

Department for Business, Energy and Industrial Strategy Consultation

Building Our Industrial Strategy

Institute for Family Business Response

1. Executive Summary

- 1.1 Family businesses need an industrial strategy which reflects their own long term outlook, and takes a genuinely long term view.
- 1.2 Encourage firms to take a more rounded view of success and what it means to be a responsible business.
- 1.3 Address supply and demand side barriers to alternatives to bank lending, and equalise the tax treatment of debt and equity funding.
- 1.4 Lift the Enterprise Investment Scheme Connected Persons' Test to boost innovation and enterprise investment. Support long term growth in business by maintaining Business Property Relief (BPR) in full.
- 1.5 Support family businesses in achieving their ambition to export by providing more tailored advice and assistance making in-country contacts.
- 1.6 Ensure family businesses are represented on local groups and institutions, to support the development of initiatives which will deliver genuine long term growth.

2. About Family Business

- 2.1 The Institute for Family Business (IFB) is a not for profit organisation, supporting and promoting the UK family-owned business sector through events, networking, representation, thought leadership and analysis.
- 2.2 We work closely with family firms to support them in growing enterprises for generations to come. A central part of our work is to provide educational resources and events designed to support business owners and those who work in family business. We champion best practice within the family business community and help others to learn from these examples.
- 2.3 Family business is the backbone of our economy, and the bedrock of our communities. In the UK, family firms generate a quarter of GDP and employ over twelve million people. By their very nature, family businesses take a long term view, build on long-term stewardship of people and resources. Their commitment to passing something on to the next generation is locked into their corporate DNA.
- 2.4 The family business sector is extremely diverse. Family businesses come in all sizes, are found in all industries and across the whole country. Whilst the majority of family firms are small or micro

businesses, there are over 17,000 medium and large firms. Family businesses are found in all parts of the UK. There are almost half a million family firms in the East of England, over one hundred thousand in Northern Ireland, and over three hundred thousand in Yorkshire.

2.5 Whilst family businesses generate a quarter of UK GDP¹, they recognise that success in business is about more than short term financial results. Success is about sustainable value creation. Family businesses perform better than non-family firms in non-financial metrics such as investing in their employees and in supporting communities.² And the best-run family businesses outlast others by a factor of two.³

3. Family Business and the Industrial Strategy

3.1 Family business is the backbone of our economy, and the bedrock of our communities. Family businesses want an industrial strategy which takes a genuine long term view, reflects the needs of UK private business and recognises what makes these businesses different.

3.2 Family business is a great British success story, and these businesses are ambitious and eager to build on their success. By their very nature, family businesses take a long-term view, built on long-term stewardship of people and resources. Their commitment to passing something on to the next generation is locked into their corporate DNA. Family firms also act as incubators for entrepreneurship and future growth - promoting innovation and entrepreneurship.

3.3 Too often the perception of 'successful business' is weighted towards entrepreneurs building businesses through rapid and unsustainable growth, and then selling or floating that business. This is a very narrow view of what business success looks like, and because of that the incredible work of family businesses is often overlooked. It is essential that when formulating the Industrial Strategy the Government re-evaluates what success in business looks like, and that they champion those family businesses which are rooted in their communities, innovating, investing and creating employment for generation after generation.

3.4 The new industrial strategy must support and boost the wider positive role of business as part of a vibrant and successful UK. The strategy should not pick winners measured solely on economic measures, but focus on encouraging firms to take a more rounded view of success, long term value creation and what it means to be a responsible business. This includes investing in people, taking a long term outlook, and considering the social footprint of your business (including environmental and community engagement).

A Long Term Approach

3.5 Whilst there are many family firms that have been operating for hundreds of years, and their longevity and enduring success are testament to their innovative and long term outlook, the Industrial Strategy

¹ Oxford Economics and IFB Research Foundation (2016) *The State of the Nation: The UK Family Business Sector 2015/16*

² M Institute and IFB Research Foundation (2012) *Sustainable Value Creation*

³ Miller, D and Le Breton-Miller, I. (2005) *Managing for the Long Run: Lessons in Competitive Advantage From Great Family Businesses*

should create an environment which supports more ambitious family firms to continue thrive and grow over multiple generations. Successful family firms survive and thrive by taking a long term and sustainable outlook, whilst adapting and innovating to stay relevant to the modern world. Family firms turnover £1.3 trillion in the UK each year. Growth in the sector brings benefits to the whole UK economy, consumer, the exchequer and the millions who work for family firms.

