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Family Investment Company (FIC)

What is a Family Investment Company (FIC)?

At root, a FIC is simply a company. There is no legal definition of a FIC, and FICs are not subject to special rules of their own

As the name suggests, a FIC is a family company, set up by an older generation that wishes to transfer wealth to a younger generation (and beyond) in a structured way.

Most FICs also have the following characteristics (to paraphrase HMRC):

- The shares in a FIC may be held directly or via a Trust for the benefit of family members.
- There are often multiple classes of shares.
- The rights attached to the shares will often differ depending on the age or generation of the shareholders. The older generation tends to retain voting rights, whereas the younger generation tends to hold income rights and the underlying capital value.
- FICs are not trading companies. Instead, they hold investments, often in the form of cash, shares or property.

In recent years, FICs have been presented as an attractive alternative to Trusts for clients who wish to pass on wealth.

Both FICs and Trusts have a place in the range of legal structures that we discuss with clients. In general, Trusts are often the most appropriate way to achieve clients' objectives. However, depending on a client's assets, overall wealth, family circumstances and objectives, FICs can compare very favourably with Trusts.

Possible 'Pros' and 'Cons' of FICs v. Trusts

In some ways, FICs and Trusts are similar:

- The directors of a FIC, and the trustees of a Trust, are obliged to manage assets for the benefit of the underlying beneficiaries/shareholders.
- Directors and trustees make day-to-day decisions concerning the management of the FIC/Trust and maintain a significant level of control.

However, there are some important 'pros' and 'cons' of FICs. These can include:

PROS:

Inheritance tax on creation: A FIC can be set up without triggering an immediate lifetime inheritance tax (IHT) charge. By contrast, transferring money or assets to a Discretionary Trust (in excess of one's surplus income, any IHT reliefs, and the IHT nil-rate band allowance of up to £325,000 per person) can lead to an immediate lifetime IHT charge at 20%.

Funding: A FIC can be funded in a number of ways, e.g., by subscribing for shares, or making a loan. If a FIC is funded by way of a loan, the loan can be repaid to the founder, if and when appropriate. Money or assets added to a Trust cannot usually be repaid to the founder.

Ongoing IHT charges: Discretionary Trusts are subject to ten-yearly IHT charges at a rate of up to 6%, and proportionate charges on capital distributions. FICs are not.

Taxation of income and capital gains: A FIC's income and capital gains are taxed at the corporation tax rate. This is lower than equivalent personal tax rates and the rates that apply to Discretionary Trusts. This can allow a FIC to accumulate value more quickly than a Trust. Dividend income received by FICs from other companies can be tax free if relevant conditions are met.

Bringing the younger generation onboard: FICs may offer greater scope for inducting the younger generation into the management of family wealth. For example, the younger generation can be involved as shareholders before becoming directors.

Capital growth: It is possible to finely calibrate when capital growth will accrue to particular classes of FIC shares, using 'growth shares' and 'freezer shares'. This can be useful in relation to IHT planning.

Discounted value of shares for IHT: For IHT purposes, the value of individuals' shareholdings can be discounted to reflect the number of shares held and the rights of the class of shares held.

CONS:

Setting up: It costs more to set up a FIC than a Discretionary Trust. Setting up a FIC is a more involved process.

Capital gains tax on creation: If a FIC is funded by transferring assets to the FIC, there may be a capital gains tax (CGT) charge. Relief may be available.

Double taxation of income: There can be a double layer of taxation if and when a FIC's post-tax profits are paid to shareholders as dividends. In other words, shareholders may have to pay income tax on income that has already been taxed within the FIC. But, this can be mitigated with careful planning. If the main objective is to accumulate value within the FIC, this can be done efficiently and may outweigh a double layer of taxation in the long run.

Compliance work: FICs are subject to greater public reporting requirements than Trusts, even when a FIC is set up as an unlimited company. However, the gap in reporting requirements between FICs and Trusts has narrowed recently. Now, most kinds of Trusts need to register with HMRC's Trust Registration Service or will need to do so shortly.

Who can benefit: A FIC can only distribute money to its shareholders. By contrast, Discretionary Trusts can have relatively wide classes of beneficiaries. This issue can be ameliorated by holding FIC shares in a Discretionary Trust.

Winding up: Generally, FICs cannot be wound up as easily as Trusts.

Using FICs and Trusts together

FICs and Trusts are not mutually exclusive options. They can be used in tandem, for instance by holding FIC shares in either a Discretionary Trust or a tax-transparent Bare Trust for children.

By using FICs and Trusts together, the underlying assets can often be better protected against threats such as divorce, family disagreements and bankruptcy.

How can Wrigleys help?

Wrigleys has helped many clients set up FICs. We usually work closely with clients' personal accountants so that appropriate advice is provided concerning all relevant tax aspects.

Because Wrigleys specialises in private client law, including Wills, Trusts and Capital T axes (IHT and CGT), we can help to make sure that FICs are the right fit for our clients.

We are also well equipped to discuss how Trusts and pre-nuptial agreements can be used to protect FIC shareholdings and their underlying value.

For further information please contact one of the team or visit:

www.wrigleys.co.uk

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