Keeping it in the Family – Focus on Asian families preserving family wealth for future generations

Advantages for families from India and Pakistan

Hard working individuals who are happy to pay tax during their lifetime are often surprised that up to 40% of their wealth will be taxed when passed to the next generation on their death. However, due to the unusual concept of domicile, individuals originally from India or Pakistan may have the opportunity to significantly mitigate inheritance tax on their death. Both India and Pakistan have highly beneficial inheritance tax treaties with the UK which enable advantageous planning. Furthermore, this planning can be effective even in relation to long-term UK residents. Whilst many individuals may have a simple will in place, it takes specialist advice to create a proper estate plan to mitigate tax on death.

Keeping control

A lot of Asian families have invested heavily in property in the UK, both residential and commercial. Mitigating inheritance tax on death can be difficult with this asset class, but there are lifetime planning opportunities to explore. Often, and quite understandably, older family members want to mitigate inheritance tax but do not want to lose control of their assets. However, there are tax efficient ways of co-owning a property portfolio in order to mitigate inheritance tax on death, whilst ensuring family members who created the wealth keep control, and keep the rent generated by these properties. This means the majority of the value of the assets can be passed to the next generation, without the older family members losing the benefit of the revenue from the assets, and without risking the properties being sold without their consent. This planning requires specialist legal advice to put in place.

A family investment company (FIC) is another vehicle which enables older family members to retain control over assets whilst accumulating wealth in a tax efficient manner and facilitating future succession planning. The current rate of corporation tax is 19%, which compares favourably to personal tax rates (of up to 45%) which would apply to investments held by family members personally. In this year's Budget, the Government announced that from April 2023 the rate will go up from 19% to 25% for companies with profits of over £250,000. Companies with 'small profits' of £50,000 or less will continue to pay tax at 19%, whilst companies between these two thresholds will be subject to a tapered relief resulting in a proportionate rate of tax. "Close investment holding companies" will not be entitled to the small profits rate, which is likely to include most FICs, unless they are trading or letting property commercially (amongst other exceptions). It is important to note that dividends are in most cases exempt from corporation tax, which means that the impact of the increased corporation tax rate on FICs may be relatively limited.

Despite the tax increase coming in 2023, we consider that these companies remain a very efficient estate planning tool; families from India or Pakistan will still have the ability to keep the value of a family investment company outside the scope of inheritance tax.

Succession planning for Family Businesses

We represent family owned businesses and understand that it can be difficult to discuss and put in place plans for how the business is to pass onto the next generation. However, such conversations and planning are essential if the business is to continue to thrive and grow, rather than suffer on the death of a founding/principle member. We also prevent such families falling into unexpected tax pitfalls when they are considering selling their businesses; advising on how to mitigate tax on both the corporate and personal level.

Protecting Assets from Divorce

Another way family wealth can easily be dissipated is through divorce, unfortunately an increasingly common occurrence in all cultures. We regularly prepare pre-nuptial (pre wedding), and post-nuptial (during the marriage) agreements, to protect inherited and other assets. For Asian families, often the wedding itself can be a significant financial outlay in terms of both wedding costs and gifts to family members, so it makes sense for financial arrangements to be agreed upfront. Pre-nuptial and post-nuptial agreements (which are increasingly upheld by courts, although not yet governed under legislation) are an essential form of financial planning and asset protection. Such agreements are particularly vital for those who own or co-own businesses. Where the business is the most significant asset, without the existence of an agreement, the Family Court can force a sale of the business to fund divorce settlements. This can cause significant disruption to the business, let alone the personal distress of seeing the value of the business leave the family.

At Winckworth Sherwood we take a holistic approach to advising families on both their personal and business interests. Please contact Dhana Sabanathan of our International Private Client Team or Katie Spooner of our Family Team with any queries relating to this article.

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