Rt Hon Rishi Sunak MP
Chancellor of the Exchequer
HM Treasury
1 Horse Guards Road
London SW1A 2HQ

30 September 2021

Dear Chancellor,

I am writing to you to outline the Institute for Family Business' (IFB) priorities for the upcoming Budget. The IFB is the UK's largest family business organisation, supporting and promoting UK family-owned businesses to help them continue to be successful for generations to come. Family businesses are the backbone of the UK economy, generating a quarter of our GDP, employing more than 14 million people, and contributing £205 billion in tax.

This Budget represents a vital opportunity for the Government to continue to lead the recovery from the coronavirus pandemic, and to build upon the progress that has been made in supporting business through this incredibly difficult economic period. It is vital that there is stability in the tax regime. Short term taxation changes will make little impact on the level of debt incurred during this crisis, but further changes now would be highly damaging to businesses' ability and confidence to rebuild and invest in a way that will deliver sustainable future growth. Instability or additional burdens will have a knock-on effect not only on the owners and managers of UK family businesses, but on all of their stakeholders and their ability to create new jobs.

The priority must be on supporting and incentivising sustainable investment, which will help our economy to grow and create the wealth needed to reduce the long-term debt burden. Outlined below is a summary of our policy recommendations for areas in which we would like to see the Government provide greater support for the family business sector:

- **Prioritise stability** in the tax regime and prioritise long term investment as a means of stimulating economic growth.
- Support confidence, stability and future investment in family businesses by **maintaining Business Property Relief** (BPR) in full.
- Support succession transition planning in businesses by **aligning Holdover Relief (HR) eligibility** with BPR.
- Update the conditions for both Holdover Relief and Business Property Relief to ensure businesses with **Joint Ventures** aren't penalised.
- Support greater **sustainable long-term investment** through targeted incentives and allowances.

- Re-evaluate the ways in which family businesses secure long-term funding through launching a **second Patient Capital Review**.

- Prioritise greater focus and support for **mid-sized firms**.

- Help young people get back into work by **improving the apprenticeship system**: enabling businesses to fund in-house training and develop a coordinated approach across the home nations.

We would welcome the opportunity to meet and discuss the issues raised in this submission in more detail.

Yours sincerely,

Sir James Wates CBE
Chairman
Institute for Family Business

Autumn Budget 2021
Institute for Family Business Submission

Summary

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IFB's Recommendations

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- Update the conditions for both Holdover Relief and Business Property Relief to ensure businesses with Joint Ventures aren't penalised.
- Support greater sustainable long-term investment through targeted incentives and allowances.
- Re-evaluate the ways in which family businesses secure long-term funding through launching a second Patient Capital Review.
- Prioritise greater focus and support for mid-sized firms.
- Help young people get back into work by improving the apprenticeship system: enabling businesses to fund in-house training and develop a coordinated approach across the country.

Introduction

The Budget earlier this year was broadly welcomed by our members for providing the short-term stability and certainty in the wider operating environment for the family business sector. The decisions taken in March, such as the continuation of the Job Retention Scheme, the introduction of the Super Deduction for business investment, and the delay in the planned increase to Corporation Tax, provided much-needed certainty for our members and supported the return to their usual operations in line with the wider lifting of lockdown restrictions.

The months that have followed have seen businesses face further operational disruptions and financial pressures, including issues in logistics and supply chains, increasing shipping and raw material costs, labour shortages, and further changes to exporting and importing linked to Brexit. This has all been while businesses have been dealing with the impact of COVID-19 on their workforces, and the changes to rules around how they can operate.

While the worst of the pandemic is hopefully behind us, businesses can see further difficulties on the near horizon. Ongoing logistics and labour challenges will add to the pressure around the busy Christmas period. For those businesses with Defined Benefit Pension Schemes, there are the ongoing effects of low interest rates and reduced levels of trading during the pandemic to contend with, which will see businesses facing significant increases to their deficit payment plans, at a time when they need to be investing in getting their businesses and employees. This is an area which needs urgent focus from the Government and The Pensions Regulator.

