PayLessTax
2023 Spring Edition

Freezer/growth a property IHT option

For persons with a property portfolio one of the tax headaches, keeping them awake at night, is how to mitigate their inheritance tax (IHT) liability when passing on the properties to their children or grandchildren on death.

In the vast majority of cases the property values, net of any liabilities, such as debt, will form part of their estate for IHT purposes, resulting in a potential IHT charge of 40%.

There are limited ways to minimise this tax hit. **One such option requires the property portfolio to be housed in a corporate vehicle.**

As long as the company has been set up for bona fide commercial reasons, the parent's shares could be frozen at the current market value of the company. In broad terms, that is likely to be the value of the properties, plus any retained reserves within the company, less any outstanding debt. **Care needs to be taken that the parent's shares are not undervalued as this could have negative tax consequences.** To play safe, you may want to freeze those shares at market value plus say, 15%.

The company could then grant a second tranche of 'growth' shares, either directly to the children or through a trust (if you want to put a protective wrapper around the shares in case of potential issues in the future, such as divorces). **If the company increases in value above that set for the freezer shares, that growth will drop into the children's shares and fall outside the parent's estate for IHT purposes**.

The increase in the company value could come about from property capital growth, the reduction in the corporate debt and/or retained profits which neither the parents nor the children require being paid out of the business.

If properly implemented, this planning can be used even for children of a minor age. However, if a dividend is paid out on those particular growth shares it would be taxable on the parents and not the minor kids.

Example

- Tom, is a single man, with two children from a previous relationship.
- He has an established property investment company.
- **He decides to freeze his shares at an acceptable value of £1 million**.
- The company grant growth shares to his two children.
- **10 years later Tom sadly dies at which point the company is valued at £3 million**.
- **Carrying out this planning has saved his estate at least £800,000 in inheritance tax**.

TIP... If this is of interest to you please do not hesitate to contact us, as we can call upon specialists to look at the feasibility and the implementation of going down the freezer/growth shares route.

The Corporate Prodigal Son Bites

For accounting periods straddling 31st March 2023 and those thereafter, companies will see the return of the corporate prodigal son, last seen back in 2015, which could result in old favourites such as varied corporation tax (CT) rates, thresholds and the infamous complexed associated company rules returning to inflict heightened CT pain.

For the past 6 years the majority of companies have paid CT at a fixed 19% on their taxable profits (TP). From 1st April 2023, it will depend upon the size of your total taxable profits to see what CT rate will apply as CT threshold limits have been set.

► If TP are no more than the £50K threshold it will all be taxed at 19%.

► If TP exceed the £250K threshold it will all be taxed at 25%.

► If TP fall between £50K and £250K it will be taxed again at 25% but would also attract what is called marginal relief which would reduce the liability.

For example:

► Vale Park Ltd TP for the year ending 31st March 2024 is £150,000 thereby falling between the £50K and £250K thresholds.

► **After taking account of marginal relief the CT liability is £36,000.**

► **Pre-1st April 2023 it would have been £28,500.**

However, if a company is caught by the associated company rules, the CT liability could be worse. In basic terms, if you, or you in conjunction with others, are deemed to be in control of more than one company then each of those businesses could be affected.

Depending on the number of associated companies there are, one has to divide the £50K and £250K lower and upper threshold limits by that number before working out that particular company's CT liability.

