

Five years with no inheritance and gift taxes

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Foreword

MAY INHERITANCE AND WEALTH TAXES REST IN PEACE!

It has now been five years since Swedish inheritance and gift taxes were repealed. On the 16th of December 2004, the Riksdag repealed the inheritance and gift taxes. Originally, the repeal was to have taken effect on 1st January 2005, but when the tsunami disaster occurred, the Riksdag voted to repeal the taxes retroactively to 17th December 2004.

The challenges faced by Swedish family businesses were one reason for repealing the inheritance and gift taxes. About half of all family-owned businesses were then facing a generational change within the next ten years. Hundreds of thousands of employees, customers and suppliers would be affected, right alongside the business owners.

The inheritance tax was a double burden on family business owners – who often had all their assets tied up in the business – because it forced them to withdraw taxed capital from the enterprise to pay inheritance tax. Many entrepreneurs agonised about how their businesses would survive the coming generational change and the associated taxation. The taxes compelled many of them to implement complex business structures to provide for the survival of the business. Business often suffered as owners had no choice but to think about, discuss and plan tax-related matters, which demanded a great deal of time and energy. Sometimes there was even direct impact on the direction of the business. It is no wonder Swedish business owners greeted the decision to repeal the inheritance and gift taxes with tremendous relief.

In order to arrive at a picture of how the repeal of taxes associated with generational change has affected family businesses, the Confederation of Swedish Enterprise interviewed attorneys, bankers, accountants, business brokers and other relevant market players. The interviews were conducted by Christofer Pihl and Nima Sanandaji, both of the think tank Captus, in December 2009.

The respondents are happy about the repeal, even though it has resulted in less tax work for many advisers. The repeal has simplified matters considerably for businesses, and professional firms that work with business transfers are pleased that these transactions have become easier for their clients. One positive impact is that the need for tax planning in connection with generational change is a thing of the past. Most importantly, this has helped shift concentration to business-oriented decisions and provided greater scope for finding the optimal solution for the business. There are also several similarities here to the respondents' views on the repeal of the wealth tax. More capital is left in the hands of businesses and entrepreneurs and regulatory simplifications have cut costs. First and foremost, business owners have been able to concentrate on making strictly business-oriented decisions—without the disruptions and distortions of tax-related side-effects.

The repealed inheritance, gift and wealth taxes comprise a package that facilitates transfers of ownership in family businesses. However, professionals who work with business transfers report that their clients are worried about the prospect that the wealth tax may be reinstated. The mere threat has resulted in less capital returning to Sweden.

Brand new statistics from Statistics Sweden (SCB) show that of the 148,000 family business operators in the country, counted as partners in a closed companies, 46 percent are 50 or older and a goodly number—18 percent—are 60 plus. Thus, favourable conditions for business transfers are still a topical and highly prioritised policy area. Business owners and professionals involved with the issue have one clear message: repeal of the inheritance, gift and wealth taxes was and remains important to Swedish family businesses. May these taxes rest in peace and not be resuscitated in order to pander to populism.

Krister Andersson
Head of the Tax Policy

Confederation of Swedish Enterprise

INTRODUCTION

A total of 14 interviews were held in late November and early December 2009 with professionals whose work involves matters related to the inheritance tax. The objective was to arrive at an understanding of the effects of its repeal.

The sample consisted of lawyers, accountants, tax consultants, financial advisers and tax and accounting experts. The interviews were held by phone, and the questions on which the ensuing discussions were based were as follows:

- How has repeal of the inheritance tax affected your operations?
- Have you seen any particular effects due to the repeal?
- Has the repeal resulted in any change in the number of business transfers?
- Has the nature of business transfers changed?
- What long-term effects has the repeal had, and what is your outlook on the future?
- How has the repeal affected companies whose ownership has remained in the family?
- How has the 2007 repeal of the wealth tax affected business transfers?

A summary of the study findings as a whole is presented below, followed by individual summaries of the interviews.

IMPACT OF THE REPEAL ON THE OPERATIONS OF SURVEYED FIRMS

All respondents reported that repeal of the inheritance tax has affected their operations to some extent. How they perceived the magnitude of the impact varied depending on what kind of firm they work for and the nature of their tasks.