3.6 Sustainability, custodianship and long termism are core values which unite family businesses. This long term outlook gives family firms the opportunity to invest in training their employees, and to innovate and develop new products, processes and services. Continuity within the businesses support innovation, investment and increased productivity.

3.7 Family businesses need an industrial strategy which reflects their own long term outlook, and takes a genuinely long term view. A strategy which is looking ten to twenty years ahead and creating long term value, not just focusing on short term outcomes.

4. Supporting Businesses to Start and Grow

Financing Growth

4.1 The long term outlook of family firms influences their needs when accessing finance to invest in their businesses. A fundamental check on the growth of UK businesses is the availability of finance for investment in growth. In this section we set out measures which the Government should consider to help support family firms to invest in long term growth.

4.2 The long term focus of family business means they are often prepared to sacrifice short-term gains to achieve their longer-term goals. As part of this, family firms reinvest profits back into their businesses rather than loading themselves with debt. **Equity funding supports and encourages decision making that enhances the long term competitiveness of business.** This long term outlook means family firms are able to make large investment in new product lines, factories or in transforming underperforming companies - benefitting the wider economy through investment in productivity and employment.

4.3 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.

4.4 Those family firms looking for external finance need increased competition in the finance market, with **more options aligned to their long term outlook that don't necessitate sharing equity.** In our recent survey around three quarters of family firms agreed that "Government should encourage greater competition and choice in business financing", with over half saying that "a lack of non-bank lending in the UK acts as a barrier to growth".

- 4.5 Whilst private placement, insurance and pension lending are all financing options which support the long term requirements of family firms, there is still not widespread awareness of these options. The UK private placement market has a great deal of potential but is still underdeveloped.
- 4.6 It is positive to see Government looking to address supply and demand side barriers to broaden the types of finance on offer, and increase the number of alternatives to bank lending. We support the development of initiatives in this area and would welcome the opportunity to work with Government and others to progress this work.
- 4.7 As well as being drivers of long term growth, family businesses are excellent incubators of entrepreneurial talent – with an estimated 13 per cent of family businesses starting as spin-offs from an existing family firm⁴. While the Enterprise Investment Scheme 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.
- 4.8 To stimulate further business investment the **Government should lift the Connected Persons’ Test, this tax simplification measure would be a further boost to innovation and enterprise.**
- 4.9 Some 85,000⁵ family SMEs transfer ownership of their business to a new generation each year. Around 64% of family SMEs are estimated to be first generation businesses⁶. In order to ensure that these businesses can focus on scaling up their businesses, the Government must maintain Business Property Relief (BPR) in full.
- 4.10 **Business Property Relief (BPR) is a crucial relief from inheritance tax (IHT) that facilitates the transfer of family management and ownership of the businesses between generations;** allowing a long term approach which focuses on growth, stability and sustainability.
- 4.11 BPR allows businesses to plan for the future, without having to fear a ruinous IHT bill in the event of the unexpected death of a shareholder. Despite best intentions for planning and preparation, death is often unexpected and sudden. BPR provides a safety net for the owners and employees of family businesses, and the knowledge that they will not be unfairly penalised for an unexpected death.
- 4.12 BPR is a positive example of how tax reliefs can support business growth. The introduction, and maintenance, of BPR gave business owners the confidence to focus their efforts on building their businesses and competing globally, rather than looking inwards and impeding growth to prevent risking the future of the business after their death. The introduction of BPR took away the disincentive for families to grow their businesses, and subsequently continues to benefit the UK economy as a whole. **BPR is an economically efficient relief, by supporting long term growth in businesses which go on to create employment and make a significant contribution to the UK exchequer.**

⁴ Global Entrepreneurship Monitor, Family Business Specialist Summary, 2006

⁵ Department for Business, Innovation and Skills, 2014 Small Business Survey

⁶ Praxity, 2015

Sustainable Business Investment

- 4.13 Family businesses have a long history of acting as responsible employers, and this includes their provision of pensions to their employees. Many firms now have significant pension scheme obligations, and family business owners are committed to ensuring that their business is able to meet these sustainably whilst also investing in growth for the future. 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. This has been exacerbated in the wake of the EU referendum result as bond yields have further declined, and is likely to extend the timeframe needed for deficit recovery.
- 4.14 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.
- 4.15 We welcome the release of a Green Paper on the sustainability of funding for defined benefit pension schemes, and encourage the Government to address these issues to ensure the long term sustainability and growth of family businesses.