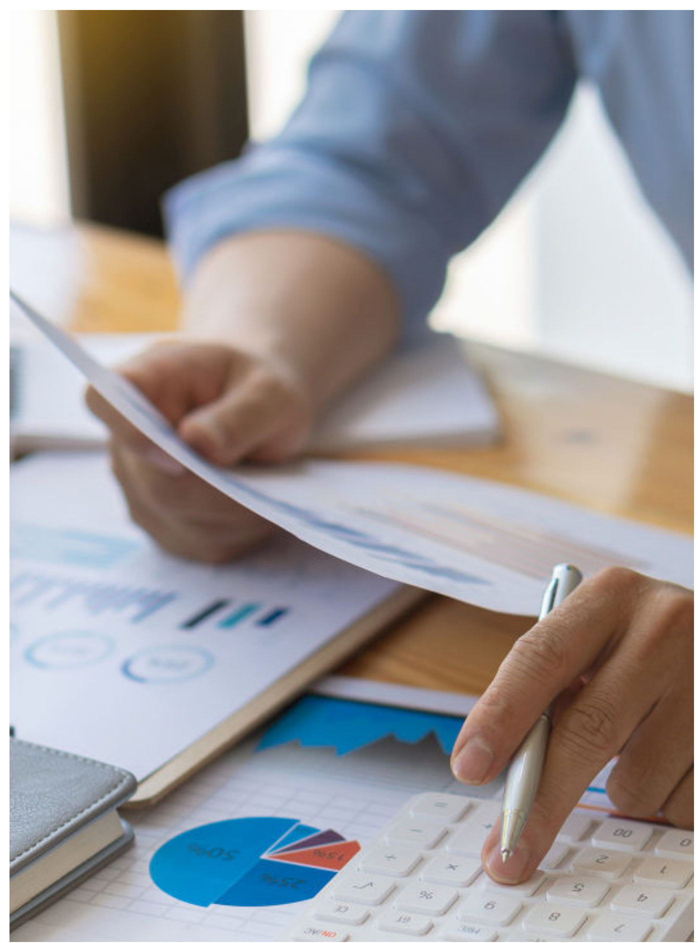
For example:

► Mr and Mrs Pope own 100% of Pope Ltd which in turn owns 100% of Massey Ltd which also own 90% of Wozza Ltd.

► There are 3 associated companies as they are all under the control of Mr & Mrs Pope.

► The lower CT threshold will therefore be £50,000/3 = £16,667

► The upper CT threshold would be £250,000/3 = £83,333



► Pope Ltd profits for the year ending 31st March 2024 are £40,000.

► **Pope Ltd CT liability is £9,350. If it had no associated companies it would have been £7,600**.

Many factors can influence whether or not companies are going to be drawn into the associated companies net for CT purposes such as the substantial commercial interdependence rules, the minimum controlling combination test or it being a non-trading or dormant company. **Planning could possibly be looked at to mitigate the CT position such as the feasibility of shortening or lengthening the accounting date or even merging companies if it is commercially acceptable to do so**. All of that will, of course, be dependent upon such things as:

► The size of the TP and the flow of those profits.

► When did the respective companies become or cease to be associated.

TIP... If you own a company and are worried about how the changes in the corporation tax system might impact upon your business from 1st April 2023, please contact us and we can carry out a review for you.

Why not help a dear relative

▶ **Subject to the child's age or education status, as a parent, you can claim Child Benefit.**

▶ By making the claim, if you are not working or your earned income for the tax year is not above a certain limit (2023/24 £6,396), it counts as one year's worth of national insurance (NI) contributions towards your state pension.

▶ **To be entitled to receive the full state pension you must be deemed to have made 35 years of NI contributions.**

However if you are already earning, for example, £6,396 or more, that in itself counts as one year towards the target. You cannot then include the Child Benefit NI credit too.

But is the Child Benefit NI credit lost for good? Not necessarily.

If you have a child, under the age of 12, being looked after by a UK resident relative whilst you are working, you can choose to transfer your Child Benefit NI credit to them.

▶ **The relative would need to make a Specified Adult Childcare Credit (SACC) application using form CA9176.**

▶ As the parent you need to countersign that application.

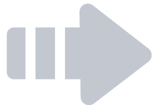
▶ If the relative is not working or their earned income for that tax year is below the threshold this would then count as a relevant year for state pension purposes for them. Helping them towards the 35 year target.

▶ **For every year claimed under SACC, that relative's state pension could increase by £302 per annum (based upon 2023/24 state pension figures)**.

The term 'relative' is significantly wide but, for example, it could be a grandparent of non-pensionable age or a brother or sister, or their spouses.