While we appreciate that an economic crisis such as that brought on by the pandemic will inevitably mean difficult economic decisions need to be made, we do not believe that now is the right time to be increasing the tax burden on business. Social care reform remains a pressing political need, but our members were concerned by recently announced increase to National Insurance contributions (NICs) and Dividend Tax and the disproportionate impact that it will have on small and medium-sized businesses at a time when they can least afford it. We therefore call on the Government to exercise caution in introducing any further tax changes, and to instead prioritise investment as a means of achieving future economic growth.

Aside from the announced increase to NICs, Dividend Tax and Corporation Tax, it is vital that there is stability in the tax regime. Short term taxation changes will make little impact on the level of debt incurred during this crisis, but further changes now would be highly damaging to businesses' ability and confidence to rebuild and invest in a way that will deliver sustainable future growth. The priority must be on supporting and incentivising sustainable investment, which will help our economy to grow and create the wealth needed to reduce the long-term debt burden.

This Budget provides a further opportunity for the Government to outline how it will deliver on its agenda to 'build back better'. While it is understandable that the Budgets earlier this year and in March 2020 were focused on the short and medium terms, this Budget is a chance for the Government to set out its long-term vision for the post-pandemic future. Given the importance of this and the wider Levelling Up and sustainability agendas, we look forward to working with government to deliver a more equal and prosperous economic and business environment for all.

The Government must use this Budget to send a clear message of support to those family businesses creating jobs and wealth in the UK. UK family businesses want to continue to create good quality jobs and support vital public services, but this is only possible if they have the confidence to invest and can continue to grow. The Government must ensure this Budget, and its wider policy platform, create an environment that ensures these businesses can thrive.

Our last submission set out our two-part framework for the economic recovery from the pandemic, focusing on short term stabilisation and long-term investment as a means of stimulating growth. Given the changed context from March, our updated framework is as follows:

- **Continued stability in the tax regime** – No conversation can be had about growth without addressing the stability needed for businesses to survive. These are still extremely uncertain times for business, with many still adjusting to the new reality post-lockdown. Having been given the initial stability they needed following March's Budget, it is vital that the Government continues to provide certainty to businesses by providing the wider tax framework which enables them to rebuild and invest, rather than worrying about any additional tax burdens and how this may impact on their wider operations as a business. Instability or additional burdens will have a knock-on effect not only on business owners and managers, but on all their stakeholders and their ability to create new jobs.

- **Stimulate investment to achieve growth** – The Government must also look at how to stimulate investment as a means of achieving future economic growth. In particular, the Government must use all the levers at its disposal to help stimulate capital investment, investment in new jobs and investment in skills. As the UK looks to level up the country and target regional growth, we also need to take a strategic approach to support mid-sized businesses, which play a hugely important role in our country but often seem to be overlooked in policy.

This framework informs our policy recommendations put forward in this submission and sets what we believe to be the necessary landscape in which businesses can bounce back following the pandemic.

Recommendation One: Support confidence, stability, and future investment in family businesses by maintaining Business Property Relief (BPR) in full

Transitions within family firms – whether in the management or ownership of the business – are times of significant opportunity and challenge. Ensuring that these successful businesses can plan and continue to thrive after an ownership transition is important not only for the owners, employees, and communities which rely on those businesses, but the UK economy as a whole.

BPR is a crucial relief from Inheritance Tax that facilitates the transfer of family management and ownership of the businesses between generations; allowing a long-term approach which focuses on stability and sustainability.

Without BPR, each time ownership of a business is passed from one generation to another, an IHT tax liability would be created. To satisfy this liability, the family business would be required to be sold, liquidated, or indebted. This would distort the market by imposing an additional tax penalty on the transfer of family firms which is not paid by other businesses.

BPR means that when inheriting a share of the family business, and successfully continuing the business, the next generation of owners does not face a tax charge which they do not have the liquidity to fund. This policy has been highly successful and other countries have adopted a similar strategy.

