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Private wealth

A guide for entrepreneurs

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Introduction

Running a business is hard so it's understandable that personal wealth planning often takes a backseat for many entrepreneurs.

You're focused on building up the business and, as it grows, so too does your workload, meaning your own planning inevitably falls down your priority list.

But, while it may be hard to imagine now, there is likely to come a time when you will want to step back or sell and it's important to have the right plans in place so that you and your loved ones can reap the benefits of all your hard work.

It is also sensible to make sure your affairs are in order in the unfortunate event that anything happens to you. Often, people have a business partner or family member who they trust implicitly to manage their affairs should anything happen. But, it is always advisable to put this on a more formal footing and to have a documented plan in place.

Our guide lays out some of the practical considerations for entrepreneurs to help ensure you have the right plans in place for your future.

Laying the foundations

It's never too early to start thinking about your future financial security. However, people rarely do until a significant life event, such as getting married or the birth of a child, or a move to sell or attract investment forces them to put a price on what their business is worth.

There are some core things to consider that, if reviewed and executed properly and professionally, are the foundations of personal wealth planning.

We've put together a short overview on each area to cover what it is and why it is important:

Consider a shareholders' agreement

If you own a private limited company, you'll be familiar with the articles of association. This is a statutory, legally-binding document that sets out how the company will be run, protects key rights and obligations and is something that is registered with Companies House.

Shareholders' agreements regulate relationships between shareholders. These are optional and sometimes considered an unnecessary expense if you're just starting out. But, they are well worth the investment to protect your interests in the future.

Shareholders' agreements typically cover issues such as policies on what the company may or may not do, the issuing, selling and transferring of shares, dividends, the appointment of directors, and which decisions need shareholders' consent.

They can be used to address many eventualities including disagreements between shareholders or what will happen if a partner wants to exit the business in the future.

They are also particularly useful for SMEs, where there are usually fewer shareholders, and those shareholders are often directors. For example, in a company owned equally by three people, two could join forces to oust the other without good reason if there was no shareholder agreement in place.

Importantly, they can interact with a shareholder's own personal estate planning to ensure that shares can be transferred to family members or trusts, or a mechanism is in place to ensure that those beneficiaries receive the value from the shares, if not the shares themselves.

The articles of association offer some security, but adding a shareholders' agreement helps avoid risk. It is also worth noting that it is possible to combine both in a single document.

Plan for business owner inheritance tax reliefs

A will should not only integrate with the approach taken in the shareholders' agreement, but it should maximise the inheritance tax reliefs available to you as a business owner, specifically business relief.

Any business, or share of, must be treated as part of the estate for inheritance tax purposes can get business relief of 50% or 100% on certain business assets such as property and buildings or unlisted shares, provided that the business is trading.

You may also be able to take advantage of business relief on inheritance tax during your lifetime if gifting business property or assets that you have owned for at least two years. The recipient will qualify as long as the assets are kept on as a going concern until your death. Should you survive for more than seven years after the date of the gift, you will no longer be liable for Inheritance tax.

Put in place a lasting power of attorney

A lasting power of attorney allows you to appoint an attorney to act on your behalf should you lose mental capacity. It is typically not something people tend to think about until they are much older.

There are two types – one for health and welfare, and one for property and financial affairs. You can appoint more than one attorney and it is increasingly common for business owners to appoint a colleague or trusted adviser to handle business decisions including exercising your voting rights as a shareholder.

You cannot delegate the role of director to an attorney, but a contingency plan for if you lose capacity should normally be included in the articles of association and/or shareholders' agreement.

A growing concern

Often, business owners are so consumed by the day-to-day that they don't realise the value of what they have. That tends to come when they decide they want to scale up, start to look at the figures more closely and see that their once fledgling business has now grown into a valuable asset.

At this point, there are various options worth considering in order to protect your interests. It is also important to be aware of business asset disposal relief, formerly entrepreneurs' relief, should you decide you want to sell all or part of your business. Put simply, this reduces the rate of capital gains tax you pay.

Pension contributions

Pension planning should be a top priority for entrepreneurs, not only to ensure you have a healthy source of income upon retirement but to take advantage of the available tax relief.

If you're a director of a limited company, you can contribute pre-taxed profits to your pension pot both as an individual and an employer. However, while personal contributions are only tax-free up to certain limits, there's no restriction on the amount that can be put in by the company thus allowing you to make larger contributions.

Employer contributions are also deducted from the company's taxable profit and will reduce the company's corporation tax liability.

Deeds of variation

In the event that you are due to receive an inheritance that you do not need then you can alter how your share is distributed via a deed of variation. There are various reasons why someone might use a deed of variation, one of which is to make the estate more tax-efficient by reducing the amount of inheritance tax and/or capital gains tax payable.

An example of this would be if a person were to employ a deed of variation to pass their inheritance directly onto their children.

Any changes must be made within two years of the deceased's death and only if all the beneficiaries agree. The executor will also need to provide a copy of the deed to HM Revenue and Customs.

