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GUIDE TO FAMILY INVESTMENT COMPANY'S (FICs)

Chartered Financial Planners

A Family Investment Company (FIC) is a company structure that can be used for investment, wealth protection and succession purposes. FICs have become more popular in recent years, particularly since the Finance Act 2006 whereby several changes to the tax rules for UK trusts were introduced. In essence, this resulted in less agreeable initial and ongoing taxation for significant transfers into Trust.

These changes have meant that affluent individuals wishing to pass their wealth on to their family have had to consider alternative, more tax efficient, options.

Family Investment Companies have become a viable solution for the wealthy, namely because the corporation tax rate (rising to 25% in April 2023) is generally more favourable when compared to the income tax rates payable personally or by trusts (up to 45%).

Another factor in the popularity of FICs is that assets within are deemed to be outside an individual's estate when calculating any liability to inheritance tax (IHT) - subject to proper structuring. This often results in lower IHT liabilities on family wealth, meaning more can be passed down. Conversely, assets held personally may be subject to IHT on death and income/profits earned for high earners could be charged to income tax at rates of up to 45% (although this top rate is now slated to be removed).

In this guide we will cover the following:

- What is a Family Investment Company?
- How does a FIC work?
- Privacy and Confidentiality of a FIC
- Flexibility of a FIC
- Why set up a FIC?
- How do you retain control of your wealth in a FIC?
- Frequently Asked Questions
- How Fiducia can help you

Please note, this guide provides an overview on Family Investment Companies and does not constitute financial advice. To identify whether a FIC is right for you and your circumstances, you should seek regulated financial advice.

Fiducia Wealth Management Ltd, Dedham Hall Business Centre, Brook Street, Dedham, Colchester Essex CO7 6AD or Saxon House, 27 Duke Street, Chelmsford, Essex CM1 1HT

What is a Family Investment Company?

A Family Investment Company (FIC) is a bespoke, private, company whose shareholders are family members. They are used as an alternative to a family trust for those with substantial cash or assets, generally £1million plus, excluding the value of their main residence.

An FIC enables originators to retain control over assets whilst accumulating wealth in a tax efficient manner and facilitating future succession planning. The structure can help to maximise the accumulation of private wealth whilst ensuring that any future IHT bill is kept to a minimum.

A primary objective in setting up a FIC is often to transfer wealth efficiently to the next generation, or even a subsequent generation, whilst retaining control over that wealth. FICs are also valuable for wealth accumulation, not just succession. Within an FIC, tax rates on income and asset growth are likely to be lower than would be paid personally or by a trust. Over several years, this may result in the FIC accruing greater wealth, faster.

FICs are set up for the long-term, the idea being that the founders of the FIC (usually parents), set up the company with an initial injection of funds or assets. Their children, and potentially grandchildren, will also be shareholders and benefit from the growth created by investments held within.

How does a FIC work?

Usually, the founder of the FIC will either gift or loan assets to the company. Cash, property, shares, artwork and even classic cars can be held in a FIC.

It is necessary to consult specialists in this area to set up an FIC, though once established they are taxed like any other Limited Company. The nature and split of assets held (i.e. property vs shares) within an FIC will impact its classification for tax purposes and therefore, the ongoing tax treatment.

A Shareholders agreement is drawn up as a contractual document between the Shareholders. The Shareholders will be family members and potentially a Family Trust or Employee Benefit Trust, if applicable. In order to make the FIC suitable for family estate planning, it is effectively treated as a Private Limited Company with bespoke articles of association.

Upon setting up the FIC, you may be named Director and preferential Shareholder, giving you control over the capital. It is important to understand that this may not give you rights to the capital itself, as often some value will be gifted to children. Gifted funds will generally fall outside of your estate for inheritance tax purposes after a period of seven years, provided you retain no beneficial interest in the asset, although an element of value may remain due to the control premium that you will retain in the FIC.

The type of shares that the FIC can issue include ordinary shares with differing rights, e.g. the right to vote, to receive dividends and to receive capital on winding up. These different rights and share types can be used to direct income to family members and to set out who controls the company.

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All rights are set out in the Company Articles of Association and in a Shareholders' Agreement. The day to day running of the Company will be carried out by the Directors, with their powers set out in the Shareholders' Agreement.

Family Investment Companies are subject to corporation tax on income and capital gains. The current rate of corporation tax is 19% (rising to 25% April 2023). Dividends received by a company from other UK companies are mainly exempt from corporation tax, this includes income from a share portfolio. Dividends paid to beneficiaries over the tax-free allowance of £2,000 will be taxed at the dividend rates of 8.75%, 33.75% and 39.35% depending on the individual's other income.

Privacy and Confidentiality of a FIC

It is rare for families to want to publicly share details of how much they are worth. The ability to invest privately is often desirable and can be achieved with a FIC.

