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Not to be relied upon by retail investors.

Identifying clients who could benefit from BPR-qualifying investments

An Octopus guide

octopus investments

A brighter way

Key investment risks

- The value of a BPR-qualifying investment, and any income from it, can fall as well as rise. Investors may not get back the full amount they invest.
- Tax treatment depends on individual circumstances and could change in the future.
- Tax relief depends on portfolio companies maintaining their BPR-qualifying status.
- The shares of unquoted or smaller companies could fall or rise in value more than other shares listed on the main market of the London Stock Exchange. They may also be harder to sell.

BPR-qualifying investments are not suitable for everyone. Any recommendation should be based on a holistic review of your client's financial situation, objectives and needs. We do not offer investment or tax advice.

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Investments that qualify for Business Property Relief (BPR) can be passed on free from inheritance tax upon the death of the investor, provided the shares have been owned for at least two years at that time.

Find it fast

Introducing Business Property Relief

Business Property Relief is an established estate planning solution that can be used to pass on more of a person's wealth, free from inheritance tax.

It was originally introduced as part of the 1976 Finance Act, and was created to allow small businesses to be passed down through generations without facing a large inheritance tax bill. Beneficiaries inheriting family businesses no longer had to sell the business to pay any inheritance tax due when their parents died.

Over the years, successive governments have recognised the value of a tax relief that encourages people to invest in trading businesses, regardless of whether they run the business themselves, and so have expanded the scope of BPR.

This has included increasing the relief to 100% for qualifying shares (up from 50%) and allowing any interest in a qualifying company to benefit from relief – not just majority stakeholders.

As a result, BPR is now recognised as an inheritance tax relief that incentivises investments in unquoted trading companies or those listed on the Alternative Investment Market (AIM).

As long as BPR-qualifying shares have been held for at least two years at the time of the shareholder's death, they can be passed on to beneficiaries free from inheritance tax.

Using BPR to solve client problems

A BPR-qualifying investment can help solve common problems that clients face when it comes to estate planning. Clients who could benefit include those who want to retain access to their investment, those who have sold a business in the last three years and those where there is a power of attorney in place.

This guide shows how BPR-qualifying investments can be used to solve these and other common client problems.

It's important to note that BPR-qualifying investments are not suitable for all clients. Companies that qualify for BPR are not listed on any main stock exchange. As such, the value of an investment, and any income from it, can fall as well as rise. Investors could get back less than they invest. The tax incentives are there to help compensate investors for the risk they take with their money.

About Octopus

As the UK's largest manager of investments that qualify for Business Property Relief[1], we help families plan for their financial future. And we're making a difference in areas people really care about too. We invest in businesses that generate power from renewable sources, build retirement villages and support the UK's valuable smaller companies.

If you have any questions after reading this guide, please call our estate planning specialists on **0800 316 2067** or visit **octopusinvestments.com**. We're always happy to hear from you.

[1]Tax Efficient Review, April 2019.

Key benefits

Let's take a look at some of the benefits of BPR-qualifying investments.

Ongoing access and control

As BPR is an investment, it stays in the investor's name and offers on-going access to capital. If the investor's situation changes and they need access to their funds, they can sell down some or all of the investment. This might be the case for an older client who needs to pay for long-term care, for example.

Shares sold will no longer be exempt from inheritance tax.

Fast inheritance exemption

BPR-qualifying shares should become exempt from inheritance tax after just two years, so long as the investor is holding the shares at the time of their death.

Simplicity

Buying shares in BPR-qualifying companies is simple compared to some other estate planning solutions. There are no complex legal structures, like trusts, and there is no requirement for underwriting or medical questionnaires as with life insurance.

Key risks

BPR-qualifying investments come with risks.

Capital is at risk

The value of a BPR-qualifying investment portfolio, and any income from it, can fall as well as rise. Investors may not get back the full amount they invest.

Tax rules and reliefs can change

Tax treatment depends on individual circumstances and tax rules could change in the future. Whether the investment qualifies for tax relief will depend on portfolio companies maintaining their qualifying status. HMRC will consider a claim for BPR based on the facts when a claim is made, including the relevant legislation in place at the time.

