AUDIT • TAX • ADVISORY

Family Investment Companies

A Family Investment Company is a private company whose shareholders are family members. It offers a flexible vehicle for managing family wealth and enables the tax-efficient accumulation and distribution of profits among family members.

Tax planning

FIC's have become more popular in recent years for several reasons.

Changes to the taxation of trusts make them less attractive for holding family wealth, but if appropriately structured, family investment companies can offer similar benefits in terms of asset protection and earmarking for future generations, without the restrictions.

In particular the inheritance tax charge of 20% on contributions in excess of the trust settlor's available nil rate band (currently £325,000) is not a concern with an FIC.

The divergence between the rates of tax applying to individuals and trustees (up to 45%) and companies (currently a maximum of 25% but can be as low as 19%) has provided a further incentive to incorporate and hold family wealth within a company.

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The way you are taxed

Dividend income is generally exempt from Corporation Tax in the hands of the company. Other income and gains are subject to corporation tax, at 19% for companies earning under £50,000, while companies earning over £250,000 will pay at 25%, and marginal relief will apply for companies earning more than £50,000 but less than £250,000. This can be a substantial saving compared to much higher Income Tax and CGT rates.

There is no Inheritance Tax on the establishment of the company or subsequent gift of shares to family members. Unlike a trust, an FIC is not subject to Inheritance Tax charges on each ten-year anniversary. Relief is available to the company for interest on loans to acquire further investments. This compares favourably to individuals and trustees who generally receive no tax relief on such loans. In the case of residential property investment, individuals and trustees now only receive restricted relief for finance costs, whereas a family investment company would receive full relief.

Relief is also available for expenses incurred in managing the company's investment and running its business. This includes investment managers fees, which an individual would not be able to claim.

Simple example

We are often advising clients who have realised significant cash, for example from a business sale, and are considering these structures as efficient ways to manage and pass on personal wealth with flexibility and security. However it may not always be straightforward, but we can assist you with transferring an existing investment business into a limited company. This would typically be a property investment business, which can sometimes qualify for reliefs from CGT and SDLT on the transfer.

There is then the option of paying dividends. These are subject to income tax but there may be different classes of share to provide some flexibility to whom dividends are paid. One significant advantage of a family investment company over personal investment is the ability for the company to make employer pension contributions for directors or employees of the company, typically the family members. Pension contributions will normally be tax deductible for the company and will be a tax-free benefit for the individual.

Inheritance tax and estate planning

Inheritance tax is one of the main reasons that clients set up family investment companies. A simple case where a client has some cash to invest, a company may be set up as follows:

- Ordinary shares for themselves (husband and wife) and shares for any children or grandchildren. These could be different classes of share which may provide you with some flexibility over the payment of dividends.
- The share rights may be different to provide more voting rights on one class for the purposes of control, but perhaps more capital rights to another class to pass the accumulation of wealth down a generation.
- You may fund the family investment company by way of loan, repayments of which can be made from investment profits without incurring any additional tax liabilities.
- The loan would remain within the founding shareholder's estate for inheritance tax purposes, but you could consider gifting that loan to other family members allowing them to receive tax-free repayment of the loan. The loan would fall outside the founder's estate after seven years.

Should the donor continue to hold shares in the family investment company at the date of death, the value of those shares will be calculated reflecting the size of the shareholding and restrictions imposed in the articles and any shareholder agreement on the sale of those shares.

The discount might be substantial, meaning that the value remaining in the estate is significantly less than the percentage shareholding.

For further assistance

Please contact your usual MHA adviser for more guidance on these changes and help in reviewing your tax plan. Alternatively, please contact your local office and we will be happy to assist you.

This communication is for general information only, not intended to be individual investment advice, a recommendation, tax, or legal advice.

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