Learning outcomes: 1. The various tax breaks available on VCTs 2. The different type of investment mandates available 3. The risks and rewards of investing in VCTs Tutors on the panel are: Anthony Yadgaroff, Managing Director, Allenbridge Tax Shelter Report Douglas Lawson, Director, Amati Mike Piddock, Head of the VCT Business Line, Octopus Investments Ben Yearsley, Head of Investment Research, Charles Stanley Direct PRESENTER: In order to consider the viewing of this programme as structured CPD, you must complete the reflective statement to demonstrate what you've learned and its relevance to you. Venture capital trusts are closing in on their 20th anniversary but are they as relevant today as they were back at launch; when John Major was prime minister, Barings Bank collapsed and Frank Bruno won the world boxing championship? I'm Mark Colegate and in the course of the next 30 minutes I'll be looking at how the concept has developed and what it can offer today's investors. I began by asking Anthony Yadgaroff, managing director of the Allenbridge Tax Shelter Report, who has been looking at tax efficient investments since the 1980s, for the background on the VCT. The origins of the VCT market ANTHONY YADGAROFF: VCTs started in 1995. Originally there was the concept of the business expansion scheme, which started in 1983. The problem with business expansion schemes, there was no market and people had no way of getting out. So government came up with this concept of having an investment trust, so you had a quoted vehicle. PRESENTER: What were they intended to do when the concept originally launched? ANTHONY YADGAROFF: The concept was to fund SMEs. There was a funding gap for small companies, government wanted to support smaller companies, investors wanted to invest in vehicles to provide capital, and this way they got tax relief, and government got funding for smaller companies. PRESENTER: So has the concept of tax breaks to investors in exchange for funding worked? Has it delivered for investors, government and taxpayers? I began by asking Douglas Lawson, director at VCT provider Amati. DOUGLAS LAWSON: Well first of all for investors it's been something of a mixed bag. So many of the early VCTs invested heavily into early stage technology companies, and when the dotcom bubble burst, those VCTs suffered quite badly. Since then I would say that most VCTs have taken a less risky approach to investment, and the returns more recently have been pretty good, and they're now a very good source of income. For the government, I think VCTs have done what they've intended to do. There is pretty good evidence that VCTs have replaced other sources of funding, and for the taxpayer, there's also pretty good evidence that venture capital trusts have stimulated growth and employment, and the AIC estimates that for every one pound of venture capital trust money, six pounds of new turnover has been generated. ANTHONY YADGAROFF: Yes, I believe over £5bn has been raised since 1995. Job creation's difficult to work out; anything between 14,000 and 40,000 is what has been quoted. For the Government, they've got funding for smaller businesses, corporation tax, PAYE, VAT, substantial benefits for the Government. And also for investors, they've got an average of a tax free return between 5 and 8%. Government commitment to the VCT PRESENTER: Given that track record, is the Government still committed to the VCT - not just today but for the future? I caught up with Mike Piddock, head of the VCT Business Line at Octopus Investments MIKE PIDDOCK: I think the Government's very committed to VCTs. If you look at the changes that they've made to the legislation over the last few years, these have generally been positive. They've increased the size of the companies that VCTs can invest into, whether that's the number of employees or the size of the investments that can be made into those companies, so all of the intentions from the Government are pointing in the right direction. PRESENTER: Where's the proof that VCTs are really working for government? MIKE PIDDOCK: Well if you take one of our VCTs, our Titan VCTs, when they invested, the companies they invested into were employing 300 people. Around two years later, they're now employing 1,100 people. So VCTs are creating jobs for the UK economy. PRESENTER: But is it a concern that some VCTs are really operating as a tax shelter rather than investing in small companies? MIKE PIDDOCK: I think VCTs have a great track record of investing in small companies. You only have to look at the likes of Zoopla and Secret Escapes, which are two