The main change that emerged in the interviews is a radical contraction of the advisory services market related to business transfers subsequent to the repeal of the inheritance and gift taxes. One interesting observation is that none of the respondents said they were in favour of the tax or thought it should be reinstated, despite the impact on their operations. On the contrary, they are happy the repeal was such a relief to their clients.

Ten people reported that the repeal has had relatively substantial impact on their work and the operations of their firm. These individuals are lawyers, tax consultants, accountants and tax and accountancy experts. Their professional roles are distinguished by frequent involvement with business transfers, generational changes and transactions related to distributions of marital assets.

Four people reported that the repeal has had relatively little impact. These individuals mainly work with business matters that are not closely related to transfers of ownership. For example, two of the four work primarily with investment advisory services to private individuals and closed limited liability companies. However, these four individuals said that repeal of the wealth tax has had significant impact on their operations.

EFFECTS OF THE REPEAL

As one, the respondents stated that repeal of the inheritance and gift taxes has simplified matters for their clients. A majority reported that the repeal has reduced the need for planning in preparation for a generational change. Meticulous planning used to be essential to minimise the impact of inheritance and gift tax through a variety of structures, such as foreign solutions or reductions in business assets.

Planning is still important for business and financial management reasons, but is not used to the same extent for tax reasons. One respondent said there is a downside to the repeal of the inheritance tax, in that less emphasis is put on planning, which thus may not get done in a timely manner.

Some respondents argued the opposite and held that the repeal has made generational changes and business transfers more flexible. For that reason, they believe the repeal was good for entrepreneurs and for the economy in general.

Another key impact some respondents mentioned is the substantial reduction of transaction costs in terms of both time and money. As well, focus on tax consequences has declined, allowing greater scope for and concentration on business decisions.

One individual related that there was some speculation that repeal of the inheritance and gift taxes would lead to evasive practises related to gifts, and widespread returns to Sweden ahead of generational shifts and business transfers, something this individual has not found to be the case. Another respondent described the opposite and said the repeal has inspired more people to return to Sweden.

LONG-TERM EFFECTS OF THE REPEAL

The respondents were asked what long-term effects they believe the repeal will have, especially in relation to generational changes and business transfers. Here again, several stressed the importance of simplification.

Three individuals said that one key long-term effect is that since capital no longer has to be used for taxes, more of it staying with the businesses. One person said that Swedish enterprise as a whole is stronger as a result.

According to another respondent, repeal of the inheritance and gift taxes gives Sweden a tax law advantage from the international perspective.

Some of the people we spoke to said there is some uncertainty in terms of the risk that these taxes could be reinstated, particularly the wealth tax, but also inheritance and gift taxes. Four people were unsure about what the long-term effects of the repeal might be.

Beyond these effects, the respondents also described the following potential effects from a long-term perspective:

- Greater latitude and scope for action, which is considered positive
- Macro-economic benefit as a result of the simplification brought by the repeal, which improves conditions for putting Swedish enterprise in younger hands
- Easier planning of other tax consequences, such as those related to income tax law

EFFECTS OF THE REPEAL ON THE NUMBER OF BUSINESS TRANSFERS

A majority of the respondents—ten people all together—have no views on whether the repeal has affected the number of business transfers in terms of generational changes and business transfers. Some of those surveyed report that other factors, such as the nature of the business and whether the younger generation are interested in taking over, have greater impact.

Three people believe the repeal has led to an increase in the number of transfers and one believes the number has not changed. None believe that business transfers have declined in number due to the repeal.

EFFECTS OF THE REPEAL ON THE NATURE OF BUSINESS TRANSFERS

When asked whether the nature of business transfers has changed, most reiterated the importance of the general effects of the repeal as they understand them. For instance, the repeal has brought greater flexibility in terms of when transfers of ownership and generational changes take place, and it is considerably simpler to carry out transfers than it used to be.

One effect described by six respondents is that more people are choosing to do more of the planning involved in generational changes and business transfers themselves, due to the substantial reductions in complexity, cost and required expertise. Three respondents had no opinion about whether the nature of business transfers has changed.

IMPACT OF THE REPEAL ON BUSINESSES THAT STAY IN THE FAMILY

Nine respondents had no definite views on the impact of the repeal on businesses that stay in the family, other than the general effects previously described.

One respondent believes that the repeal is a boon to family businesses because the suitability and level of education of the potential new owners are becoming more central considerations in connection with transfers. The repeal has also made it easier for third parties to step in with partial financing. Another respondent reiterated the greater importance of other factors in connection with transfers and said the repeal has made only a marginal difference.

