Dow Schofield Watts
Private Client Tax

Family Investment Company

Tax Factsheet

A family investment company ("FIC") is a bespoke, tax-efficient structure which can be used in succession planning as an alternative to traditional family trusts. The arrangement enables family wealth to accumulate and be passed on to future generations, whilst allowing parents or grandparents to retain control and protect their assets.

Key Facts:

- A family investment company can help in succession planning with the tax-efficient transfer of wealth to future generations.
- The structure can help to protect assets as an alternative to a trust
- There are a number of company tax benefits that help to increase wealth accumulation over time.
- The company can be structured to ensure the founder retains ultimate control.

How does a FIC work?

A typical FIC structure could be as follows:

- A UK private limited or unlimited company is incorporated to hold the assets of a 'founder' for his or her family.
- The wealth transferred into the FIC will usually be surplus to the founder's everyday requirements.
- The founder can provide the funds to the FIC by way of a loan, share capital or a combination of both.
- On formation, the company will usually have at least two classes of shares.
- The parents or founders will subscribe for shares, with the company articles drafted in a manner to retain control of the assets through shareholder rights.
- Additional classes of shares can be subscribed for by other family members personally or via a Trust structure to enable not only the transfer of wealth but, the opportunity and flexibility to pay dividends in the future.
- This subscription of shares by family members does not result in an immediate tax charge and, provided the founders survive seven years from the date of subscription, there will be no inheritance tax implications.
- As the value of the company increases, this is spread amongst the shareholders, being the wider family, which over time will prove to be powerful IHT planning.

Key Tax Benefits

The company will pay corporation tax on its profits at a low rate of 19%, falling to 17% from 1st April 2020.

Any capital gains realised in the company are subject to corporation tax at 19% rather than the main capital gains tax rate of 20% for individuals.

A company is able to claim a corporation tax deduction for any interest it pays on a loan taken out for the purposes of its business – this is different to individuals who are not eligible for the relief.

Most dividends received by a UK company are exempt from corporation tax.

Expenses incurred by a company in managing its assets are often deductible for corporation tax purposes, this could include investment management and accountancy fees.

Excess management expenses and loan interest relief can be carried forward and offset against future business profits

Control

It is often the case that parents and grandparents are eager to look at transfer wealth to younger generations, but are concerned about the loss of control that may result in succession planning - a FIC structure may help to overcome this obstacle.

As with any company, day to day control and decision making rests with the directors. From an investment perspective, the board of directors decide where funds are invested and what dividends are declared, it is therefore often the case that the founder takes up this position either individually or alongside trusted friends and family, to retain control of their assets through the daily management of the FIC.

Supplementary to this, the way a FIC's shares are structured is flexible. Shareholdings can be arranged in such a way as to allow a certain share class to have control over the company including making key decisions such as the appointment of directors, voting of dividends etc.

Other share classes are likely to have rights to income, but the company is likely to be structured in such a way that control is retained by the founder, therefore restricting others ability to make significant company decisions.

As time passes and children get older, the FIC allows control to be transferred gradually when appropriate, through the appointment of additional family directors or the transfer of shares to younger generations.

Tax on company distributions

Before any taxable distributions are made, the founders are able to withdraw the capital they provided on creation of the FIC, tax-free, by drawing down on their directors loan accounts.

Following this, if the shareholders declare dividends to extract profits from the company, distributions will be subject to dividend tax at a rate of 7.5% for basic rate taxpayers, 32.5% for higher rate taxpayers and 38.1% at the additional rate.

Inheritance Tax Planning

A FIC can be used to reduce or mitigate inheritance tax in a number of ways.

On incorporation, family members can subscribe for shares without incurring an immediate tax charge. Over time, when the underlying company investments appreciate in value so will these shares, spreading the wealth across the family.

The use of Trusts within the shareholder structure can act to offer further flexibility and control when transferring wealth. A founder could set up a discretionary trust with a wide class of beneficiaries to allow choice distributions to be made as and when required.

In addition, when looking at the death estate or future trust inheritance tax charges, HMRC often afford minority shareholders significant discounts when looking at the value of their shareholdings in unquoted investment companies.

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