Whilst IHT falls under the personal taxation regime, the reality is that the cost of paying the liability would fall on the business, as the individual shareholders will in most cases not have enough assets outside of the business to meet the tax charge. This would have a knock-on effect on employment and investment. BPR has allowed family businesses to compete on a level playing field with businesses in the UK under different kinds of ownership, and foreign businesses (family owned or not) for which IHT is not a concern.

IHT is also exceptional in the tax landscape given that nobody knows when they might die and the tax charge be incurred. Because of this uncertainty, families and businesses will always have to assume that a charge could happen at any time, and plan accordingly. This would mean profitable businesses would have to divert money away from sustainable and productive investment, and instead build up a pot of cash that could be accessed to pay for a bill that could come at any time.

Businesses which were subject to a full or partial sale to meet the IHT charge, and those that paid extraordinary or additional dividends to shareholders to do this, would also face significant double taxation. If a dividend payment were made, this would mean the individual would face a tax charge on the dividend in addition to the 40% IHT charge. This would see even more money – which could be used for investment in growth – taken out of the business to cover the dividend and IHT charges. Where businesses were sold, as a whole or in part, they would also incur a Capital Gains Tax (CGT) charge.

BPR is a positive example of how tax reliefs can support business growth. The introduction and maintenance of BPR has given 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, allowed family businesses to grow and subsequently continues to benefit the UK economy. The impact of a possible future IHT charge on family business confidence and ability to invest would be significant whatever the rate of IHT at the time, and the challenges around the illiquidity of family business owners' estates and assets would remain regardless.

Some 85,000 family SMEs are expected to transfer ownership of their business to a new generation each year. BPR affords these firms an option to plan for a stable succession while maintaining ownership stability. It also plays a key role in ensuring that these small and medium firms can focus on scaling up their businesses. Around 77% of family SMEs are estimated to be first generation businesses; without BPR, these family firms would lose the opportunity to grow under stable ownership and successfully transition to the next generation, as the firms would have to be partially liquidated or sold to fund payment of any IHT charge arising for the business owners. Therefore, BPR is a significant pro-growth policy for business.

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Ultimately, without BPR, the death of a major shareholder could lead to the end of an otherwise profitable business, and associated job losses. 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. It provides family businesses with some of the stability they need to be able to continue to operate and plan for the future.

BPR is essential to sustaining the family ownership model in the UK, a model which we know will be crucial to supporting the continued economic recovery from the pandemic. By affirming your commitment to maintaining this important relief in full you will provide family business owners with additional confidence to invest in recovery and future growth.

Recommendation Two – Support succession transition planning in businesses by aligning Holdover Relief eligibility with BPR

Not all transfers of family business occur at death. Some business owners will phase their departure from the company, often passing part of the business ownership to the next generation upon retirement. This is both a sensible and efficient part of planning management and ownership succession in a business. For transfers made before death, business owners may be eligible for Business Assets Holdover Relief from Capital Gains Tax (CGT). Both Business Assets Holdover Relief and Business Property Relief (BPR) protect family firms from the danger of having to sell a business to pay a personal tax bill when no cash disposal is intended or planned. It also ensures family businesses do not have to hold cash aside for future tax bills and can instead continue to reinvest profit into the business.

However, to qualify for these reliefs, firms must pass different trading tests, creating confusion and difficulties for family businesses. The different tests for Business Assets Holdover Relief and BPR can act as a barrier for some businesses in executing an efficient ownership transfer during an owner's lifetime. Business Assets Holdover Relief is only available if a business contains more than 80 per cent trading activities. In contrast, the BPR position refers to a business being 'wholly or mainly' trading, the company must undertake at least 50 per cent trading activities.

There are many legitimate reasons which may see a trading family business taken out of the 80 per cent trading activities, including the impact of economic conditions and natural business cycles. Certain types of businesses are also more likely to be taken out of the 80 per cent threshold, whilst still being trading businesses (e.g. pub and brewing companies). Successful family businesses also often choose to retain profits (to use for future investment in the growth of the business) and invest in physical or counter-cyclical assets. Such assets, including property, can provide the balance sheet strength that enables investment in new ventures that may otherwise be considered too risky.