IMPACT OF THE REPEAL OF THE WEALTH TAX ON BUSINESS TRANSFERS

There are great similarities in how the respondents describe the effects of repeal of the wealth tax and repeal of the inheritance and gift taxes.

Many of the respondents assert that more capital is remaining in the hands of firms and entrepreneurs due to the repeal of the wealth tax. Other common answers were that attention to tax consequences has become less important since the repeal, and that the repeal has simplified transactions and thus reduced costs.

A majority of the respondents believe their clients are worried the wealth tax may be reinstated. There is also concern in some quarters that the inheritance and gift taxes may be reinstated in some form.

The people who feel their clients are worried speculate that this may result in less capital returning to Sweden. They also believe that concerns about reinstatement make it too early to judge the full impact of the repeal.

Five respondents had no views on possible effects, or believe the impact is marginal.

OPINIONS ON THE REPEAL OF THE INHERITANCE TAX

Brief excerpts of the respondents' answers during the interviews are provided below. Some respondents have asked to remain anonymous.

GUNNAR HJERTQUIST, ATTORNEY AND PARTNER IN THE LAW FIRM OF GÄRDE WESSLAU ADVOKATBYRA

The repeal has made business transfers easier for all parties concerned, according to Hjertquist. Structures aimed at minimising inheritance tax are a thing of the past. Planning in connection with generational changes or business transfers used to be of paramount importance, but the repeal has changed that.

Opportunities to focus on who should take over and how a transfer should be carried out are better than they were before the repeal. Hjertquist said that repeal of the inheritance and gift taxes combined with repeal of the wealth tax has the potential to produce more professional business conduct, with the main emphasis on discussions and decisions instead of tax issues.

“Business growth and development are facilitated when business-optimal solutions to changes of ownership are possible. It is easier to carry out a transfer because the suitability and interest of the parties can be examined.”

He is uncertain about what the potential future effects of the repeal, and believes that other factors may have greater impact on the shape of business transfers to come. For example, Hjertquist stated that the younger generation are more likely to pursue higher education these days, and thus may be very well equipped to take over businesses when future generational changes occur.

GÖRAN STRÖM, TAX AND ACCOUNTING EXPERT, KPMG

According to Ström, the main impact of the repeal has been on owner-operated businesses. Restructuring is probably easier to carry out due to the repeal. Generally speaking, the gift and inheritance taxes, especially the gift tax, were problematic in connection with various types of restructuring.

Ström believes that the number of restructurings and transfers of ownership may have increased due to the repeal and that more businesses have begun handling transfers on their own.

“You don't need the same kind of planning now. A lot of planning used to go into minimising taxes, especially inheritance and gift tax.”

Ström further related that there are many examples of how planning aimed at reducing the tax consequences of inheritance and gift taxes, such as when family-owned groups changed hands. In hindsight, it turned out that this planning, which frequently zeroed in on reducing inheritance and gift taxes, instead resulted in income tax liability, which was unnecessary in view of the repeal. Ström believes that one key long-term impact of the repeal is that more capital is now remaining in Sweden.

HERMAN HOLMQVIST, INVESTMENT ADVISER, MAX MATTHIESSEN

Holmqvist reported that most of his clients know about and are favourable to the repeal of inheritance and gift taxes.

“I think the repeal of the inheritance and gift taxes was good for both private individuals and companies. People no longer have to fear they will have to pay tax when they give monetary gifts.”

Holmqvist described how he believes people are saving more for their families due to the repeal. He referred primarily to grandparents who save in their own names with the intention of later giving assets to their children and grandchildren.

Holmqvist is unsure whether the repeals have resulted in any change in the number of transfers and changes of ownership or changes in the nature of business transfers. He said the repeals have had positive impact mainly because they have simplified things to such great extent.

JOAKIM NORSTRÖM, FINANCIAL ADVISER, STOCKHOLM

Norström related that in his experience, the business operators he meets (mainly owners of closed limited liability companies) have difficulty finding people who want to take over the business in a generational change. Instead, the business is wound up and the company's remaining assets are distributed. Norström deals with issues related to the repeal on occasion and said:

“If I had to guess, I would say that most people find things easier now, compared to how things were.”