Shares could be more volatile and less liquid

Investments in AIM-listed and unquoted companies are likely to fall or rise in value more than shares listed on the main market of the London Stock Exchange. They may also be harder to sell.

Identifying clients who could benefit from BPR-qualifying investments

BPR's attractive range of benefits means it can be used as an estate planning solution for a variety of clients.

On the following pages are some of the more common scenarios where a BPR-qualifying investment could be used to reduce an inheritance tax liability.

The example scenarios that follow are for illustration purposes only and assume that the nil-rate band is offset against other assets.

It is important to note that the risk profile of each portfolio, and any investment growth or losses, is likely to differ.

The tax benefits of the BPR portfolios compensate investors for the additional risks they're taking with their money.

The scenarios assume the costs for each portfolio are the same, but actual costs may be different. Examples do not include any charges paid for financial advice.

Clients who require access to their investment

As BPR is an investment, it stays in the investors name and offers on-going access to capital.

Carol doesn't want to lose access to her capital in later years. She's 80 years old and has inherited assets valued at just over £1.5 million from her late husband – including a house worth £700,000, a large investment portfolio and some savings in fixed-term bonds. Although she understands that her estate will leave her beneficiaries with an inheritance tax liability, she is reluctant to make gifts for several reasons.

First, she wants to leave money to her grandchildren, but they are young and she worries how they will spend it. Second, she worries about needing money for care home fees if her health deteriorates. Third, she is concerned that if she gives away assets and doesn't live for seven more years, she'll leave her beneficiaries with potential inheritance tax bills.

How a BPR-qualifying investment can help

After making an assessment based on her circumstances, and outlining the benefits and risks to her, Carol's financial adviser recommends selling £500,000 of her existing share portfolio and reinvesting the proceeds in the Octopus Inheritance Tax Service.

With an investment in the Octopus Inheritance Tax Service, Carol can make can make ad-hoc requests to sell some of her shares if she needs access to her capital. And if she finds that she needs to access her investment more regularly in the future, she can set up regular withdrawals, as well. However, like all investments that qualify for BPR, liquidity cannot be guaranteed.

Provided the BPR-qualifying investment has been held for at least two years, the shares can be left free from inheritance tax to Carol's grandchildren when she passes away. She will have access to her investment during her lifetime, meaning that she can meet any future care fees or other costs by selling some or all of her investment.

For most investors, withdrawals are below their annual capital gains tax (CGT) allowance, so there would be no CGT to pay on the proceeds from the share sales.

Remember, shares sold or money taken out of the investment will no longer be exempt from inheritance tax.

Carol

£500,000
kept in her share portfolio

£500,000 sold from her share portfolio.
£485,149 invested in the Octopus Inheritance Tax Service after 2% initial fee and 1% dealing fee charged

Carol passes away after three years

Share portfolio worth £546,364
Assuming an example net growth rate of 3% per annum

Octopus Inheritance Tax Service portfolio worth £530,135
Assuming an example net growth rate of 3% per annum

£218,546
Inheritance tax charged at 40% on Carol's share portfolio

£0
No inheritance tax charged as Carol died after holding the shares for more than two years

£322,355
passed to grandchildren after 1% dealing fee to sell the portfolio has been paid

£524,770
passed to grandchildren after 1% dealing fee to sell the portfolio has been paid

If Carol's health deteriorates during her lifetime and she moves into a care home, her financial adviser can set up regular withdrawals for her. Any growth in shares sold would be subject to capital gains for tax (CGT).

Any growth in the value of the shares between investment and Carol's death will not be subject to CGT (unless she sold them during her lifetime).

The Octopus Inheritance Tax Service has an initial charge of 2%, a deferred annual management charge (AMC) of up to 1% + VAT, and a dealing fee for investments and withdrawals of 1%.

Clients who want an inheritance tax-efficient ISA

ISAs come with attractive tax benefits during someone's lifetime, but are subject to inheritance tax along with the rest of a person's estate when they pass away.