companies that are really doing well, and they've been VCT backed. Now some VCTs do focus on capital preservation, and they do look to focus on the tax break as well as the underlying investment, but the vast majority of VCT money is going into small companies which are supporting the UK economy. DOUGLAS LAWSON: I think VCTs are still very relevant today. There remains a shortage of bank finance for very small companies. VCTs tend to invest in the areas of the market that traditional private equity funds and traditional fund managers would not invest, because it's too small. And whilst other sources of funding have appeared, such as crowd funding, crowd funding tends to be from much smaller companies, early stage startup companies, whereas VCTs tend to target the next stage of a company's growth, so I think they remain very relevant today. PRESENTER: How committed to the VCT is the Government? DOUGLAS LAWSON: I think the Government is very committed to VCTs for the future. Over the past few years they've made some changes to the legislation, for example what constitutes a qualifying company, and other legislation to do with the structure of venture capital trusts, but I think that as long as venture capital trusts focus on doing what they were originally intended to, which is to provide finance to young British growth companies, I think the Government will remain very supportive. The tax breaks and allowances on VCTs PRESENTER: So there's a tax story and an investment story here. Let's look at the former. First of all, what are the tax breaks and allowances for a VCT investor, here's Mike Piddock MIKE PIDDOCK: When you invest into VCTs, there are three tax breaks. There are tax breaks at the start of the investment, during the investment and when you come to exit. First of all, you get 30% income tax relief on your investment, up to an investment of £200,000. Secondly, you get tax relief on dividends, so the dividends that the VCTs pay, you don't pay tax on. And thirdly, when you come to exit the VCT, you don't pay any capital gains tax on the growth in that VCT. PRESENTER: And are there any tax breaks within the VCT itself? MIKE PIDDOCK: So a VCT is just a form of investment trust. So the VCT itself has the same tax breaks that investment trusts would have. So it doesn't pay corporation tax on capital, it just pays it on income. PRESENTER: But how long does an investor have to hold on to a VCT to get all their tax breaks? I asked Ben Yearsley, head of investment research at Charles Stanley Direct BEN YEARSLEY: The minimum time period is five years for the income tax relief, the 30% income tax relief, and if you sell it before the end of the five year period you have to repay it. To get tax free dividends and tax free growth that's just an ongoing, you'll get that however long you're invested; the minimum time period is purely for the income tax break. PRESENTER: And is there much of a secondary market for VCTs? BEN YEARSLEY: Yes and no. It has been dreadful, or it certainly was dreadful for a long time. VCT managers and boards have made a concerted effort to improve the secondary market, have more liquidity, bring in discounts, and it's definitely improved; however at this current time there isn't a huge amount of secondary market trading. Now one caveat to that as VCTs are now getting larger, I mean you've got quite a few VCTs in £70-80m size now, compared to maybe five years ago, ten years ago when the biggest were about £30m. They are now attracting more interest from investors and actually as VCTs get bigger you've got more chance of developing a proper secondary market. PRESENTER: But is it basically you can't take the tax breaks in the secondary market? BEN YEARSLEY: In the secondary market you get the tax free dividends and tax free growth; you don't get the upfront 30% income tax break. However obviously most VCTs trade on a discount, some of 5-10%, some of 20% plus. So you can actually pick up VCTs in the secondhand market with a bigger discount than the initial tax break you're foregoing. PRESENTER: And who exactly can invest in VCTs? BEN YEARSLEY: Anybody over the age of 18 can invest in VCTs. In order to get the income tax break you obviously have to have paid sufficient income tax; you can't claim back more tax than you're due to pay in a specific tax year. So anybody over the age of 18 can invest up to £200,000 per tax year, giving you a maximum reclaim of £60,000 if you've paid enough income tax. VCT qualifying assets PRESENTER: But to get the specific generous VCT tax breaks for investors, the trust has to invest in qualifying assets. MIKE PIDDOCK: A VCT has three years in which

to invest the money that it raises in qualifying assets. But it only needs to invest 70% of that money into qualifying assets. But once it reaches that point, it needs to stay above 70%. PRESENTER: And what exactly constitutes a qualifying investment – here's Ben Yearsley again. BEN YEARSLEY: There are a whole raft of rules and regulations that managers have to abide by. Some of them are relevant or dependent upon when the money was raised into the VCT. But as a general rule of thumb now for new money the companies themselves can have gross assets of no more than £15m, so relatively small, but not start-ups necessarily. They can't have more than 250 full-time employees and quite crucially they can only receive £5m of state aid. Now effectively a VCT or an EIS investing is classed as state aid. Now there