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Is a Family Investment Company right for you?

Historically, trusts have been the standard way to pass down family wealth to future generations. The Finance Act 2006 introduced changes in the UK's tax regime which significantly curtailed tax opportunities that trusts enjoyed previously. This change, alongside the more recent escalation in personal and dividend tax rates, has resulted in individuals wishing to protect and pass down wealth to look at other alternatives, one of which is the use of a Family Investment Company (FIC) as an 'investment wrapper'.

So what is a FIC?

A FIC is essentially a private investment company. The directors and shareholders of the Company will be individual family members or trusts. A FIC is a very flexible structure allowing families to define how specific family members benefit through varying rights attaching to shares or the number of shares in issue.

The shares can therefore be structured to allow the passing of ownership of underlying assets to the next generation without the older family members losing control too soon. The 'corporate veil' of an FIC arguable provides a greater degree of protection than a trust, particularly in circumstances where the structure is considered in a family court situation.

Creation of a FIC

There will be no tax charge when the Company is first set up and the initial subscription for shares is made in cash. If assets are transferred to the Company it will be deemed a disposal at market value for capital gains purposes and if property is transferred there may also be stamp duty land tax in addition to capital gains tax.

Perhaps shares or other assets not standing at a gain could be transferred or gains could be offset by also transferring assets standing at a capital loss. There may also be merit in considering the transfer of recently inherited assets which have benefitted from a Capital Gains Tax uplift.

How is a FIC taxed?

The UK has one of the lowest corporation tax rates of any of the Group 7 (G7) countries, currently set at 20% for 2015/16 this is set to reduce down to 17% from April 2020.

FICs are taxed the same as other companies and pay corporation tax on their annual income and gains. Unlike individuals, FICs still benefit from indexation on capital gains, removing an allowance for inflation from the charge to tax.

Crucially, there is no charge to corporation tax if the FIC is in receipt of dividend income from UK companies and the FIC therefore offers potential protection from high personal and trust tax rates of up to 38.1% from 6 April 2016.

Extracting Funds

FICs are often most efficient as long term investment vehicles when profits are retained within the Company.

If an individual places the money in the Company, this will often be by way of a loan. These loans are often interest free and repayable on demand. If income is required repayments of loan capital can be made without incurring further tax. For example shares may be sold to the company but the proceeds left on loan, perhaps due to a newly formed FIC not having available funds. When dividend income begins to flow to the company these could be used to fund loan repayments, giving the 'founder' access to the funds in a tax free form.

As with most companies, tax will arise where profits are extracted either in the form of income tax on distributions or capital gains tax on share disposals. From April 2016 the dividend regime has changed and a new tax free dividend allowance of £ 5,000 has been introduced. Any dividends above this level will be taxed at 7.5% (basic rate), 32.5% (higher rate) and 38.1% (additional rate).

Succession and Estate Planning

On creation the FIC may have minimal value and a gift of shares in a new company is unlikely to create any problems from an Inheritance Tax (IHT) perspective. The subsequent growth in value, either as a result of growth in the investments or reduction in an initial founder loan, is effectively removed from charge to IHT.

Consideration could also be given to the use of freezer or growth shares to direct growth to the next generation or the use of a discretionary trust in the structure to hold FIC shares, opening the door to a tax free ten year window for growth.

In summary, a FIC can provide a straightforward, tax efficient solution to family succession issues and offer flexibility to retain control over family issues. The solution will be most relevant to individuals with substantial investment assets and income, to be preserved for the next generation and protected from high personal tax rates. The tax perspective of a FIC is important but it is also essential to consider the protection, commercial and emotional aspects.

Should you wish to consider the use a FIC we can consider the best route forward based on the circumstances of you and your family. Please contact Mark Thompson or Kirsty MacDonald for further information by email at mark.thompson@renniewelch.co.uk or kirsty.macdonald@renniewelch.co.uk , telephone 01573 224391.