As of 2013 though, investors can hold shares in AIM-listed companies that are expected to qualify for BPR within an ISA.

Peter is a committed ISA investor. But like thousands of people across the UK, he is concerned about inheritance tax. Peter is 70 years old and has never married. His house alone is worth more than £500,000 and he expects that his daughter Emma will have to pay 40% inheritance tax on his investments when he dies. This includes the ISA investments he's been building up over the years.

He'd like to find a way to invest that retains the tax benefits of an ISA wrapper, without the inheritance tax liabilities.

How a BPR-qualifying investment can help

Peter talks to his financial adviser, who makes an assessment based on his objectives and attitude to risk. Given this, his adviser suggests investing in a BPR-qualifying investment held within an ISA. It comes with the same tax benefits his ISAs have always enjoyed, but after two years the ISA becomes free from inheritance tax, assuming it is still held at the time of death.

It also offers access to the growth potential of carefully selected UK smaller companies. Peter's money will be invested in a selection of companies listed on the Alternative Investment Market. Certain AIM-listed companies qualify for BPR, and after holding the ISA for two years the investment should become free from inheritance tax.

The estate planning benefits of this ISA may make it particularly interesting for clients considering ISA transfers, especially older clients who have large estates, and have built up significant ISA portfolios.

Many forms of inheritance tax planning put money permanently out of an investor's reach. This lack of access can make it more difficult to deal with any unexpected costs that come up in later life. However, with a BPR-qualifying investment held within an ISA, the investment is still held in the client's name, and they can access their investment when they need to.

Peter

£100,000
retained in stocks and shares ISA

£100,000
transferred into the Octopus AIM IHT ISA, from which a 1% dealing fee is taken as shares are purchased

An example growth rate of 5% has been assumed across both investments. Annual management charges and dealing fees have been applied to both portfolios in line with those applicable to the Octopus AIM IHT ISA

Peter passes away after five years

The value of his portfolio with growth and fees
£127,034

The value of his portfolio with growth and fees
£125,776

£50,814
inheritance tax due at 40%

£0
inheritance tax due

£74,950
cash value available to beneficiaries after shares have been sold and 1% dealing fee has been applied

£124,518
cash value available to beneficiaries after shares have been sold and 1% dealing fee has been applied

The annual management charge is 1.5% + VAT. The estimated annual dealing charges are 0.20%, typical for the Octopus AIM Inheritance Tax ISA. However, actual dealing charges experienced by an investor may be higher or lower. Also, the current ISA provider may charge a fee for transferring an existing ISA.

Clients with a power of attorney in place

Where a lasting power of attorney is in place, the ability to make gifts is very limited without approval from the Court of Protection.

But by investing in shares that are expected to qualify for BPR, just like any type of investment, the shares remain the property of the investor.

Tom has power of attorney over his aunt Eve's affairs. Eve, who is 84, consolidated her assets and converted them into £850,000 cash before entering a care home. Following the death of her husband, Eve has a nil-rate band of £650,000, but faces leaving behind an inheritance tax bill on the remaining £200,000.

Tom has lasting power of attorney over his aunt's assets, and the circumstances in which gifts can be made from his aunt's estate without Court of Protection approval are limited. In any event, gifts will take seven years to fully fall outside of Eve's estate for inheritance tax purposes. Tom is one of three beneficiaries of Eve's will, alongside his brother and sister.

How a BPR-qualifying investment can help

Tom needs to ensure that any investment decisions are made in his aunt's best interests and won't disadvantage her, for example, by making her money inaccessible.

Eve's financial adviser makes an assessment based on her objectives and attitude to risk. The adviser suggests that Tom invest £200,000 on his aunt's behalf in a BPR-qualifying investment. The investment is made in Eve's name, meaning she retains ownership of her wealth. As long as Eve has held the investment for at least two years when she dies, she can leave the shares to her beneficiaries free from inheritance tax, saving the three beneficiaries an inheritance tax bill of £80,000.