An FIC may be set up as a private company with limited share capital or with unlimited share capital. The main difference is that unlimited companies are not required to file accounts at Companies House (retaining some of the privacy of the family's wealth). However, unlimited companies do not have the same protection from creditors, though depending on the assets held, this is unlikely to be an issue.

Clients often ask, "Do the children need to know at this stage?", though depending on the structure, they do not need to know anything about the family wealth until appropriate.

Flexibility of a FIC

FICs are intended to remain in place for the long-term, meaning flexibility is very desirable. Like with a Trust, though arguably with more scope to manage wealth in the way you desire, this can be achieved in a number of ways:

- Flexibility around what you can invest into
- Flexibility around who benefits and to what extent
- Flexibility around when and how these benefits are distributed
- Flexibility around control and succession of wealth

Why set up a FIC?

One of the main advantages of a Family Investment Company over a Trust, namely a Lifetime Discretionary Trust, is that in the latter an individual is limited to placing £325,000 (the inheritance tax nil rate threshold) without an immediate tax charge arising. Any excess will result in 20% tax being payable immediately. There is no upper limit on assets that can be placed into an FIC so it can enable a larger transfer of wealth in a tax efficient manner.

Family Investment Companies are subject to corporation tax on the income they receive. However, as corporation tax is often lower than personal or trust rates of tax, there will often be significant income advantages.

For those with property portfolios, mortgage interest is fully reclaimable in a company and not subject to a 20% tax credit as would apply to personally held buy-to-let property holdings. Therefore, if you have several rental properties, a FIC could be used to improve your tax efficiency dramatically.

Should the FIC hold an investment portfolio, most dividends received by a UK company from other companies are currently exempt from corporation tax. This may result in an increase in growth by deferring taxation until monies are distributed by the FIC.

There are other practical advantages, depending on your family's approach to investments. For example, the FIC's Directors can choose to take greater risks or consider alternative investment options, compared to those which Trustees might be comfortable with within a trust structure.

Where estate planning and inheritance tax are concerned, an FIC will allow you to place cash or assets into a company and potentially pass on your wealth to loved ones free of inheritance tax (after seven years), whilst retaining control over your assets during your lifetime.

How do you retain control your wealth in a FIC?

When setting up a Family Investment Company, as mentioned previously, a set of Articles of Association will be drawn up. These set out the different rights, rules and interests for each of the Shareholders in the company.

In these articles you can protect your wealth by including specific clauses covering certain shares and circumstances. These clauses can prevent shares being transferred outside of your family by restricting Shareholders to immediate family or family Trusts. Each direct descendent of your family can be allocated a different class of share. Spouses of children and grandchildren could be prevented from owning shares for protection in the event of divorce, for example.

Family members can have varying levels of responsibility and control over company decisions, rights to receive dividends and entitlements to the capital value of the company. The FIC can be structured to account for your own income or capital needs, as well as those the wider family, helping to control and distribute capital and income throughout your lifetime.

Frequently Asked Questions about FICs

I already have a property portfolio held in a Limited Company, why set up a FIC?

There are a couple of primary reasons to consider a FIC instead of a typical limited company. Firstly, having different classes of shares for your children and grandchildren to help with income tax issues is easier with a FIC as opposed to a typical limited company. Secondly, protecting your wealth and keeping it within your family can be more straightforward. In the event of one of your children or grandchildren divorcing, the ex-spouse cannot lay claim to any shares in the FIC if they cannot hold shares under the rules of a FIC.

I own properties in my personal name, can I set up a FIC immediately?

Significant property portfolios have potential for high levels of capital gains tax and can be inefficient from an income tax perspective. FICs may be used to improve the position and, over time, absorb a property portfolio into a more efficient structure. The way in which this is achieved can be somewhat complex so is beyond the scope of this guide, though individuals with substantial property in their own names should consider this route.

Can my children be Directors of a FIC?

Most people make their children Shareholders within the different classes of shares. Future growth of the company value will reside in those shares, thus stopping an IHT problem getting worse for the Settlor. However, the Directors are usually those who originally owned the assets as even after all capital shares are given away, an income could still be paid to them for management and Director's duties. Most people also want to retain control of the dividends paid out, so ordinarily adult children might not be made Directors until the death of the original Directors.

Can minors be shareholders?

Due to the tax implications of parents gifting to minor children, this may not be a sensible strategy. Once your children or grandchildren are over 18, they can be added as Shareholders to the company. This can help to reduce tax arising from income and gains through use of more personal allowances.

Why do I need a Financial Adviser to set up a FIC?

This type of structure requires specialist attention and many firms will be unfamiliar with FICs. Knowledge and experience is essential to ensure that the setup and ongoing management is carried out correctly. We work closely with experts in this area to ensure all angles have been covered and the FIC is established and managed in a way that suits your family and makes best use of the available tax advantages.