Wealth planning through a discretionary trust

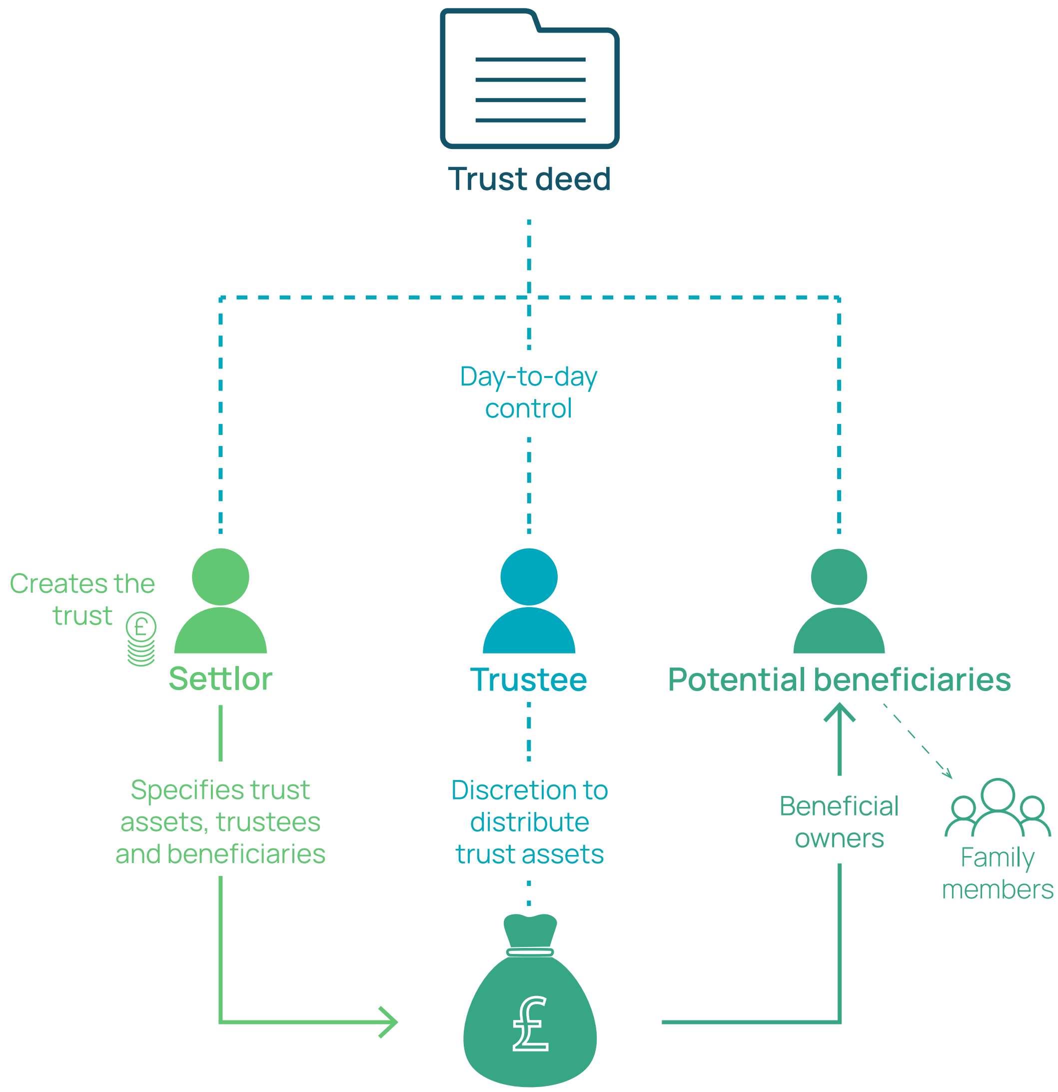
A popular wealth planning tool is to take shares out of your personal ownership and put them into a trust, typically for the benefit of a child/children. This is one of the most common forms of estate planning as it allows you to retain control of shareholder voting rights whilst ringfencing the share value. You can act as trustee alongside others.

The structure of a discretionary trust is popular as it allows for maximising inheritance tax reliefs and is particularly useful as an estate planning tool prior to a business sale.

As the beneficiaries of trusts are not entitled to the trust assets, this can safeguard against situations such as where beneficiaries are not yet responsible enough to manage the money themselves or where relationships deteriorate.

Unlike a will, which becomes a matter of public record, discretionary trusts can also be a way of keeping private the details of how your estate is divided upon your death.

How a discretionary trust works



Managing assets abroad

It is increasingly common for people to have international assets, for example, if they have invested in property abroad. Different jurisdictions are governed by different rules and it is important to have the correct legal documentation.

For some countries, that simply means having your will translated and notarised in a format that the foreign courts will understand and electing for English law to apply when the will is executed. This is not always essential but likely to make things more straightforward and avoid adding to the already lengthy probate delays.

Other jurisdictions may be more complex as they do not have the same testamentary freedom as England and Wales where, generally speaking, you can leave your assets to whomever you like.

For example, French law stipulates that you must leave some of your assets to your child/children if you have them. It is, however, now possible to impose English law when dealing with French property.

Sharia law also dictates who the beneficiaries of at least two-thirds of a deceased person's estate must be, but there is a process that non-Muslim persons can go through in order that they are not required to comply.

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Review regularly

As a general rule, we advise clients to revisit and review their plans every five to ten years or earlier if there is a significant life event or change. That could be rapid business growth, the unexpected exit of a director, or if you decide to sell. In terms of the latter, we would advise involving a lawyer at least six months in advance in case any restructuring is needed.

Personal wealth planning should be front of mind throughout the lifecycle of any business and if it's something you haven't yet considered, it's never too late – or too early – to start. Laying solid foundations now will ensure that you and your loved ones have peace of mind and financial security in the future. You can't put a price on that.

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