

Guard Your Business Property Relief!

One of the most valuable reliefs available to company owners for Inheritance Tax (IHT) is Business Property Relief (BPR). This allows the owners of business assets to transfer them to family members without incurring an IHT charge. The relief is given by reducing the value, for IHT purposes, of the assets transferred.

In a family company context, BPR is given at 100 per cent for shares in unquoted companies and at 50 per cent for assets which are used in the business controlled by the transferor. There are various requirements that must be satisfied in order to qualify for BPR but the main one is that the assets must have been owned by the transferor for the two years prior to the transfer. If the transferor (or transferee) dies within seven years of the transfer, the business property or 'replacement property' must still be owned by the transferee at that date. Replacement property is property which would qualify as business property, but where the original property has been sold and its proceeds reinvested within three years. There are other ways replacement property can arise, such as on share-for-share exchanges.

There is a common pitfall which can affect BPR where replacement property is bought out of the sale proceeds of the original property which qualified for BPR. When the property which is transferred is replaced, but the whole of the proceeds of the original property (net of expenses) are not reinvested in the replacement property, the relief is completely lost. So, if property is sold for £400,000, with £30,000 of expenses, the replacement property bought must cost at least £370,000, otherwise the BPR available on the whole of the £400,000 will be lost. This could increase an IHT bill by £160,000.

Another common problem results when borrowing is undertaken using the company assets as security. In this case, the BPR is limited to the value of the asset or assets net of the borrowing. If, on the other hand, the borrowing is secured on an asset that is outside the company (say a house), then the BPR will be available on the gross amount.

For example, if a business asset, such as a property, is valued at £500,000 and a loan of £200,000 has been advanced to the business, the BPR available if the property is subsequently transferred is alternatively:

1. £300,000 (£500,000 - £200,000) if the loan is secured on the property transferred; or
2. £500,000 if the loan is secured on an asset outside the business (such as the house of the director).

Care must be taken when structuring transfers and it is advisable to seek professional advice well in advance. The laws governing IHT on business assets are complex and there are interactions with other taxes, particularly Capital Gains Tax, to consider. We shall be pleased to advise you on all corporate planning and IHT planning.