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Newer Venture Capital Trusts: A Stronger Option for Clients

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VCTs: An Established and Mainstream Investment Vehicle

If you're looking for a well-established tax-efficient investment vehicle to recommend to clients with a range of tax-planning concerns, a Venture Capital Trust (VCT) is the obvious starting point. VCTs have been in existence for nearly 30 years, and were launched to encourage support for new and growing firms while offering investors a range of advantageous tax breaks. To offset the investment risk, VCTs offer 30% Income Tax relief (minimum holding period five years); gains exempt from Capital Gains Tax on sales of shares; and no Income Tax on any dividends.

Over the years, they've understandably become more popular with investors, reflected in annual subscription amounts. According to the Association of Investment Companies (AIC) , VCT fundraising passed the £1 billion mark for the second time in the 2022/2023 tax year, reflecting the continued appetite for VCTs among UK investors. And with tax mitigation always high on the agenda, VCTs continue to feature in client portfolios.

The VCT Universe

Naturally, given the history of VCTs there is a wide range of offerings within the VCT investment landscape to choose from. Many older VCTs have been operating since the mid-1990s, while a steady stream of newer VCTs has been launched in the last few years. With all VCTs subject to HMRC's strict criteria, investors may want to consider some of the structural reasons for choosing newer VCTs over their more mature counterparts.

Older VCTs will contain a portfolio of mature holdings which might, on first glance, appeal to investors. However, one possible drawback of investing in these vehicles are the management fees which could impact future returns.

For example, many older VCTs will have long ago passed through their hurdle for performance fees, which could dilute future growth for both existing and new investors. In contrast, newer VCTs will still need to surpass their hurdle before a performance fee is payable, rewarding those investors with a greater share of the growth.

Capital Deployment Timeframes

It's also worth noting that a new VCT has three years to deploy a minimum 80% of its capital into qualifying companies, and that of funds raised in any one year, at least 30% have to have been deployed by the end of the next year. This gives the VCT's investment managers more time to assess deals, and gradually build a diverse portfolio of firms with strong growth prospects.

Built-In Diversification

An important aspect of newer VCTs is that they can help bring greater diversification into an investor's portfolio. Most VCTs will have this effect, by giving investors exposure to smaller companies. However, as many newer VCTs invest in tech-enabled firms, investors can achieve better diversification. As VCT investment teams invest at varying stages of growth, and across multiple sectors, this can help to add more layers of diversification.

Adding a newer VCT of this kind to a portfolio of existing mature VCTs can also increase diversification. This is through holding investments at different stages of maturity, with different VCT managers, employing different strategies.

Enhanced Dividend Prospects

Investing in a newer VCT can often amplify the potential for dividend payments. These could include special dividends from early exits along with the objective of paying regular dividends in the future as the VCT matures.

Investments with a Positive Impact

As client demand for investments that apply environmental, social and governance (ESG) considerations grows, another benefit of newer VCTs is that they have a greater tendency to support firms making a positive impact. For example, within the realm of tech-enabled firms, investee companies are often more likely to score well on ESG factors. Many of these firms, spanning sectors from health to education, offer solutions that can change the way we live and work for the better. And in terms of their own operations, they will be working with ESG at their core.

Beyond the advantages of investing in portfolio companies with a positive ESG impact, there's also a broader ESG impact from new and growing UK companies. These companies are working to help strengthen the future UK economy through creating jobs and generating much-needed tax revenue. They are also helping to ensure the UK remains a world leader in business, particularly in the area of innovation.

Choosing the Right VCT Manager

When considering which VCTs to recommend to clients, advisers may find it worthwhile looking beyond the traditional VCT houses and towards those VCT managers applying a fresher and more client-focused approach. Those that offer value-based fee structures, clear technology mandates, tax-efficient expertise and a commitment to ESG, will be best placed to support advisers and deliver the best outcomes for their clients.

Solutions for Investors and Support for Advisers

Blackfinch is a tax-efficient investment specialist working in partnership with advisers to meet clients' requirements. To find out more please speak to one of our team on **01452 717070** or email **enquiries@blackfinch.com.**

IMPORTANT INFORMATION

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