Briefing Note

Mercer & Hole

FAMILY INVESTMENT COMPANIES

Family Investment Companies (FICs) can be a flexible option when considering your succession planning, particularly where you want to retain a level of control.

Until recent times, where an individual wished to remove assets from their estate, whilst retaining a level of control, their main option was to establish a trust (typically, a discretionary trust) of which they were a trustee.

However, trusts are an unfamiliar structure to most people which, coupled with the adverse press they have received as a component of a number of tax avoidance schemes, can mean that individuals are wary of them. In addition, there are limits on what cash funds can be settled in trust without there being an immediate Inheritance Tax (IHT) charge.

As a result there has been an emergence of the FIC structure as possible alternative to a trust.

When might a FIC be worth considering?

Generally, it is worth considering whether a FIC may be appropriate in the following circumstances:

- You have significant cash balances, typically above the IHT nil rate band (£325,000) and you wish to undertake IHT planning;
- You would like to retain a level of control and flexibility;
- Your children are adults (whilst it can work with minor children, it is more involved)

What is a FIC and how is it structured?

A FIC is a company, typically incorporated in the UK. The Articles of Association may be prescriptive as to who can own shares in the company and be restrictive as to share transfers only being amongst family members.

Whilst the share framework of the company is tailored to your specific needs, we have outlined below a couple of common example structures:

- The parent(s) retain(s) control via Ordinary voting shares (say 55%) with the children subscribing for the remaining Ordinary shares and also non-voting preference shares.

  The acquisition of Ordinary and Preference shares by the children is funded by way of a cash gift from the parent(s), which is a Potentially Exempt Transfer (PET) for IHT purposes. This means that there is no immediate IHT charge, irrespective of the level of the gift (unlike a gift to a discretionary trust) and it will not be subject to IHT on the death of the parent if they survive at least seven years.

This structure tends to be used where the parent(s) wish to give away significant value (invested in the preference shares by the children) whilst retaining control via their Ordinary shareholding. They are also likely to be directors of the company.

- Alternatively, the parent(s) fund the company by way of a loan and then retain control via Ordinary voting shares (say 55%) with the children susbcribing for the remaining Ordinary shares.

  The acquisition of Ordinary shares by the children is funded by way of a cash gift from the parent(s), which is a PET for IHT purposes (see above). In this scenario, the parent(s) make less of an immediate gift for IHT purposes, but retain the flexibilty to drawn down on the loan in the future or gift the loan to the children (which would be a PET at that time).

The share structure and funding of the company, and the tax consequences thereof, are key components of the design phase of a FIC structure which requires the input of both a tax advisor and a corporate lawyer.

How is the FIC taxed?

The profits of the FIC are subject to corporation tax in the same way as any other company. This is currently at a rate of 19%, but this will increase to 25% from 2023. A FIC will fall within the definition of a close investment holding company and therefore will not benefit from the small company rate. However, if the company invests in stocks and shares then currently any dividends received will be exempt from corporation tax (compared to income tax at 38.1% on dividends paid to a trust).

If the FIC pays dividends itself to shareholders, these will be taxed on the shareholders at their marginal rate of income tax which can currently be up to 38.1% (rising to 39.35% from 6 April 2022).

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