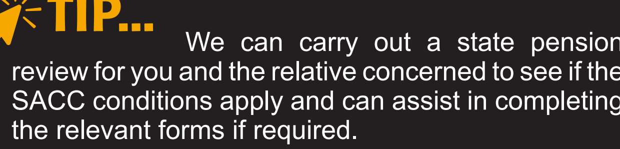
▶ **If the qualifying conditions are met throughout, the relative can make a SACC application from as far back as the 2011/12 tax year right through to the 2021/22 tax year inclusive in one claim. You need to wait until October 2023 to claim for the 2022/23 tax year.**

▶ **The charity, AGE UK looked at grandparents over the age of 50. Their research suggests that 20% of them (approximately 5 million) provide regular care for their grandchildren.**



▶ The parent does not need to be actually receiving the Child Benefit, they simply have to register for it to enable the relative to make the application.

▶ Potentially a significant number of people could be missing out on additional state pension they are entitled to.



TIP... We can carry out a state pension review for you and the relative concerned to see if the SACC conditions apply and can assist in completing the relevant forms if required.

Incentivisation is the key option

For many employers there are key employees who they don't want to lose. They are integral to the growth and success of the business. It is important to keep these employees tight to the trading company.

One option is to go down the Government approved Enterprise Management Incentive Scheme (EMI) route, which enables the employer to incentivise those key employees by granting them the option to acquire shares in the company, at a later date, for a price set at the time of the grant. Protection can be put in place as the employer can put restrictions on the share options which might be linked to performance or if the employee leaves or voting rights.

The employee is incentivised to help grow the value within the business as they could benefit from:

a) **An increase in the value of their own shares from the date the share options were granted**.

b) **Significant tax breaks along the way and at the time when the shares are subsequently sold**.

The tax breaks for the employee could be:

► **No tax and national insurance liability on the value of the shares at the time the option was granted nor when the employee decides to exercise their right to acquire the shares.**

► **Upon selling the shares, assuming the share options were held for at least 2 years or more, the capital gains tax rate applicable to the gain may only be 10% as opposed to possibly as high as 20%**.

For example:

► Jamie's employer grants him the option to acquire 5000 shares in the company pre the sale of the company 5 years further down the line.

► The grant option price is £7 per share, which is the true market value as at that date. There are no tax consequences for Jamie at this point in time.

► 5 years later, just prior to the sale of the company, Jamie exercises the right to buy the shares. The market value at that date is £50 per share. Jamie pays only the grant price of £35,000 as opposed to the market value price at the date of exercise of £250,000. Again there are no tax consequences for Jamie.

► The company could also obtain a corporation tax deduction of £215,000, the difference between the grant and exercise price.

► Jamie sells those shares for £250,000 3 days later. His capital gain would be £215,000. After taking account of the capital gains tax annual exemption for that year, he might only pay capital gains tax at 10% as opposed to 20%.

The company and the key employee have to qualify to be able to offer an EMI. The conditions are:

a) **It has to be an independent trading company**. Certain trades such as farming, property development, legal and accountancy services, hotels and care homes, for example, are excluded.

b) **The gross assets of the company must not exceed £30 million at the time of the grant**.

c) **The company must have fewer than 250 full-time equivalent employees**.

d) The share options themselves must be over ordinary shares that are fully paid and are not redeemable.

e) The maximum value of share options an employee can hold is £250,000.

f) The total share option value for the company must not exceed £3 million.

g) **The options must be capable of being exercised within 10 years of the grant**.

h) **The employee must spend 25 hours a week working for the company or, if they fail to meet that criteria, they must devote 75% of their working time to the company**.

i) **Employees who have a material interest of more than 30% of the share capital before the options are granted are excluded from participation**. This takes into account associates such as a spouse, civil partner, parents, grandparents, child or grandchild. However it does not include brothers and sisters.

TIP... EMI is just one of the ways a business can incentivise its employees. If you want to look at what might be the appropriate option for your business please do not hesitate to contact us.

We are here to help

We can help you by ensuring that you're aware of the changes that will affect you, your family and your business. To find out more about the ways that we can help you, do not hesitate to contact us.

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