are some sectors that you can't invest in, for example hotels, and also you can't invest in companies that get FITs payments, i.e. payments linked to some of the renewable tariffs out there, but it leaves you a whole swathe of areas you can invest in. But that the main rules are around the size of the company and with a few sectors that you can't invest in. PRESENTER: But if I invest in a company, it does fabulously well, gets to 500 employees say, does that suddenly become a non-qualifying investment or can you hold onto that? BEN YEARSLEY: No, the qualifying status is only at the time you invest money in the business. PRESENTER: And what do VCTs typically put into the non-qualifying element of their portfolio? BEN YEARSLEY: So first of all a VCT ha to invest 70% of its assets in qualifying investments as a minimum after three years. Now in theory the manager can put the full 100% into qualifying investments, so some might not use any non-qualifying investments at all - that's quite rare. So the 30% that could be non-qualifying is often in a mixture of cash, could be bonds, could be unit trusts. There are some managers that use unit trusts. It could be other shorter term investments that are non-qualifying in nature that can provide a healthy return, for example some effectively do almost bridging loans to some companies, so a high rate of interest on a short term secured on a specific asset. Others might put unquoted investments, for example actually good example is Esure the insurance company. That was actually held in a couple of VCTs as a non-qualifying investment that was clearly too large, but the manager thought it was a good opportunity, bought into it and added that into the portfolio as a non-qualifying company. So managers use it in very different ways. PRESENTER: But as an investor should you get worried if somebody's got 30% in non-qualifying investments, on the nail, and it only takes a little move in markets and suddenly you're in trouble. BEN YEARSLEY: Don't get too hung up on the move in markets, because the qualifying level isn't necessarily the same as the market value today, so don't get too hung up on that. However, your point is valid in that most managers will look to have generally at least 80% in qualifying investments to give themselves some leeway, so when they're selling an investment they're not breaching limits or anything else. It's when you run too close to the 70% limit you do come into a few troubles. And one VCT recently actually decided to pay an early dividend, because it was a bit concerned that it was getting too close to the 70% test and decided it was better to pay some cash out now rather than wait another six months just to be on the safe side. So most managers will try to have at least 80% in qualifying to ensure that there's sufficient headroom for when they make new investments or when they're selling investments unexpectedly or whatever. PRESENTER: And what's the danger a manager can't get all of the money raised into qualifying investments in time? DOUGLAS LAWSON: Well recently the pipeline of qualifying deal flows has been very strong, so that hasn't been a risk for us, but in the past there's been a relatively limited number of companies looking for finance. When that happens, what you have to do as a manager is become much more proactive about going out and finding deals, and in 2009, when there was a dearth of deals coming to the market, we approached companies and offered financing. PRESENTER: So has a VCT ever had its status withdrawn? BEN YEARSLEY: This is obviously a hot topic at the moment, because it's happened for I believe the very first time quite recently. And the upshot is from an investor's point of view you lose all the tax breaks from this point onwards. So if it happens within five years of you investing you have to repay the income tax back. And from this point onwards

when you lose it you no longer qualify for tax free gains or tax free dividends. So it is actually quite a big problem. It's only happened once, or with one manager, and I think that's probably a wake-up call to other managers to actually say the Revenue, HMRC, will be taking a hard line with managers who breach the rules. VCT tax breaks vs pensions and Isas PRESENTER: Given the tax breaks on offer via VCTs, how do they compare with the other tax breaks that investors in the UK can look to: namely pensions and Isas? ANTHONY YADGAROFF: Yes. As there's very limited pension contributions one can make, and small contributions to individual saving schemes, VCTs have a role to supplement your pension contributions. DOUGLAS LAWSON: There are a number of tax differences between a venture capital trust, an ISA and a pension. The first one to mention is that there is income tax relief on a venture capital trust at 30% on the amount that you invest, on an ISA there is no initial income tax relief, and with a pension the income tax relief will be at your marginal rate of tax. The other thing to say is that they have different maximum investments per