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INVESTMENTS

Managing Surplus Cash Held in a Business

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Do you have business-owning clients with surplus cash in their company, or do you work with accountants who may have these clients? If so, this article will be of particular use.

Having a healthy bank balance is nirvana for companies, but could that nirvana turn into a nightmare for them? There are many reasons why business owners keep large sums of surplus cash in their business. It may give them peace of mind should the company hit trouble in future, or it could provide the business with a 'war chest' to fund potential expansion opportunities, such as buying additional premises or to acquire another business.

These are the most common reasons I hear for companies keeping high levels of cash on their balance sheet. However, this can cause potential issues down the line. For example, keeping too much cash in the company that is not used in the day-to-day running of the business could mean the company loses its trading status, and mean it is deemed by HMRC as an investment company. Should that happen, the shareholders risk losing Business Asset Disposal Relief (BADR), formerly known as Entrepreneur's Relief, when they sell the business, and could end up doubling their Capital Gains Tax bill!

In addition, 'lazy' cash in a company (cash which isn't being used as part of the trade) could be treated as an excepted asset by HMRC when assessing a shareholder's estate for Inheritance Tax (IHT) purposes. Therefore, the surplus cash in the business would not qualify for Business Relief (BR), and the shareholder's beneficiaries may face an IHT bill on this excepted asset, even if the rest of the business was deemed BR-qualifying.

Due to consistently low interest rates, the cash sat on deposit won't even be keeping up with inflation, never mind growing, and so companies are losing the buying power on this money as time goes by. So, what can business owners do? There are four main options available to the business owners to potentially reduce or avoid the potential pitfalls mentioned above, assuming they haven't found another business to invest into yet, or other ways to spend the money in the business.

These options are:

- Move the surplus cash out of the company and use it to by investing in their pensions (if applicable and desired), although they will need to be mindful of the annual pension allowance, which caps the amount they can invest into their pension before they pay tax at £40,000 per year.
- Take extra dividends, suffer the tax, and invest elsewhere in their own (business owner's) name.
- Take an extra dividend, suffer the tax but invest it into a Venture Capital Trust (VCT) or Enterprise Investment Scheme (EIS) and claim income tax relief of up to 30% of the value of the investment (often considered as a 4–5 year useful exit strategy of getting money out of a business tax-efficiently).
- Keep the money within the realms of the business, but have the money trading in another BR-qualifying business, such as a lending business.

The Blackfinch Corporate Management Service was created specifically for the purpose of giving companies the opportunity to use their surplus cash, as a trade, within a lending business. In order to qualify as a trade, the loans must be short term in nature (less than three years) with the expectation of them being re-cycled over time.

By utilising this cash in another trade, assuming that they will be a trading and BR-qualifying company at the time of sale or death, then it could potentially help with making their money work harder as the annual target return (net of Blackfinch's fees) is a very competitive 4%-5%p.a. and is not linked to the stock-market so does not suffer from stock-market volatility. Of course, this return is not guaranteed, but is an expected target return. Blackfinch charges an annual management fee of 0.5% (+VAT) but will only take this after the agreed target return has been achieved.

Investing the surplus cash into the Blackfinch Corporate Management Service also helps ensure the cash remains accessible. This is one of the biggest advantages of the service, as the investment can be realised in case a business opportunity does crop up, or indeed if the business does hit troubled times.

For the business owners, they can feel reassured that as the surplus cash is now being used for BR-qualifying trades, rather than as sitting as idle cash, it should continue to qualify for BR and fall outside of the shareholders' taxable estate. Additionally, as the cash no longer endangers the business's trading status, as it is now also trading alongside their main business which will maximise the likelihood of HMRC granting BADR at 10% when they sell.

The Blackfinch Corporate Management Service is an increasingly popular way for business owners to do something positive and valuable with their surplus capital. If you know clients or companies in this situation, please get in contact with Blackfinch. You may also want to share this article with some of your professional connections, especially accountants, who may want to use it as a talking point with their clients.

A bespoke tax-efficient solution for businesses.

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