Norström believes the number of business transfers depends primarily on other factors and does not think there has been any increase or decrease due to the repeal. He says wealth tax is a fairly common topic in his discussions with clients, who are concerned about whether it might be reinstated. In his experience, inheritance and gift tax are discussed less often than wealth tax.

MARTIN KARLSSON, TAX CONSULTANT, GRANT THORNTON LULEÅ

Planning for estate distribution used to be relatively expensive, but Karlsson has noted a distinct decline since the repeal in terms of assignments focused on the tax consequences of generational changes.

“Now that both the inheritance and gift taxes are no more, it is considerably easier to bequeath a business. The repeal has made things a great deal simpler.”

Karlsson said his firm is working more with drafting deeds of gift than they used to. He also believes the repeal has increased the number of business transfers. One important long-term effect of the repeal is that capital can be used for operations, instead of being tapped for taxes. Small businesses often stay in the family, but larger companies often demand specialist expertise and are less likely to stay in the family. Instead, they tend to be sold to outside buyers.

It was fairly easy to legally circumvent the wealth tax, so the impact on business transfers was relatively minor according to Karlsson. He also believes that transfers happen at around the same point as before, due to the strong norm in Sweden related to the appropriate age of retirement.

MARTIN PAULETTE, ADVISER, CERBERUS OBEROENDE INVESTERINGSRÅDGIVNING

Paulette described how all family businesses used to have to deal with the inheritance and gift taxes and that in his experience they are happy they no longer need to do so. Before the repeal, various types of pension and trust solutions were commonly used to reduce the tax consequences, something that took a toll on resources in terms of both time and money.

A lot of people used to feel compelled to put more planning into business transfers while the principal was still living. The inheritance tax affected business decisions and caused many enterprises to focus on tax consequences rather than other factors that might have been more important from the long-term perspective.

“The inheritance tax made things less efficient. There was no talk of purely business-based decisions; the main topic was really various types of structures aimed at precluding taxes.”

Transaction costs are lower now in terms of advisers, accountants and foreign solutions. Paulette believes the EU Money Laundering Directive has led some of his clients to move assets back into Sweden. He thinks the fact that inheritance, gift and wealth taxes no longer have to be considered is beneficial, as it gives Sweden a tax advantage compared to other countries.

PETER WILLIAMSSON, AUTHORISED PUBLIC ACCOUNTANT, FALUN

Williamsson related that his clients are in favour of the repeal and that it has simplified matters considerably.

“Of course, everything gets easier when you don’t have to worry about that aspect. It is easier to carry out a transaction to ensure a sensible generational change.”

He does not believe the number of business transfers has changed, since other factors are more significant in that connection. However, according to Williamsson, it is possible that generational changes are being made earlier than they used to be.

The long-term effects are difficult to assess. From the perspective of Williamsson’s employer, the simplifications are a drawback, since more people can carry out generational changes without help. However, their clients want assistance with other matters instead, unrelated to inheritance tax, which are becoming more important.

RAOUL SVENSSON, ATTORNEY, VINGE, GOTHENBURG

Svensson said that planning from the tax angle has disappeared entirely. Businesses do not have to plan as extensively nowadays and generational changes are often carried out in connection with estate distributions. More people are choosing to return home from abroad and move their assets back to Sweden. The repeal of the inheritance and gift taxes combined with the repeal of the wealth tax is one reason for this development.

“Advance planning is unnecessary. Tax planning related to a future death used to involve a lot of pre-emptive measures that people don’t have to take anymore.”

He also surmised that people who might otherwise have moved assets back to Sweden may choose to remain abroad due to the political risk surrounding the possible reinstatement of the wealth tax.

STAFFAN SUNDKVIST, PARTNER, ÖHRLINGS PRICEWATERHOUSECOOPERS

Sundkvist described how the repeal has simplified estate distributions. Many of the effects generated by the inheritance tax could be reduced, which, in a sense, made the tax voluntary. However, the inheritance tax did entail planning costs, which had negative impact.

“Capital that would otherwise have gone for taxes is staying in companies. I am certain Swedish enterprise has gained stronger companies since the repeal than we would have if the inheritance tax were still in effect.”