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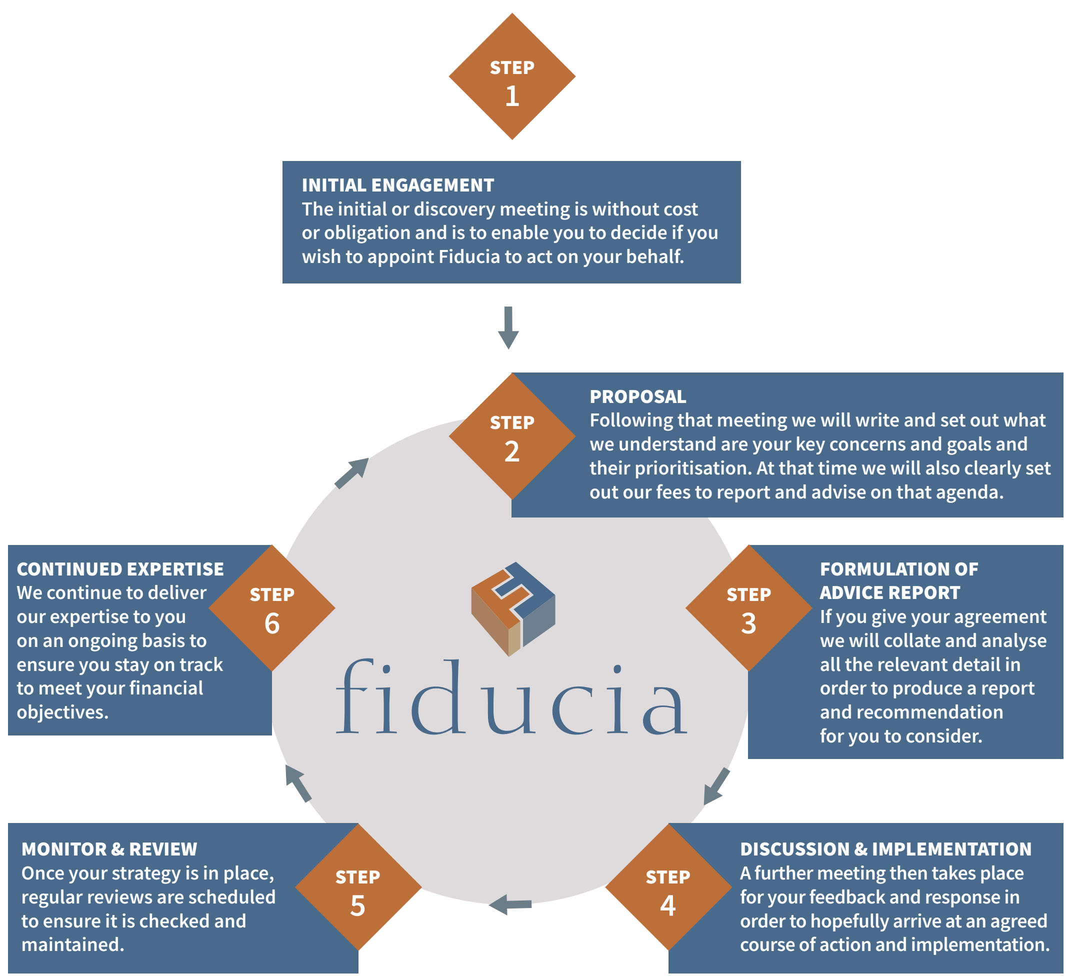
How can Fiducia help you?

Fiducia Wealth Management are a well-established, multi award-winning firm of Chartered Financial Planners. We have a proven track record of delivering outstanding wealth management and financial advice to private clients, business owners, family estates, charities, pension funds and trustees on tax, investments and financial planning.

Our offices are in Dedham on the Essex/Suffolk border and in Chelmsford.

We provide our expertise to a diverse range of clients throughout the East of England, London, and the UK nationwide. Integrity, openness and transparency are our core values, and we recognise that no two client's requirements, situations and objectives are the same – our solutions are therefore tailored to help you meet your financial goals and later life needs in the most tax efficient way.

We follow a tried and tested six step process to identify your financial objectives and risk profile to help determine the solutions that are right for you and your overall financial plan.



Are you ready to identify whether a Family Investment Company is right for you?

Speak to our team today, arrange your FREE initial discovery meeting and start your journey to achieving your financial goals.

Visit: www.fiduciawealth.co.uk
Email: email@fiduciawealth.co.uk
Telephone: 01206 321045

Visit our office:

Dedham Hall Business Centre
Brook Street,
Dedham
Colchester
Essex CO7 6AD.

Also at: Saxon House,
27 Duke Street,
Chelmsford,
Essex CM1 1HT.
Telephone: 01245 950922.

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wealth management & wealth preservation

fiduciawealth.co.uk

Dedham Hall Business Centre, Brook Street, Dedham, Colchester Essex CO7 6AD. Telephone: 01206 321045
And at: Saxon House, 27 Duke Street, Chelmsford, Essex CM1 1HT. Telephone: 01245 950922