Unlike estate planning strategies that rely on life assurance, there are no underwriting or complicated medical forms to complete – the application process is straightforward. Withdrawals can be requested at any time, for example if Eve requires additional funds for care home fees. It's important to remember that any withdrawals will be facilitated by the sale of shares and so can't be guaranteed.

Eve

£200,000
invested in a listed share portfolio
£650,000 remains in cash

£200,000
invested in the Octopus Inheritance Tax Service
£650,000 remains in cash

Eve passes away four years later

A stocks and shares portfolio worth **£218,416***
is subject to inheritance tax at 40%

Investment in the Octopus Inheritance Tax Service
worth **£218,416*** is free from inheritance tax

£650,000 of cash
can pass free from inheritance tax due to Eve's and her late husband's
combined nil-rate bands (2x £325,000)

£87,366
inheritance tax due

£0
inheritance tax due

£778,865
left to pass on after the portfolio has been sold
and 1% dealing fee charged

£868,416
left to pass on after the Octopus Inheritance
Tax Service portfolio has been sold and 1% dealing
fee charged

*An example net growth rate of 3% per annum assumed across both investments along with an initial charge of 2%, dealing fee of 1% and annual management charge of 1%+VAT per annum.

The Octopus Inheritance Tax Service has an initial charge of 2%, a deferred AMC of up to 1% + VAT per annum, and a dealing fee for investments and withdrawals of 1%. We only take our annual management charge after the investor or their beneficiaries ask us to sell shares. We will only take our full AMC if the investment has delivered the annual target return of 3% over its lifetime, after AMC has been taken into account.

Clients who want to settle assets into trust

Settling assets into trust is a way of reducing a potential inheritance tax bill as they are no longer part of your estate.

With a discretionary trust, however, investors are subject to a 'chargeable lifetime transfer' – a charge of 20% on the amount settled in excess of the investor's nil-rate band.

This charge can be effectively eliminated by investing in BPR-qualifying shares and then settling those shares into trust after two years, after which time they should become exempt from inheritance tax.

Louise wants her wealth passed down to her younger generations. One of her biggest concerns is that the marriage of one of her children could end in divorce. Louise wants to make sure that her grandchildren will benefit from her wealth, rather than her assets being lost through any divorce proceedings.

Louise talks to her financial adviser about settling her existing share portfolio worth £600,000 into trust for her children and grandchildren. Her adviser explains that as she has not previously made any gifts or set up any trusts, she will be able to put the first £325,000 (the nil-rate band) into trust with no charge. Anything settled into trust over £325,000 would immediately trigger a chargeable lifetime transfer of 20%. This would reduce the amount in the trust by £55,000. If Louise were to die within seven years of setting up the trust, further inheritance tax would also be payable.

How a BPR-qualifying investment can help

Louise's adviser makes an assessment based on her objectives and attitude to risk. Given this, her adviser suggests selling her share portfolio and reinvesting the proceeds into a BPR-qualifying investment.

Once the BPR-qualifying shares have been held for a minimum of two years, they should be exempt from inheritance tax. Louise can then transfer the shares into a discretionary trust and no chargeable lifetime transfer will be payable.

If the trust continues to hold investments that qualify for BPR, there will be no future inheritance tax charge on the trust. What's more, this planning hasn't used any of her nil-rate band, which can therefore be used to offset against other assets, even if she dies within seven years.

Louise

£600,000
placed in trust

First **£325,000**
set against nil-rate band – therefore no charge

Remaining £275,000
subject to **£55,000** chargeable lifetime transfer

£600,000
invested in the Octopus Inheritance Tax Service

After two years

£617,633
investment (now BPR-qualifying) placed in trust

£0
chargeable lifetime transfer

£578,191
held in trust for beneficiaries

£617,633
held in trust for beneficiaries

Although Louise is in good health, if she were to die within seven years of settling assets into the trust, an additional inheritance tax liability may be triggered

No further inheritance tax liability, provided the trust retains the investment until either Louise's death or the seventh anniversary of when the assets were settled into trust

An example net growth rate of 3% per annum has been assumed. An initial charge of 2%, dealing fee of 1% and annual management charge of 1%+VAT per annum have been applied to both portfolios. These are the charges associated with the Octopus Inheritance Tax Service.