One possible drawback to the repeal might be that estate distributions are sometimes not planned in time, according to Sundkvist. He also related that fewer businesses are staying within the family these days, since in his experience the younger generation are not as interested in taking over. Sundkvist believes this trend may be a function of structural transformations in terms of the transition to a larger service sector. The inheritance, gift and wealth taxes should be regarded as a package; according to Sundkvist, having only one of the taxes distorts the system.

AN ATTORNEY IN KARLSTAD

In this attorney’s view, the repeal has affected all legal work in connection to estate distribution and has simplified matters to a relatively great extent.

“Quite a few transactions have been made easier, since people no longer have to consider the tax consequences of the former inheritance tax.”

The attorney has noted no impact on the nature of business transfers, other than that the repeal has generally facilitated planning in relation to tax consequences. Nor has the attorney felt any significant impact of the wealth tax on business transfers, since the law firm has done little work on matters related to wealth tax.

A PARTNER IN AN ACCOUNTANCY FIRM IN STOCKHOLM

This individual related that repeal of the inheritance and gift taxes has had relatively little impact on the firm's operations, since other factors are often more germane to generational changes and business transfers. The individual stated that planning for tax consequences was a great deal more common before the repeal.

“Everybody profits by clearer rules and regulations. If you know there will be no tax on the estate, of course it makes your scope for action more secure. That has to be a good thing in all kinds of situations.”

The individual said that it is hard to judge whether the number of business transfers has changed due to the repeal. This partner in an accountancy firm believes that the impact is felt most by tax attorneys and that it is difficult to assess whether the nature of business transfers has changed.

“Entrepreneurs have a tendency to be passionate about their businesses. It is a lot easier to plan a transfer now, since people can choose when it will happen, perhaps more freely and easily than they could before.”

With regard to the wealth tax, this individual thinks the repeal has had beneficial effects, since more capital can remain with the entrepreneurs, who can use it to start new enterprises or build up existing ones.

A LAWYER IN VÄXJÖ

The repeal has simplified estate inventories from the adviser's perspective. According to this lawyer, people no longer have to waive their inheritance rights for tax law reasons related to the inheritance tax.

People used to have to spend resources to create various avenues to reducing inheritance tax, such as endowment policies and their proceeds. A great many of these structures have fallen by the wayside due to the repeal.

“In my opinion, the main impact is that focus is now being put on more important things than tax.”

The lawyer related that focus on inheritance and gift tax often caused people to overlook the problems related to income tax law that are intertwined with inheritance and gift tax. The lawyer was adamant that the repeal was beneficial from the macroeconomic perspective.

Before the repeal, it was probably more common for certain businesses to remain in the family, and the gift tax was shifted to an inheritance tax instead.

“In practise, it was cheaper to bequeath the money than to give it away while you were still living, even though the differences were not immense.”

The lawyer believes there has most likely been a marginal increase in the number of business transfers. The lawyer also believes people are choosing to handle more themselves now than in the past, when they commonly retained an expert. Moreover, according to this lawyer, generational changes in businesses are more often being carried out in a timely manner now. As a result, business owners are getting younger, which benefits the national economy.

A TAX CONSULTANT IN GOTHENBURG

The tax consultant described how the firm used to work more with generational changes than they do now, in part because the advisory services market has contracted sharply due to the repeal.

“As far as I can see, queries related to generational changes have generally declined.”

The tax consultant maintains that the nature of generational changes in businesses has changed, in that people are carrying out these transactions unassisted more often than they used to. There were some initial concerns that repeal of the inheritance and gift tax would lead to abuses of other regulations, but the tax consultant has not found this to be the case since the repeal.

A MANAGING DIRECTOR OF A LAW FIRM IN STOCKHOLM

This lawyer said that the repeal has generally facilitated and simplified business transfers and transfers of ownership.

“It has made things considerably easier for everyone involved. Not everyone is aware that the inheritance tax is gone, and some people are under the impression that it is still in effect.”

The lawyer further related that before the repeal, some law firms helped clients move and reduce visible assets to reduce the tax burden. Initially, some assignments disappeared and the market shrank. Ultimately, the market dried up entirely. When asked what a reinstatement of the inheritance and gift taxes would mean to the firm, the lawyer answers:

“It would mean more work for us, but that is something we neither want nor support.”

With regard to the wealth tax, the repeal has made things simpler, but has also reduced the firm's market. Overall, the repeal of the gift, inheritance and wealth taxes has simplified matters for private individuals and their market.