Protecting wealth for future generations using a Family Investment Company

UK Landlord Tax

What is a Family Investment Company?

A Family Investment Company (FIC) is a bespoke private company whose shareholders are family members. A FIC allows parents to retain control over the assets gifted and any investment decisions by using different classes of shares each with their own rights. A FIC is a useful vehicle to accumulate wealth in a tax efficient manner and to protect and pass on this accumulated wealth to family members such as children or grandchildren to accommodate succession planning in a tax efficient and controlled manner.

When setting up a FIC we can use so-called "freezer" shares for the children or grandchildren. The intention is to freeze the value of the shares belonging to the parents or grandparents so that any future growth in value accrues to the next generation thus saving Inheritance Tax (IHT) on the growth in value of the shares. Whilst it is possible to alter the structure of an existing company into a FIC it is always best to do this at the time the company is formed when the value of any shares is nominal.

On death, for IHT purposes parents or grandparents will be taxed only on the value of their shareholdings in the FIC which will be equivalent to the amount of funds loaned to the FIC that are still outstanding on death. It is possible to gift these outstanding loans away during the lifetime of the parents or grandparents to achieve maximum tax efficiency if these funds are not required. Providing the parent or grandparent survives for 7 years after the date of the gift of these loans they would fall outside of their estates for IHT proposes.

> ***"A FIC is a useful vehicle to save both Income Tax and Inheritance Tax for your family if utilised correctly"***

Why should I consider using a FIC?

Many landlords are concerned about Inheritance Tax and succession planning. A FIC can allow landlords to benefit from the income of a property portfolio whilst gifting the capital growth in value of the portfolio to their children or grandchildren. This can result in significant IHT savings as the growth in value of the assets gifted will fall outside the estates of the parents or grandparents for IHT purposes.

Another major concern for landlords who are higher rate taxpayers is the restriction of tax relief on mortgage interest payments which was introduced by HMRC with effect from 6 April 2017, commonly known as Section 24. Any properties in a FIC will be eligible for full tax relief for mortgage interest payments made which can result in significant Income Tax savings in comparison to properties held personally by a higher rate taxpayer.

FIC's are subject to Corporation Tax at 19% on the net profits of the company up to £50,000. Further tax is only payable when funds are extracted from the company by the shareholders. Therefore, if funds are retained in the FIC this can facilitate the repayment of mortgages or the funding of further property acquisitions in a more tax efficient manner than if the properties were held personally by a landlord.

Any dividends taken from the company will be taxed at the marginal rate of the individual for that tax year other than the first £500 of dividends per shareholder which can be taken tax-free each year. If a shareholder does not have any other income, they could take out income from the FIC to utilise their lower rate of Income Tax instead of a family member who is a higher rate taxpayer to save Income Tax as a family. Shareholders also have the flexibility of taking dividends in a tax year of their choice in which they are subject to a lower rate of Income Tax which is not possible for properties owned personally by landlords as any such income is taxed in the year of receipt.

For the parents or grandparents who have loaned funds to the FIC to acquire any properties, these loans can be repaid to the parents or grandparents tax-free when the FIC has sufficient funds.

If you need funds in respect of your minor children, i.e., for school fees, it may be possible to structure the FIC in a manner that will allow you to pay for these school fees with little or no tax to pay depending on the amount of income required to meet these school fees. If a child's grandparent gifts them shares in the FIC or sets up a Trust to hold these shares for the benefit of the child, it is possible to use the child's personal allowance and dividend allowance to extract £13,070 (based on the 2024/25 tax year) per child tax-free from the FIC to meet such expenses. It is important to note that this tax treatment will not apply if the parents gift the shares to the children as they would be taxed on the income from their minor children.

We recommend that the FIC is set up alongside a robust Shareholders' Agreement which is a private contractual document between the shareholders. The Shareholders' Agreement can include provisions that protect the shares in certain circumstances. For example, to prevent shares being transferred outside of the family in the event of a vexatious claim by future partners of the children thus providing 'bloodline protection' for the family. The Shareholders' Agreement can also include the basis and mechanism for valuing the shares in certain circumstances such as claims by future partners of the children which can mitigate the amount of wealth that escapes the family.