Clients who've sold a business in the last three years

While family businesses can typically be passed on to beneficiaries free of inheritance tax, if the person sells the business in advance, they could leave behind an inheritance tax liability as the capital will no longer qualify for BPR.

Alan used to own a small business, but sold it two years ago. He's a widower and his health has deteriorated recently, which means he is considering ways to get his financial affairs in order. He would like to be able to leave the proceeds of the sale of his business (£1 million) to his three daughters without them facing a large inheritance tax bill. Given Alan's health, his adviser has cautioned against traditional forms of estate planning, such as gifts and trusts, which take seven years before becoming free from inheritance tax.

How a BPR-qualifying investment can help

When Alan still owned his company, his shares were expected to qualify for BPR, meaning he could have left them to his daughters on his death free from inheritance tax. However, now Alan has sold his investment in his business, he is concerned about the inheritance tax that may be payable on the proceeds.

New investments into BPR-qualifying shares usually take two years to become exempt from inheritance tax. However, the good news for Alan is that there is a three-year window during which some or all of the proceeds resulting from the sale of a BPR-qualifying business can be invested back into BPR-qualifying assets. If Alan does this, the newly acquired BPR-qualifying assets should be immediately exempt from inheritance tax – he wouldn't need to wait the two years it would normally take for a BPR-qualifying investment to become exempt from inheritance tax.

After Alan talks to his financial adviser, who makes a recommendation based on Alan's objectives and attitudes to risk, he decides to invest £1 million into a BPR-qualifying investment. Because Alan's investment qualifies for replacement relief, his new investment should be exempt from inheritance tax from day one. This means that, on his death, he expects to be able to leave it to his daughters free from inheritance tax.

Alan

Stocks and shares portfolio	Octopus Inheritance Tax Service
£1,000,000 invested into a stocks and shares portfolio	**£1,000,000** invested into the Octopus Inheritance Tax Service investment (instantly BPR-qualifying)

Initial charge of 2%, dealing fee of 1% and annual management charge of 1%+VAT per annum applied

Value of portfolio after 1 year at 3% net growth **£999,406**	Value of portfolio after 1 year at 3% net growth **£999,406**
£399,762 inheritance tax due	**£0** inheritance tax due
£589,650 left to pass on at death after 1% dealing fee to sell the portfolio has been paid	**£989,295** left to pass on at death after 1% dealing fee to sell the portfolio has been paid

It's important to remember that the risk profile of each portfolio, costs and any investment growth or losses are likely to differ.

The Octopus Inheritance Tax Service has an initial charge of 2%, a deferred AMC of up to 1% + VAT per annum, and a dealing fee for investments and withdrawals of 1%.

Clients with a loan trust in place

With a loan trust, any investment growth on the capital lent to the trust will be expected to fall outside the client's estate for inheritance tax purposes.

However, the amount of the original loan remains subject to inheritance tax when the client dies.

Tony has named his children as beneficiaries of a loan trust. He's in his late 70s and has an attractive income from his pension. Two decades ago, Tony inherited a large sum of money. He used this inheritance to set up a loan trust so that the growth on his capital would benefit his children. At the time, the capital lent to the trust was invested into a portfolio of stocks and shares which have delivered growth. However, while the growth of Tony's investment is outside of his estate for inheritance tax purposes, the capital lent to the trust remains inside the estate, and is therefore still subject to inheritance tax.

How a BPR-qualifying investment can help

Tony is aware that the capital is subject to an inheritance tax liability, and is now considering wider estate planning. He talks to his financial adviser, who makes an assessment based on his risk profile, and attitude towards investing in unquoted companies. He explains to him the benefits and risks of investments that qualify for BPR.

Now that the underlying investments in the loan trust have matured, his adviser suggests Tony requests repayment of the loan and reinvests the proceeds in a BPR-qualifying investment held in his own name.

