The Chelsea Guide to
Venture Capital Trusts

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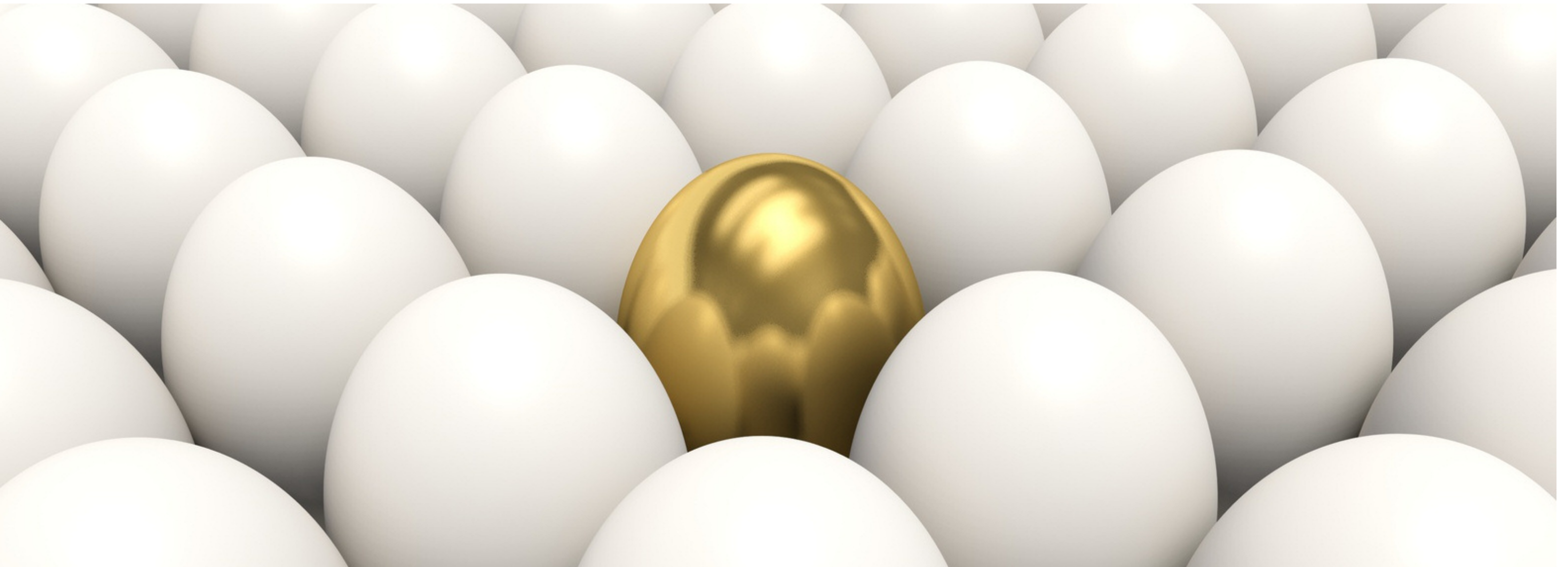

Introduction

Venture Capital Trusts (VCTs) celebrated their 20th Anniversary in 2015. They can be helpful to both higher net worth clients who have already filled their personal ISA and pension limits, and investors seeking an alternative source of income, who are willing to take on some extra risk with their capital. This is because they offer an attractive tax-free dividend, as well as income tax relief and no capital gains payable. The average VCT is currently paying an average yield of 8.2%, with the average generalist VCT yielding 8.8% and the average AIM VCT yielding 5.6%*. This guide explains the product in more detail.

*Source: AIC, 20th April 2015

What are VCTs?

Venture Capital Trusts (VCTs) were created in 1995. They are investment trusts, so are listed on the London Stock Exchange, and generate returns by investing into smaller companies which are looking for capital with which to develop their business.

VCTs are a product for the sophisticated investor, who is able to take a long-term view (at least five years) as they expose that investor to greater risk than some other investment products. In order to encourage potential clients to take on this risk, they offer attractive tax breaks.

What are the characteristics of a VCT?

- A VCT must be listed on the London Stock Exchange.
- It must derive its income wholly or mainly from shares or securities and it can retain no more than 15% of this income. Any income in excess of this must be returned to shareholders.
- No single holding can represent more than a 15% share of the overall portfolio value.
- A VCT must also have invested at least 70% of money raised within three years into either qualifying companies or shares.

What are the tax benefits into VCTs?

There are a number of tax benefits with VCTs.

The main benefit, in the eyes of most investors, is that you can receive 30% income tax relief on investments up to £200,000 (the limit for this financial year). However, in order to receive and keep this tax relief there are three conditions:

The first is that you must purchase new shares in VCTs. You cannot get this tax relief if you buy shares in VCTs on the secondary market (if you buy an existing VCT investment from another investor, rather than a VCT company).

Secondly, you must have already paid the equivalent amount, or more, in income tax that year. For example, in order to claim back £15,000 from a £50,000 VCT investment, you must have paid at least £15,000 in income tax that year. If you have only paid £10,000 in income tax you can only claim back that amount.

Finally, you must hold shares in the VCT for at least five years to keep the income tax relief; if you sell before this point, you will have to pay it back.

Other tax benefits include; no income tax being payable on dividends received from the VCT investment, no capital gains tax being payable upon the sale of the VCT and gains within the VCT being free from corporation tax.

What are the different types of VCT?

There are four different types of VCTs available:

1. Generalist – These cast a wide net to find investment opportunities in companies at various stages of development, in all sorts of different sectors. These are arguably the most popular form of VCTs.
2. Specialist – These find companies to invest in within one specific sector. These are not as common as they have been in the past.
3. AIM – These invest into companies which are, or are about to be listed on the AIM market.
4. Limited Life – At the lower risk end of the VCT spectrum, these aim to invest capital and then wind up within five to seven years. This is a guideline time horizon however, and not a guarantee.

What are the drawbacks of VCTs?

Although investing into smaller firms offers the opportunity for a higher return, it comes with a much higher risk.

The value of the VCT can go down as well as up, meaning it is possible to get back less than you have invested.

Shares can also be difficult to sell and the market price of what you are selling does not always reflect the real value of the assets.

What are the charges?

There is usually an upfront charge of 5.5%, which is reduced if you choose to invest in a VCT on an execution-only basis via Chelsea. The annual running costs of a VCT can be high but are usually capped at 3.6%. Annual costs include Directors' fees, fees for taxation advice and registrars, any trail commissions payable to the sponsor and broker as well as the Investment Manager's fee.

As is customary in the venture capital industry, the manager will be entitled to receive a performance-related incentive based upon returns made to shareholders. These can vary greatly from manager to manager, so it is worth reading the criteria for each one carefully before investing.

How do I invest?

Before you invest, make sure you understand the risks and rewards of investing in this product. Also, be assured that you have the time horizon to hold the shares in a VCT company for at least five years to ensure that you can benefit from the income tax relief.

You can find more information about VCTs and current VCT offers on our website at: https://www.chelseafs.co.uk/products/vct/offer

If you need any further information, would like to request application forms, or have any questions then please get in touch with us on 020 7384 7300 or e-mail us at info@chelseafs.co.uk