Some landlords have been apprehensive in the past about setting up FIC's as they were unsure as to HMRC's view of such structures. However, we are pleased to confirm that HMRC's FIC unit which was set up in 2019 has been recently disbanded as it concluded that families using FIC's are no more inclined towards tax avoidance than any other group in the taxpaying population. This should provide landlords with comfort that the FIC structure is a robust and sensible vehicle that can be used for succession planning and managing an income for your children whilst simultaneously saving you both Income Tax and IHT as a family.

"A Shareholders' Agreement alongside the FIC can help provide 'bloodline protection' for the family in the event of any vexatious claims by future partners of the children"

Case Study

Tom, 41, and Amy, 43, have two minor children aged 6 and 4. They wanted to gift their children a significant proportion of their wealth in the future but were unsure how they could do this in a tax efficient manner whilst retaining the income from the assets gifted during their lifetime for their ongoing needs.

We were able to set up a FIC for Tom and Amy who are the Directors of the FIC and the only shareholders with voting rights thus maintaining control of the company. The FIC acquired properties valued at £1m over three years by using £600k of commercial mortgages and £400k deposits which were loaned to the FIC by Tom and Amy. These loans will be able to be repaid to Tom and Amy free of any tax when the FIC has enough funds in the future.
We created a separate class of shares for the children using so-called “freezer shares” which allowed the future growth in value of the property assets to accrue to the children instead of being part of Tom and Amy’s estates for IHT purposes. This has saved Tom and Amy a significant amount of IHT in comparison to if Tom and Amy had owned the assets in their personal names until they passed these on to the children.

As an example, if Tom and Amy held these properties personally until the date of death for the last surviving spouse when they were valued at £3m, their IHT liability could be as much as £1.2m (assuming their IHT nil rate bands are already utilised by other assets). Using the FIC, only the original equity introduced to the FIC of £400k would be subject to IHT in Tom or Amy’s estate and the IHT liability would therefore be capped at £160k. The FIC will save Tom and Amy £1.04m in IHT based on these circumstances. The IHT liability could be reduced even further if Tom and Amy were to draw down the £400k Directors’ Loan account with the FIC free of any tax.

Further, Tom and Amy are able to take dividends from the FIC to meet their ongoing income needs and can do so flexibly between each other depending on their marginal rates of tax in any given tax year. If they decide not to take any income from the FIC, the left-over funds in the company can be rolled up to help pay the mortgages on the properties or to fund the acquisition of new properties without any additional tax being paid by Tom and Amy.

We helped save Tom and Amy both a significant amount of IHT and Income Tax and we can help your family save tax too. Please get in touch with us today if you would like more information.

How we can help

We're one of the UK's leading specialist accountants for property owners, whether you're just starting out on your letting journey or you're a multi-property rental veteran. At UK Landlord Tax we are here to listen to your objectives and to help you achieve your objectives by giving you robust practical advice in plain language with no jargon or long-winded technical explanations.

We can provide the following advice:

- Whether the FIC is a suitable vehicle for your family based on your personal circumstances
- Tax implications of acquiring properties using a FIC
- Tax implications of transferring existing properties to the FIC
- Which family members to include in the FIC and what rights to provide each family member based on your objectives
- The potential IHT savings available by setting up the FIC
- How to include grandparents to achieve maximum Income Tax savings as a family
- Setting up a Shareholders' Agreement to protect the wealth accumulated in the FIC for the family against any potential claims in the future
- How to extract funds from the FIC for each family member in the most tax efficient manner
- Other options available to landlords in respect of their existing property portfolio
- IHT advice in respect of your exposure to IHT based on your total assets including those owned in your personal names outside of the FIC

Consultation

Please get in touch and book a consultation with us today to discuss this further:

Simon Thandi
T: + 44 1902 711 370
E: enquiries@uklandlordtax.co.uk

Pav Mandir
T: + 44 1902 711 370
E: enquiries@uklandlordtax.co.uk

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