medicines & Electronic Product Radiation

Internal Revenue Service (IRS)
www.irs.gov
Responsible for tax collection and tax law enforcement

National Institute of Standards and Technology (NIST)
www.nist.gov
Promotes US innovation and industrial competitiveness by advancing measurement science, standards, and technology in ways that enhance economic security and improve quality of life

Occupational Safety & Health Administration (OSHA)
www.osha.gov
Assures safe and healthful working conditions by setting and enforcing standards and by providing training, outreach, education and assistance

Small Business Administration (SBA)
www.sba.gov
Provides support to entrepreneurs and small businesses

United States International Trade Commission (USITC)
www.usitc.gov
Provides international trade statistics and the Harmonised Tariff Schedule

United States Patent and Trademark Office (USPTO)
www.uspto.gov
Issues patents to inventors and businesses for their inventions, and trademark registration for product and intellectual property identification
UK Export and International Business Development Resources

**British American Business, Inc.**
www.babinc.org
Leading transatlantic business organization, dedicated to helping companies connect and build their business on both sides of the Atlantic.

**British Standards Institute**
www.bsigroup.com/en
Multinational business services provider that advises on how to meet technical standards and approvals procedures.

**Business Link**
www.businesslink.gov.uk
UK government’s online resource for businesses, providing guidance on regulations and to access government services.

**Department for Business Innovation and Skills (BIS)**
www.bis.gov.uk
UK department that supports sustained growth and higher skills across the economy.

**Export Control Organisation**
www.businesslink.gov.uk/exportcontrol
Helps businesses regarding export procedures and documentation.

**Export for Growth Guide**
(Click here for PDF Guide)
SME export guide produced by Forum of Private Business in conjunction with UK Trade & Investment.

**HM Revenue & Customs**
www.hmrc.gov.uk
UK department responsible for the collection of taxes.

**UK Export Finance**
www.ukexportfinance.gov.uk
Export credit agency that provide assistance with credit insurance and financing products.

Company Information

**Better Business Bureau**
www.bbb.org

**Dun and Bradstreet:**
www.dnb.com

**Oanda**
www.oanda.com
Foreign exchange rates, current and historical.

**Nasdaq**
www.nasdaq.com

**US Securities and Exchange Commission**
www.sec.gov

**Forbes Magazine**
www.forbes.com/forbes

**US News & World Report**
www.usnews.com
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UK Trade & Investment offers expertise and contacts through its extensive network of specialists in the UK, and in British embassies and other diplomatic offices around the world. We provide companies with the tools they require to be competitive on the world stage.