annum. For a venture capital trust it's £200,000; for a pension it is £50,000, which is falling to £40,000 from tax year 2014/15. The other difference is with lifetime allowances, which are unlimited with VCTs, whereas with pensions the lifetime allowance is £1.5m, which will be falling to £1.25m from tax year 2014/2015. PRESENTER: With all these tax breaks and reliefs – does an investor have to declare it on their tax return? BEN YEARSLEY: Yes. So to claim the income tax back you either do it via your Self Assessment at the end of the or after the end of the tax year, or you can actually get your PAYE coding changed during the tax year to actually get your income tax back during that tax year. Dividends however when you receive them don't have to be declared at all. So your dividends you get you can bank, don't need to worry about that in the slightest, don't need to go on your tax return, no further tax to pay. The risk reward characteristics of VCTs PRESENTER: That's the tax position of VCTs, but what about the underlying investment? They typically invest in pretty small companies – what are the risk and reward characteristics? DOUGLAS LAWSON: VCTs tend to invest in quite small companies. That certainly applies to 70% of the VCT fund, which has to be invested in what is called qualifying investments. As an example, we invest in a company called Martin & Co, which is a UK residential lettings franchisor, and when we invested in that company the market capitalisation was around about £22m. Another example is a UK engineering company called AB Dynamics. When we invested in that company the market capitalisation was about £14m. In terms of the other 30% of the venture capital trust, we're unrestricted in terms of what we can invest in, and some VCT managers, for example Amati, choose to invest that portion of the VCT in larger more liquid small and midcap companies. PRESENTER: How great a risk is liquidity in a VCT portfolio? DOUGLAS LAWSON: Liquidity really needs to be provided by the VCT itself. There's a limited secondary market for VCT shares, and that's because if you buy VCT shares on the secondary market, you don't benefit from the income tax relief, so most fund managers will have a buyback policy for their VCTs. For example ours is that we will buy back shares at a 5% discount to net asset value. PRESENTER: And how risk does Ben Yearsley of Charles Stanley think they are compared to mainstream equity investing? BEN YEARSLEY: This is one of the hardest questions to answer. If you go by the rule book effectively they are classed as very high risk investments for a whole variety of reasons. And you have to point out from a liquidity point of view to investors they are high risk. There's very little secondary market, we've already talked about this improving, but it's still not there. When you sell, if you've got a large holding you might not be able to sell, so from a liquidity perspective these are high risk. From a size perspective as well the high risk world they invest in some of the smallest companies around, not necessarily start-ups, but some of the smallest companies. However, managers to do a lot of work into the structure of the underlying deals to try and reduce the risk where possible and has put a lot of say for example debt into a company rather than buying pure equity so that they get first call on the assets of that company if something goes wrong. And also that debt provides ongoing income streams into the VCT as well. So you're reducing the underlying risk by getting payments back on a

regular basis. So the managers are aware of that and trying to structure a lot of the deals where possible to mitigate the risk. They can't minimise the risk, but they can certainly help mitigate it. PRESENTER: But what happens if one of the investments in a VCT goes horribly wrong? What are your options as a fund manager? DOUGLAS LAWSON: Well there are certain things that you can do to try to protect against that eventuality, and clearly the first one is to do very rigorous due diligence before you invest in a company, but the nature of small company investing is that it's risky and things can and do go wrong. One of the benefits of an AIM VCT is that you have the opportunity to exit your position, subject to liquidity, if you feel that the investment case isn't panning out as you'd hoped. The other mechanism that we use to derisk the investment proposition is that we occasionally invest through something called a convertible loan, and a convertible loan is an instrument that converts into equity if we choose; if not, then like any debt instrument, it repays at the end of a fixed term. PRESENTER: How global are the investment portfolios of VCTs, or are you really just buying into UK PLC? DOUGLAS LAWSON: It's really still about buying into UK companies, but many of those companies export abroad. So we've done some analysis on our portfolios and we estimate that between 55-60% of the revenues of our portfolio companies combined are to export markets. PRESENTER: When