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Selling a business whilst protecting proceeds from Inheritance Tax

Owning and building a business is a huge commitment. Over the years, business owners invest almost all of their time and energy, not to mention finances, to make it a success. It's common to have overcome a wide range of challenges and sometimes business owners have pivoted the business into completely new areas in order to thrive.

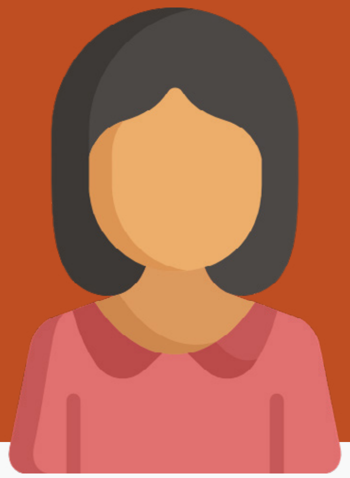
So it's understandable that when the time comes to sell the business, it's sad news for clients to hear that their hard earned proceeds may become part of their estate for Inheritance Tax (IHT) purposes. Faced with the potential of losing 40% to tax, clients will want to know what their options are to protect the value they have built up.

If a business that's sold was Business Relief (BR) qualifying, then with smart re-investing the owner could benefit from immediate IHT relief, by re-investing into another BR qualifying company.

Shares in BR-qualifying companies must be held for a minimum of two years and at the time of death to qualify.

Don't invest unless you're prepared to lose all the money you invest. This is a high-risk investment and you are unlikely to be protected if something goes wrong.

Take 2 minutes to learn more on page 4



Meet Eve

Eve has experienced ill health and decided that it's time to sell her business. As the business is expected to be BR-qualifying, the £500,000 in shares had been exempt from IHT up until the sale.

Eve had been considering putting the shares into a trust after hearing that it would protect the proceeds of sale from IHT. However, with her health now being in question, she's concerned that the minimum holding period of seven years may be too long. She speaks to her adviser to learn what her options are to achieve IHT relief sooner.

Guidance given by the adviser:

The adviser completes a thorough review of Eve's finances and explains the risks associated with investing, including an assessment of her ability to absorb the impact of financial loss.

Her adviser explains that as she has held the shares for at least 2 out of the previous 5 years, and if held at the time of death, they are expected to be BR-qualifying. So she has a window of opportunity. If the proceeds are reinvested into another BR-qualifying investment within three years of the sale, she should be able to gain IHT relief immediately.

In addition, Replacement Property Relief rules means that as she is transferring BR-qualifying assets into another potentially BR-qualifying investment, within 3 years of sale, the two-year clock will not restart in order to qualify for IHT relief.

Eve is also happy to hear that with this type of investment she will be able to retain access to her money, subject to liquidity, as this is important to her in managing her health moving forward.

Let's look at how her estate could change, using two different strategies (both examples assume the client has exhausted all applicable reliefs):

Eve sells the business and keeps the £500,000 as cash assets	Eve reinvests £500,000 proceeds into the Blackfinch Adapt IHT Service
40% IHT due against the full amount **£200,000**	IHT **£0**
Amount available to pass on: £300,000	**Amount available to pass on:** £500,000

Due to the Replacement Property Relief rules, the re-investment should provide an immediate exemption to IHT.

Clients must be advised that fees may apply. Please refer to our product literature for further details.

Inheritance Tax

Everyone has an allowance of £325,000, known as the nil rate band, which they can leave to beneficiaries free of IHT. If the individual has an estate valued above this amount, it could be subject to IHT at a rate of up to 40%.

Residence Nil Rate Band

Introduced in 2017, the Residence Nil Rate Band (RNRB) is an additional IHT relief that can be claimed against the value of a main residence. The RNRB is currently £175,000. RNRB rates are frozen until 2027/28 and is only applicable to one home of which the deceased has lived and owned at some point, and is being passed on to direct descendants (e.g. children or grandchildren). RNRB starts to be reduced where the death estate exceeds a £2m taper threshold.

Supporting the UK Economy

Certain businesses qualify for Business Relief, including shares in many AIM-listed firms. Unlike traditional IHT solutions, which can invest globally, clients' money is invested in BR-qualifying firms, that are predominantly UK-based

Advantages of BR

Can help preserve a family's wealth

BR assets can replace each other

Transfer by way of gift:
If the individual (donor) holds BR-qualifying shares for 2 years before gifting, and the recipient of the gift still holds the shares at the time of the donor's death, the investment retains IHT exemption for the donor (reduce estate).

Transfer into Trust
If the shares were already held for two years before the transfer into trust, the potential lifetime charge to IHT is reduced from 20% to zero.

Only takes 2 years to qualify for BR
Shares must be held at the time of death

Upon death there are various options

- Shares can be encashed and distributed to beneficiaries.
- Shares can be encashed, and proceeds paid to HMRC to pay any IHT bill due on the estate (Direct Payment Scheme).
- Shares can be passed down to beneficiaries who can then retain them. If the original owner had held the shares for over two years, the shares would be immediately BR qualifying (exempt) in the beneficiaries estate

For more information, speak to one of the team.

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Risks

Due to the potential for losses, the Financial Conduct Authority (FCA) considers this investment to be high risk.

What are the FCA key risks?

1 - You could lose all the money you invest
If the business you invest in fails, you are likely to lose 100% of the money you invested. Most start-up businesses fail.

2 - You are unlikely to be protected if something goes wrong
Protection from the Financial Services Compensation Scheme (FSCS), in relation to claims against failed regulated firms, does not cover poor investment performance. Try the FSCS investment protection checker. (https://www.fscs.org.uk/check/investment-protection-checker)

Protection from the Financial Ombudsman Service (FOS) does not cover poor investment performance. If you have a complaint against an FCA-regulated firm, FOS may be able to consider it. Learn more about FOS protection. (https://www.financial-ombudsman.org.uk/consumers)

3 - You won't get your money back quickly
Even if the business you invest in is successful, it may take several years to get your money back. You are unlikely to be able to sell your investment early.

The most likely way to get your money back is if the business is bought by another business or lists its shares on an exchange such as the London Stock Exchange. These events are not common.

If you are investing in a start-up business, you should not expect to get your money back through dividends. Start-up businesses rarely pay these. (https://www.financial-ombudsman.org.uk/consumers)

4 - Don't put all your eggs in one basket
Putting all your money into a single business or type of investment for example, is risky. Spreading your money across different investments makes you less dependent on any one to do well.

A good rule of thumb is not to invest more than 10% of your money in high-risk investments. (https://www.fca.org.uk/investsmart/5-questions-ask-you-invest)

5 - The value of your investment can be reduced
The percentage of the business that you own will decrease if the business issues more shares. This could mean that the value of your investment reduces, depending on how much the business grows. Most start-up businesses issue multiple rounds of shares.

These new shares could have additional rights that your shares don't have, such as the right to receive a fixed dividend, which could further reduce your chances of getting a return on your investment.

If you are interested in learning more about how to protect yourself, visit the FCA's website. (https://www.fca.org.uk/investsmart)

IMPORTANT INFORMATION

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