

## Winning the Generation Game

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With around 70% of all family businesses failing in the initial transition from generation 1 to generation 2, the earlier they embark on succession planning the greater the chance the business will win the generation game.

One of the biggest challenges faced by family businesses is finding the right balance between effective estate planning for the older generation, and the transition of control through the family. Let's take a scenario with which many readers may be familiar:

Parents have set up a successful business.

They have two children, both of whom are actively involved in the business but still fairly junior. All agree the intention is for the business to pass down at the appropriate time. Mum and Dad have asked for advice as to how to best plan for the future.

The primary concern for the parents is to minimise their exposure to inheritance tax, whilst ensuring asset protection. The most common solution would be to transfer their shares in the company to a trust.

By placing the shares in trust, the value of the business would be taken outside their estate, and the trust would typically hold the shares until the children were considered "ready" to receive them, or for the longer term, to provide for subsequent generations. While the way in which trusts are now taxed can be a barrier, trusts offer enormous flexibility and asset protection and can still play a key role, particularly if the family business is a trading company qualifying for inheritance tax relief.

However, trusts are not the solution to every scenario. An alternative option which may better meet the family's objectives is for the parents to restructure the business by creating different classes of share. Those shares can



then be issued to the various family members in a manner which is tailored to suit the family's requirements. For example:

The parents want to retain day to day control of the business for the foreseeable future, and they could achieve this by creating a new class of voting share which is held only by them. Mum and Dad's Wills could be drafted to deal with the passing of those voting shares and control of the company in the most appropriate way.

The income requirements of the parents and the children differ significantly. The company could create four separate classes of income shares, allowing the company (controlled by the parents) to declare dividends independently to each family member as and when required.

## Planning pointers

To minimise their inheritance tax exposure, the parents could create two different classes of capital share, to which the underlying value of the business attaches. One class would be held by them, with the value of those shares being capped (perhaps at the available nil rate band of £325,000 each), with the other class being held by the children who would share any value over and above this threshold (ie the 'growth' value of the business).

The family could build in provisions surrounding the future ownership of shares to ensure the business remains in the family going forward. If they want to restrict shares being transferred to non family members, and the parents may want to go a step further and exclude spouses from this definition to protect in the event of a divorce.

Each family member would prepare a Will setting out how they want to pass their shares on death, taking into account their own circumstances and the long term aims for the business. This structure could be achieved through bespoke articles of association, or if sensitive drafted into a shareholder agreement which would remain off the public register.

Larger families may also want to couple bespoke articles with a family charter, setting out a framework for communication between those family members who are involved in the business on a day to day basis, and those who are not.

Family charters are relatively rare, but can be invaluable in helping families manage the difficult balance between the demands of business and the politics of everyday family life. They can also create a useful forum to develop the next generation and manage their expectations to future entitlements.

## How we can help

If you would like any more information, please contact [Victoria Symons](#) or [Kate Arnold](#).



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