you look to invest in a company, do you also look to take a seat on the board? DOUGLAS LAWSON: When we're investing in a company, we do often either take a seat on the board or reserve the right to take a seat on the board. So I think the way that we approach AIM VCT investing is that it's something of a hybrid between venture capital investing and public markets investing. So whilst we're investing predominantly in public companies, we tend to take an approach which is a bit more proactive than you would normally expect from an investor in listed companies. The income characteristics of VCTs PRESENTER: And given that this all sounds pretty growthy – for want of a better word – how should investors consider the product? DOUGLAS LAWSON: I think probably an income product more than anything else; VCTs tend to pay out capital gains that they've made as dividends which are tax free in the hands of the investors. PRESENTER: So what sort of yield can you get from a VCT these days? How does it compare with what's available elsewhere? BEN YEARSLEY: You're getting from a lot of VCTs a very consistent 5% these days. So you put your £10,000 in and you're getting £500 a year in dividends, and you can pick a whole raft of VCTs that are paying dividends of that level. Now that doesn't take into account the tax relief. So if you bear in mind that your £10,000 only cost you £7,000 once you've taken 30% tax back your £500 is actually the effective yield is actually much higher than that initial 5%. You can also then factor in other things like the fact that income from other products would be taxable and a VCT from an income point of view stacks up very well. And actually my view and this has been the case for a long time now is that VCTs are an income producing asset. They're not a capital growth product; they're an income product. There are other investments out there you can clearly get 3-4% from mainstream equities, you can get 3-4% from investment grade bonds, you can get 5% from high yield bonds etc., so VCTs do stack up very well from an income perspective with or without taking into account the initial tax break. The main types of VCTs PRESENTER: VCT is a pretty catch all term – what are the different types of product underneath this single banner? DOUGLAS LAWSON: People talk about VCTs in three broad categories. There are generalist VCTs, which invest in private companies, limited life VCTs, which as the name suggest, try to wind up after the initial five year period, and AIM VCTs, which invest on companies quoted on the alternative investment market of the London Stock Exchange. MIKE PIDDOCK: So generalist VCT means that that VCT doesn't have to invest in any particular sector. So it has a broad investment remit. It's not tied to say solar or technology, and so the managers have the maximum scope of investments from which to pick from. PRESENTER: What are the key characterises of a limited life VCT? MIKE PIDDOCK: So a limited life VCT looks to exit its investments after the five-year period and return the funds to shareholders. It's different to an evergreen VCT, which will continue fundraising and continue investing over an ongoing period. PRESENTER: Limited life VCTs

are, however, very much on the wane. Why is that? BEN YEARSLEY: The rules changed. The Revenue got fed up, HMRC effectively got fed up with giving aid to businesses that weren't really there to help growing small - I mean take a step back what were VCTs set up for, to help small entrepreneurial businesses. The rules were quite wide. Over the years those rules have been exploited – fairly within the rules because they were allowed to – to invest in a whole range of businesses that weren't really within the spirit of the original legislation. And effectively HMRC got a bit fed up of that and cracked down and said right we're tightening the rules, and that killed off a large part of the limited life VCT space for new investment, to try and refocus it on what the legislation and what the product was supposed to be set up for in the first place, which was the smaller entrepreneurial growing businesses. PRESENTER: And what are the pros and cons of so-called specialist VCTs, for example just investing purely in tech or healthcare? BEN YEARSLEY: Again these seem to have died in popularity as well actually. So you go back ten years to the early noughties, specialist VCTs were quite popular. Certainly as you say tech and healthcare were probably the two main areas. That then got superseded to a degree and actually the specialist ones now tend to be the renewable energy ones, so investing in solar, hydro, wind, anaerobic digestion etc. So you don't tend to get new VCTs doing the tech and the healthcare so much anymore. So I suppose the question now is what's the point of renewables, and actually renewables now give you a very secure inflation-linked income stream, whereas the tech and the healthcare you're clearly investing for high growth, but a lot of managers, you know, they've moved away from that space now and you