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Rt Hon George Osborne MP
Chancellor of the Exchequer
HM Treasury
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Dear Chancellor

Family businesses in the UK employ over 9.4 million people and generate over a quarter of UK GDP. Family businesses outnumber others by about two to one – comprising around 3 million businesses – turning over around £1.1 trillion.

Our latest research shows that family firms operate across all industry sectors and regions of the UK. Whilst many are small firms, there are over 15,000 medium and large family firms operating in the UK – many household names and global brands.

The family business sector is the backbone of our economy, and the bedrock of our communities. By their very nature family businesses take a long-term view, built on long-term stewardship of people and resources. Family firms also act as incubators for entrepreneurship and future growth.

Family business is a great British success story, and these businesses are ambitious and eager to build on their success. Their prudent business model saw family firms weather the recession better than other businesses. The recommendations in this submission are designed to support family firms in boosting investment and productivity, to grow their businesses, create jobs, and facilitate transfer of successful businesses between generations.

In this last Budget before the General Election we also hope to see that the unique characteristics of the family business sector are understood, and that their hard work and commitment to sustainable business practices is recognised by Government. We welcome the trajectory of lower Corporation Tax established over this Parliamentary term, and support efforts to secure the balanced growth that the economy needs.

Recommendation: Ensure pension deficit calculations are appropriate to family firms

Why it matters: The calculation of deficits for defined benefit pension schemes at present relies heavily on the use of interest rates linked to Corporate Bond yields. A function of this formulaic calculation is that even where family businesses are confident that they are able to meet the requirements of their scheme, the exceptionally low bond yields at present mean much larger pension deficits being forecast than are necessarily accurate.

As a result, family firms are forced into finding funds to 'plug' the calculated deficit, significantly reducing the funds available to invest in growth. This applies a considerable constraint on the ability of family firms to invest in increasing productivity, creating employment and moving into export. All this is sacrificed, whilst at the same time the system provides no practical benefit to the members of the pension schemes themselves. This particularly impacts on family firms which do not usually have the same access to capital markets as other ownership models. The Government, pension regulators and accounting bodies must work together to urgently address this issue.

Recommendation: Increase the finance options available to family firms to help them grow

Why it matters: The long term outlook of family firms is reflected in the needs they have when accessing finance to invest in their business. Family businesses need increased competition in the finance market with more options which are aligned to their long term outlook and don't necessitate sharing equity. The Breedon Taskforce estimated that a UK private placement market could be worth £15bn. At present, whilst UK issuers account for nearly 21% of the global private placement market, because the UK market is underdeveloped UK businesses look to the US for this type of financing.[1]

The IFB is working with industry bodies to support growth and awareness of the options available through Private Placement Markets and investment from insurance and pension lenders; however more support is needed from Government to increase awareness of these alternatives to bank financing and to develop the UK investor base for private placements.

Recommendation: Unlock more investment in start ups by removing the Connected Persons' Test for EIS

Why it matters: A fundamental check on the growth UK businesses is the availability of finance for investment in growth. While the EIS has proved highly successful with business angels, the Connected Persons' Test results in an active disincentive for otherwise non-connected family members to invest in start-ups with a family association. Family businesses are excellent incubators of the entrepreneurial talent – with an estimated that 13 per cent of family businesses starting as spin-offs from an existing family firm[2].

In our view, investment by a family business owner in another family enterprise should attract the same relief as an investment by a family business owner in an enterprise outside the family. Such a tax simplification measure would be a further boost to innovation and enterprise. HM Treasury should consider lifting the Connected Persons' Test for a temporary period in order to encourage increased investment in new businesses.

Recommendation: Support investment in the growth of mid-sized businesses

Why it matters: There are over 14,000 mid-sized family businesses, almost half of all mid-sized businesses in the UK. The government should also extend the EIS thresholds to support investment in the growth of mid-sized businesses, taking the threshold to 500 employees (the same used for the small firms R&D tax credit) and increasing the investment limit. This will help firms grow further, and move from being mid-sized business to world-leading large firms.

Recommendation: Support sustainable business financing by equalising the tax treatment of debt and equity financing

Why it matters: Their long term focus means family businesses are prepared to sacrifice short-term gains to longer-term goals. As part of this, family firms plough profits back into their businesses rather than loading themselves with debt. The current tax system favours debt over equity financing. At a time when further growth is needed in the economy it is important to examine how growth finance is treated by the tax system. We recommend resolving this issue, and making progress in rebalancing the economy, by introducing the same tax treatment for equity financing as debt financing. This will allow businesses to make their investment decisions for commercial reasons and not tax advantage. It would also have the benefit of simplifying the tax code and the overall regulatory burden on business.

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[1] Breedon Taskforce Report, March 2012: https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/32230/12-668-boosting-finance-options-for-business.pdf

[2] Global Entrepreneurship Monitor, Family Business Specialist Summary, 2006

Recommendation: Promote long term investment by extending the Capital Allowances limit

Why it matters: The IFB welcomed the measures to temporarily increase capital allowances from £25,000 to £250,000 for two years, and then up to £500,000 until the end of 2015. As SMEs aim to grow and increase employment, this measure should be extended beyond this initial trial period. Whilst UK productivity has picked up in recent months, it is still below 2008 levels. The temporary increase in capital allowances should be extended to further encourage those businesses which are able to invest to do so and help to further improve productivity.

The cap of £250,000 was too restrictive for those firms that want to make a major investment in their UK operations. Family Businesses make up fifty eight per cent (58%) of UK private sector manufacturing firms and our members tell us that the cap of £250,000 was too low to have the desired effect of increasing incentives to. To create a meaningful incentive for medium and large enterprises the government should seek to maintain the increased cap beyond the end of 2015 to promote increased productivity and UK competitiveness.

Recommendation: Support smooth transition of successful businesses between generations

Why it matters: Without Business Property Relief each time a business passed from one generation to the next the tax implications would be so large that a sale, liquidation or indebting the company would be required. This would distort the market by imposing a tax penalty on the transfer of family firms which is not paid by other businesses on transfer.

Ultimately without BPR the death of a major shareholder could lead to the end of an otherwise profitable business. BPR has a clear objective and purpose – it facilitates the continuity of family business management and ownership between successive generations, allowing businesses to develop a long term approach which focuses on stability and sustainability. Maintaining BPR is essential to allow businesses to develop long term plans which focus on stability and sustainability.

HM Treasury should also consult on introducing a single qualifying test to apply equally for Business Asset Holdover Relief and BPR, to reduce bureaucracy and help ensure smoother succession planning for family businesses.

Recommendation: Support family firms in investing in training staff by introducing an HR tax credit

Why it matters: Family firms have a strong record of investing in their staff and communities. Investment in training of staff, particularly young people in the early stages of their careers, generates positive externalities – the long term returns accruing to the wider economy exceed the returns to the investing firm alone. Therefore without additional incentives, the levels of training and hiring of younger or inexperienced staff will continue to be below what is optimal for the UK economy.

In the same way Research and Development is recognised for the wider economic benefits it brings, the IFB would recommend the government introduces a People Capital investment tax credit focused on giving employment tax relief to firms who invest in the training and development of their employees through apprenticeships schemes.

We would welcome the opportunity to meet and discuss these issues in more detail. If you need any further information on the recommendations outlined above, please do not hesitate to contact us.

Yours sincerely,

Peter Armitage
Chairman