Because of the greater burden of the trading criteria for Business Assets Holdover Relief this can mean that gifts of shares are not made according to a desirable family business succession plan but are instead delayed for tax reasons sometimes hindering owners transferring shares during their lifetime. This can create a disconnect between the interests of the owners and the interests of the business, slowing sustainable economic growth and innovation by the next generation.

Bringing the Business Assets Holdover Relief qualifying criteria in line with BPR would be beneficial to family businesses in a number of ways. It would increase the understanding of the two reliefs, reduce bureaucracy and unnecessary costs – which we know is a priority for the Government - help ensure smoother succession planning for entrepreneurs, and ultimately increase the number of businesses continuing to thrive for generations to come.

It is essential that any changes must not restrict availability of either relief, as this would have serious implications on family business investment and growth.

Recommendation Three - Update the conditions for both Holdover Relief and Business Property Relief to ensure businesses with joint ventures are not penalised

More businesses are now also likely to fall into the category of not qualifying for Business Assets Holdover Relief or BPR because of the way in which joint ventures are treated when calculating trading tests. This is an area of particular concern when looking at how businesses will recover from the pandemic or explore opportunities to trade on the global stage. In relation to both Holdover Relief and BPR, the legislation has not moved to reflect now common business practices. This should be rectified to support modern business practices and unlock potential investment in innovative collaborations and expansion into new international markets.

Businesses will enter joint venture arrangements for a variety of reasons. If family members directly held the investment in the joint venture, and it was relevant business property, it would be eligible for relief. However, if the holding company owns an interest in a joint venture and the size of the joint venture is greater than the original business (as can be the case if the project is commercially successful) then the holding company might be considered to be holding investments (therefore excluded from reliefs). Generally family businesses also prefer to be involved in joint ventures at a practical level, not just as a silent investor. We believe this is an area which needs to be addressed.

Feedback from the IFB's membership strongly suggests that business is being held back by uncertainty on this issue in relation to IHT, and we believe the same is true in relation to CGT. The difficulty in receiving guidance from HMRC or achieving pre-clearance also causes issues for those running businesses. In light of the UK's withdrawal from the EU, and the COVID-19 pandemic, joint ventures are likely to be increasingly attractive to businesses, as they look at developing new opportunities and relationships for growth.

Joint ventures also provide an attractive route to new markets for businesses who are looking for local partners who can provide resources and expertise – particularly when undertaking global expansion - to reduce the initial risk. It is therefore important that this issue is resolved, so family businesses can make plans to grow their businesses and seek out new opportunities, feeling confident they are not risking the future succession of the business.

Recommendation Four – Support greater investment through targeted incentives and allowances

On investment, the Government must look at how it can support businesses to invest in themselves and the future. For many, the money they had planned to use for investing in their business has been used to keep them afloat in the past 18 months. Others have taken on significant debts. We therefore need measures which help lower the cost of entry for investment, in both people and capital expenditure. This approach would help recovery, productivity improvements, and good quality job creation.

The Government should therefore look at incentivising investment through targeted allowances, and set out what this regime will look like after the Super Deduction announced in March 2021 draws to a close. For example, extending the capital expenditure which is eligible for First Year Allowances. An increased Annual Investment Allowance should also be made permanent.

In line with the family business sector's strategy for long term sustainable growth targeted incentives for green investment should also be supercharged, to support the ambition to build back better, and greener.

Recommendation Five – Launch Patient Capital Review part two

Family firms have a unique ownership model which sustains and promotes long-term stewardship balancing the management of resources in the short, medium, and long-term. They tend to be less driven by short-term financial results which allows them to align the deployment of resources with their strategic objectives. A parallel exists with the German Mittelstand where profit maximisation is not the exclusive business goal. Investment, long-term sustainable growth, and commitment to their local community are generally prioritised.

The long-term outlook of family firms influences their needs when accessing finance to invest in their businesses. For example, families seek investment options which do not require them to give up equity in the business, as this is unattractive to some family business owners as it dilutes the family ownership and can introduce shareholders who may not share the same core values. They are also unlikely to look to public markets to raise finance, as keeping the business private allows for longer term planning, rather than focusing on quarterly reporting, which is essential for their sustainable economic growth.