don't seem to see them now in terms of arranging new money. VCTs focused on Aim stocks PRESENTER: Amati, has a particular focus on the AIM Market. I asked Douglas Lawson what sort of sized company he typically invested in. DOUGLAS LAWSON: The most important thing to say about AIM VCTs is that they invest in a basket of stocks that are predominantly listed on the alternative investment market of the London Stock Exchange. And as people will be aware quoted equities have had quite a strong run over the last couple of years, and as a consequence AIM VCTs have done quite well. What I would say is that, whilst certain areas of the market are starting to look quite expensive, we're still finding good value in AIM quoted companies. PRESENTER: And what's behind this pipeline of companies coming to AIM at the moment? DOUGLAS LAWSON: I think the reason for that is that, because the markets have been relatively quiet over the last few years, there's been a big pipeline of companies that's built up, and now that the markets have improved, the brokers are picking the best companies from that pipeline and bringing them to market. PRESENTER: Do the earnings from AIM stocks justify the valuations they're on? DOUGLAS LAWSON: I think they do. I mean you would expect many of the AIM companies that we look at to produce earnings growth in excess of larger companies, and we look very closely at something called PEG ratios, and that's where you look at the P/E ratio of a company relative to its earnings growth, and on that measure AIM continues to look like reasonable value to us. PRESENTER: And what about the lack of M&A activity in the markets; is that supportive of AIM, or does it have no effect? DOUGLAS LAWSON: The lack of M&A activity in the market has definitely contributed to some of the underperformance of AIM. You would expect some small company performance to come from takeovers by larger companies, and M&A has been largely absent from the market over the last few years. We think that's going to change over the next year, and the reasons we think that's going to change are because first of all companies have very robust balance sheets and secondly they're being put under more pressure by shareholders to deploy that cash, either by investing in new capital equipment or by acquiring smaller companies. So we think that should be a good driver of performance on AIM over the next year. PRESENTER: What are the opportunities for alpha generation in the AIM index, as opposed to say the FTSE 100? DOUGLAS LAWSON: There are good opportunities to generate alpha in the AIM market, because the market is far less researched than the FTSE 100, for example. What that means is that it's less efficient and there are fewer brokers covering stocks; there's less knowledge about companies quoted on AIM. So if you're willing to do the

work and to build your own financial models and come to your own view about forecasts and valuations, then you can often find anomalies on the upside and the downside. PRESENTER: How liquid's the AIM market? DOUGLAS LAWSON: The AIM market is less liquid than the main market of the London Stock Exchange; however it does provide us as managers of a VCT investing in AIM companies with some liquidity and with some flexibility in terms of exiting our investments or reducing our positions in certain investments; unlike private companies, where you normally have to wait for an exit event to realise your holding. PRESENTER: What's an acceptable P/E for the AIM market? Should it be higher than the main market? DOUGLAS LAWSON: Yes, you would expect it to be higher. So I would estimate that the weighted average P/E of our portfolio is probably in the high teens, but given we're looking at growth rates around the high teens, low 20 levels as well for many of these companies, I believe that that's acceptable. PRESENTER: So what are the main risks in VCT investing and how would a quality manager look to mitigate those? DOUGLAS LAWSON: Well investors will understand that they're investing in a portfolio of small companies, and small companies are by definition more risky than large companies. They tend to be more reliant on a smaller number of products or services; they tend to be more reliant on key people. So it's very important when you're investing in small companies to do very thorough, very rigorous due diligence. What you want to look for is a company that has strong barriers to entry, strong pricing power, which is also sustainable, and a strong balance sheet, so that if the company does encounter any shocks along the way, it can withstand those shocks. The costs of VCTs PRESENTER: All this specialism comes at a price – I asked Ben Yearsley how expensive they are and are they worth it? BEN YEARSLEY: This is one of my big bugbears at the present time, VCTs are expensive. Management fees of about 2%. You then have performance fees on top if the manager performs well. You have listing fees, because it's a listed company, so you've got the directors' fees, you've got other listing fees