Support for Scale-Ups

- 4.16 The Green Paper lays out some ways in which the Government is seeking to support scale-up companies and entrepreneurs. The Government is right to identify the role of peer-to-peer networks in sharing experiences and support for those looking to grow their business.
- 4.17 The Institute for Family Business provides a safe and trusted space for those who own and manage family firms to come together to share experiences and learn from leading experts. We support family businesses to address common challenges, such as planning for succession, but also to hear how other families have embedded innovation into their business, or how others have moved into export for the first time. We would welcome the opportunity to work with the Government and other partners to provide support for more family businesses who are looking to grow, through both peer-to-peer learning and tailored advice.
- 4.18 To ensure that successful businesses can continue to grow over the long term, it is important for the new review into entrepreneurship to also consider the support available to businesses as the next generation become involved and the founder starts to plan succession within the business. Growth should not be viewed as something which relies on the founding entrepreneur, but something which policy should support through innovation and investment for generation after generation.

5. Encouraging Trade and Inward Investment

- 5.1 Whilst there is a desire in many family firms to move into export, they report to us that they face barriers to doing so. Family businesses reported to us that the two greatest barriers to them exporting more were a lack of market knowledge and lack of local partners. They identified help in making more in-country contacts and more information as the most useful assistance that the Government could provide to support them.
- 5.2 Family businesses understand the opportunities that export offers, but a personal connection to the business can lead to a cautiousness in growing their business internationally. Their commitment to quality, their sustainable business practices and their strong family values do put family businesses at a real advantage when they do start to export.
- 5.3 Given that the majority of family SMEs do not export at all, it is clear more needs to be done to support smaller family firms in taking this step for the first time. We would welcome the opportunity to work with the Government to develop export guidance tailored to address the questions and concerns of family firms.
- 5.4 We would also welcome the opportunity to work with Government to explore opportunities to improve the support available to family businesses in making in country contacts, including ways in which UK and non-UK family businesses can find each other to build a working relationship.

6. Creating the Right Institutions to Bring Together Sectors and Places

- 6.1 Ensuring the right institutions and forums exist is an important part of creating a successful Industrial Strategy. Whilst family business leaders are often found as active members of industry bodies, school boards and charities, we believe more could be done to ensure family businesses are represented on local groups and institutions.
- 6.2 This is an important step in ensuring that these bodies understand the unique characteristics and challenges faced by family firms, and that their work is addressing these and supporting family business growth. Family business owners would also be able to bring a genuine long term perspective, supporting the development of initiatives and support which will deliver genuine long term growth.
- 6.3 This would also facilitate greater sharing of best practice between family and non-family businesses, and champion those family businesses which are rooted in their communities, innovating, investing and creating employment for generation after generation.
- 6.4 Whilst different areas will have different needs, it is essential that the needs of family businesses in all parts of the UK are understood and incorporated into the Industrial Strategy. The Government must also recognise the importance of not adding layers of complexity or bureaucracy to businesses which operate across multiple regions of the UK, especially not if that will stifle a business' ambition to expand its business domestically.

7. Conclusion

- 7.1 Family businesses need an Industrial Strategy which reflects their own long term outlook, and takes a genuinely long term view.
- 7.2 Supporting family business growth benefits the whole of the UK. The strategy must recognise the unique characteristics of family business and ensure tailored support and advice is available to family firms.
- 7.3 The long term outlook of family firms influences their needs when accessing finance to invest in their businesses. Maintaining BPR supports long term growth in businesses which go on to create employment and make a significant contribution to the UK exchequer.
- 7.4 We would welcome the opportunity to work with the Government and other partners to provide support for more family businesses who are looking to grow and export, through both peer-to-peer learning and tailored advice.
- 7.5 More could be done to ensure family businesses are represented on local groups and institutions, which in turn would support the development of initiatives which will deliver genuine long term growth.

For more information contact: Fiona Graham, IFB Communications Director, fiona.graham@ifb.org.uk