This would effectively turn the loan capital into an investment that is inheritance-tax efficient. As long as Tony has held his BPR-qualifying investment for at least two years when he dies, the shares are expected to be able to pass to his beneficiaries free from inheritance tax. The growth achieved by the loan trust would continue to be outside of Tony's estate for inheritance tax purposes, and could itself be invested to generate further growth within the trust.

Tony

£600,000
loan trust capital plus **£400,000** of growth remains within the trust

£1,000,000
remains invested within the trust in a stocks and shares portfolio

£600,000
loan trust capital repaid to Tony and invested in the Octopus Inheritance Tax Service

£400,000
of growth remains invested in stocks and shares portfolio within the trust

Tony dies after three years

Value of assets within the trust that can be left to Tony's children free from inheritance tax on death: **£492,727***. This is the growth within the trust

The **£600,000** loan is subject to 40% **(£240,000)** inheritance tax, reducing the amount left to Tony's children to **£360,000**

Assets worth **£852,727** will be left to Tony's children after inheritance tax has been paid

Value of assets within the trust that can be left to Tony's children free from inheritance tax on death: **£437,091***. This is the growth within the trust

The BPR-qualifying investment worth **£636,162** is left to Tony's children free from inheritance tax

Assets worth **£1,073,253** will be left to Tony's children after inheritance tax has been paid

*Assuming an example net growth rate of 3% per annum across both investments after annual management charges of 1.2% have been taken. Initial fees of 2% and dealing fees of 1% have been deducted from Tony's investment into the Octopus Inheritance Tax Service.

BPR-qualifying investments from Octopus

At Octopus, we're the largest provider of investments that qualify for relief from inheritance tax[1].

If you have clients that might be suitable for BPR-qualifying investments, we'll help you identify which of the following inheritance tax products could provide a solution:

- **Octopus Inheritance Tax Service**: targets modest and predicable growth. Invests in the shares of one or more unlisted UK companies that are having a positive impact on the growth of the UK economy.
- **Octopus AIM Inheritance Tax Service**: invests in a diversified portfolio of smaller companies listed on the Alternative Investment Market (AIM) and targets growth.
- **Octopus AIM Inheritance Tax ISA**: an ISA which invests in a diversified portfolio of smaller companies listed on the Alternative Investment Market (AIM) and targets growth.

Estates and Probate Team

We've been managing inheritance tax-efficient investments since 2005. Our experience suggests that when an investor dies, members of their wider family are often not familiar with this kind of investment.

An understanding adviser can make a real difference, both by helping executors during the probate process and by advising beneficiaries on their options once they inherit their shares.

Our dedicated Estates and Probate Team has helped more than 1,000 estates through the probate process and helped more than 400 advisers retain beneficiaries as clients of their own.

You can call them on **0800 294 6826** with any queries about your client's investment and the process of claiming Business Property Relief.

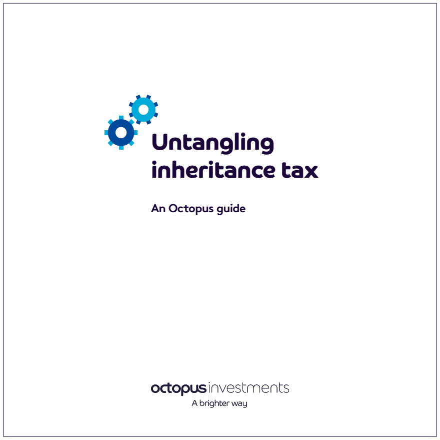
We can also support you if you want to advise any of your client's beneficiaries on what to do with the shares they inherit. There are often benefits to retaining the shares, which beneficiaries should understand before making their decision. There are, of course, also risks.

We can also facilitate paying an inheritance tax bill directly to HMRC if your client holds a BPR-qualifying investment with us. This can be done in advance of probate being granted, using the **IHT421 form**. Our team will be happy to talk you through this process.

[1]Tax Efficient Review, April 2019.

Resources from Octopus

Here are some other handy guides that you and your clients might find useful. Go to octopusinvestments.com to download a copy, or call us on 0800 316 2067 and we can get one sent out to you.



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