to do with that. You have co-invest fees effectively where the managers get to co-invest and take a bit of a fee out if the company does well. You have deal monitoring fees where the underlying companies pay the managers. And what it boils down to is VCT if you add all these fees together you are talking about probably 4% per annum. So for a VCT to deliver 6-7% it has to deliver a pre-fee return of about 11-12%. Now my contention actually is that there are two main levels of fees in many of these VCTs these days and actually the managers could be doing a lot more to try and give higher returns and actually reduce some of their fees in the long term. Whether they will do that who knows? Due diligence in picking a VCT provider PRESENTER: What are the sorts of institutions that offer VCTs? ANTHONY YADGAROFF: Well there are some managers who just do VCTs. There are other managers who do VCTs, EISs and tax shelters. Then you'll have a number of stockbrokers who will do VCTs, and some fund management groups. PRESENTER: And what should investors keep an eye out for in a VCT manager? ANTHONY YADGAROFF: Track record, proven exits, having good non-execs on their boards, a history of delivering returns to investors. PRESENTER: What sort of resources does a group need to be able to find companies to invest in from across the UK? ANTHONY YADGAROFF: I think it's very important that they have a good network that they can deal with firms of accountants, who can provide them with companies that are looking for funding. DOUGLAS LAWSON: I think the investor should look at the manager's track record, and I think the investor should look at how long the manager has been specialising in this particular area, because there are lots of pitfalls with investing in smaller companies. So I think you need a manager who really understands those pitfalls and how to deal with them. I also think it's important that you back a manager that has also invested in their own funds, and perhaps even invested in the management company running those funds. PRESENTER: How do you go about researching investment opportunities? DOUGLAS LAWSON: So investment opportunities come from two principal sources. First of all they come from corporate finance advisers and small company broking houses who have relationships with companies, and bring those companies to us when they're looking for finance, and secondly we source

companies from our own network. So we have a pretty good understanding of the companies that are already listed on AIM, and we have a good network of people who know private companies, we come across lots of private companies, and we have in the past offered those companies finance. VCTs as a complement to pensions PRESENTER: Given an investor can put £200,000 into a VCT in a tax year – just who are these vehicles suitable for? BEN YEARSLEY: Yes, I think two answers to this question. First one is you need to be investing for at least seven to ten years, so ignore the five year rule you should be looking at seven to ten year investments for these, and secondly with the minimum of £5-10,000 per VCT, and the fact you probably want a spread of them you do really need a portfolio of £100,000 plus to start considering VCTs. You should only probably put 5-10% of your portfolio in things like this. So if you'll be looking at adding in a new one every year, you probably need £100,000 plus already invested to be considering VCTs. Now again as a caveat to that there's a lot of people in the high earning bracket, say who've got £½m plus in their pension pot who might be worried about lifetime allowances that are actually turning to VCTs as an alternative now, because you can put this £200,000 in, you get the tax break today and you get the tax free income. So a lot of people now are actually looking at VCTs for that pot of money if they're worried about the lifetime allowance on pensions. PRESENTER: Could you reinvest that income? BEN YEARSLEY: Yes, you can reinvest it. Obviously any dividends reinvested would count towards your £200,000 limit for that tax year. If you're writing a cheque out for £200,000 a year and reinvesting your dividend separately you'll be over the limit. So you always need to bear that in mind if you are reinvesting. Lots of the managers have a reinvestment programme where they effectively issue new shares to you, but it does count towards your annual limit, so you need to be wary of that. The use of VCTs in an overall client portfolio PRESENTER: Should a VCT be considered because it's a tax break, or because it's an investment? MIKE: I don't think you can just look at a VCT as a tax benefit or as an investment vehicle, but look at the two together. So you get that 30% income tax relief because you are taking a risk. You're investing in smaller companies, which by their nature are higher risk than larger companies. So that tax relief is your reward for taking that risk. So to look at VCTs without the tax relief would be wrong, but at the same time we also have to look at the underlying