Family businesses also typically have lower rates of borrowing than non-family firms. Their long-term focus means family businesses are 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 saddling themselves with debt. One consequence of the average low leverage in the sector is that during the last recession, there were lower comparable failure rates for family firms.

The Government's Patient Capital Review in 2017 focused on long term funding options for 'innovative, high growth companies'. It did not address the availability of long-term funding for other types of businesses. As they look to rebuild, create jobs, and invest in green technologies, family firms will need funding. We know that having left the EU, the Government is currently in the process of drawing up the new state aid framework to enable early-stage investment in British businesses. Given this wider attention given to the important of early-stage funding, now is the time to fix the historic gaps in the funding landscape to ensure that businesses of all sectors, sizes and locations can invest in their futures. We call on the Government to consider opening a second Patient Capital Review with a broader remit, to build on the work of the first report.

Recommendation Six – Prioritise greater support and focus on mid-sized firms

Mid-sized businesses will be a key component in our recovery and future growth. There are over 17,000 mid-sized family businesses, over half of all mid-sized businesses in the UK. In the North East, there are nearly 500 of these businesses, and in the North West over 1800. Empowering these businesses and supporting investment would see significant economic and employment benefits in their communities. Supporting their growth is an opportunity to transform the business landscape in the UK, enabling them to take the step from regional player to international competitor.

The UK needs a strategy which addresses the needs of mid-sized businesses and supports mid-sized business growth. These businesses are often overlooked in policymaking, with the focus either on very large or small businesses. These firms – the UK's Mittlestand – have huge potential, which needs to be harnessed as we look to build a stronger economy at both a national and regional level.

To stimulate additional long-term investment in mid-sized businesses the government should extend the EIS threshold to support investment in the growth of mid-sized businesses, taking the threshold to 499 employees (the same level as for knowledge intensive companies) and increasing the investment limit. This will help firms grow further and move from being mid-sized business to world-leading large firms.

The Government should also launch a cross-departmental review of how all areas of business, employment and tax policy affect mid-sized firms, and how the burden on these engines of growth can be reduced. The current definitions mean a business with 300 employees is currently subject to most of the same regulations and administrative burden as a business with 13000 employees. This acts as a major barrier to growth, eating up time and money that could be dedicated to scaling up. Identifying these barriers would be an important step forward in empowering these businesses to grow and create more high-quality jobs.

Recommendation Seven – Help young people get back into work and improve the apprenticeship system

Family businesses have a generational outlook and are acutely aware of the need to support and build opportunities for the generations following them. Family business owners are particularly concerned about the impact this crisis has had on young people, who are more likely to have lost their jobs. Creating opportunities for young people and supporting them in getting back to work must continue to be a key priority for the Government.

The Government's recent announcement of changes enabling large businesses to pledge funds for smaller businesses to help create and recruit for new apprenticeships is a positive step in reforming the system, but we would like to see the Government go further in these reforms.

We believe more still needs to be done to make the apprenticeship system work for employers and young people. In particular, the Apprenticeship Levy system should be overhauled to allow businesses to use a portion of their pot on in-house training. This funding could go towards vital upskilling of employees in new, green working practices, or in supporting those who have been on furlough for an extended period upgrade their skills on returning to work.

There is also a need to develop a more coordinated approach between the different systems in each nation to ensure training and apprenticeship are delivered where they are most needed, not where a business happens to pay the most in Levy payments.

Conclusion

As the Government looks to support growth and develop opportunities across every part of the UK, family businesses have an essential role in delivering this ambition. Family firms are the driving force across all regions, communities, and sectors of the UK. Well over 80% of businesses in Yorkshire, the North West, and the Midlands are family owned. In those regions alone, family firms employ nearly four and a half million people.

This Budget must focus on continuing to deliver the stability in the tax regime that businesses need, while also outlining a longer-term plan that prioritises investment as a means of stimulating economic growth. Growth – through investment – must be the priority, not tax changes that damage confidence and recovery.