investments. There are a wide range of investments held within the VCT structure, and you have to understand which you're picking and which is most appropriate for investors. DOUGLAS LAWSON: I think that investors should look at both. The tax break is important because it's an incentive to invest in an area of the market that's deemed to be more risky than investing in larger companies, for example, but the investor, prospective investor should look at the investment opportunity as well, which I think is quite exciting, because VCTs are backing some of the UK's most interesting young growth companies. PRESENTER: But what do VCTs add to an overall investment portfolio? Again, is it a tax break, an investment, or a bit of both? There isn't 100% agreement here. MIKE PIDDOCK: VCTs provide a number of things. First of all, they provide access to smaller companies in a very tax efficient structure. Secondly, those tax benefits, 30% upfront income tax relief, the growth is tax free and the dividends are tax free, and finally they add an element of diversification. ANTHONY YADGAROFF: I don't think it adds anything to a portfolio, a client's portfolio; it's not an asset class that one would put into a portfolio. VCTs are there to supplement your tax free income from your pension scheme or ISAs, and should not be considered a part of their portfolio construction. DOUGLAS LAWSON: I think VCTs add diversification; it gives you access to an area of the market that has very interesting growth characteristics. It gives you clearly tax advantages, income tax relief on the way in, and tax free dividends, and most VCTs will now provide a good source of income. MIKE PIDDOCK: I think 2014's an exceptional time to look at VCTs. For a start, there are some great companies out there, small businesses growing out of London and the rest of the UK, and they need the VCT backing to enable them to grow, so there's great opportunities, great investment opportunities. Secondly, the Government has increasingly been looking at pensions and reducing the tax efficiency of those vehicles; for example

the lifetime allowance has been reduced, as has the annual allowance. So as a result VCTs provide a great complementary solution to investors who've maxed out their pension limits. PRESENTER: And if you want further information on VCTs where's the best place to go? DOUGLAS LAWSON: I would recommend our own website, which is amatiglobal.com. I would also recommend the HMRC website, which has very good descriptions of what kind of companies a VCT can invest in, and what the limits are and the criteria are for investors. And I would also recommend the AIC website, which has some interesting statistics on VCTs. PRESENTER: So is a VCT a natural product for an adviser to be talking to their clients about? ANTHONY YADGAROFF: Yes. I feel that VCTs and EISs are a product that makes an IFA more sophisticated, if he can provide research and products to their clients. We are seeing a big trend from the private banks now, who are putting a lot of resource behind doing research, into analysing VCTs and EISs for their private clients. PRESENTER: And here's Ben Yearsley. BEN YEARSLEY: It gives them something different. It gives them exposure to small more niche parts of the economy that you might not get otherwise. It also gives you this, as we've already talked about, the income stream, this growing or this long-term tax efficient income stream that has actually proven to be pretty stable over the last few years, clearly no guarantees that will be the case going forwards, but managers have been trying to get the consistency there with the dividend payments as they finally realise what the product is all about. So it gives you diversity, it gives you access to these small companies, but it also gives you this hopefully long-term relatively consistent dividend stream tax free. Important information Information and opinions contained in this interview have been arrived at by Amati Global Investors. Amati Global Investors and Asset.tv Ltd. accept no liability for any loss arising from the use hereof nor make any representation as to their accuracy or completeness. Any underlying research or analysis have been procured by Amati Global Investors for its own purposes and may have been acted on by Amati Global Investors or an associate for its or their own purposes. Amati Global Investors is authorised and regulated by the Financial Conduct Authority. Information and opinions contained in this interview have been arrived at by Allenbridge Investment Solutions. Allenbridge Investment Solutions and Asset.tv Ltd. accept no liability for any loss arising from the use hereof nor make any representation as to their accuracy or completeness. Any underlying research or analysis have been procured by Allenbridge Investment Solutions for its own purposes and may have been acted on by Allenbridge Investment Solutions or an associate for its or their own purposes. Allenbridge Investment Solutions is authorised and regulated by the Financial Conduct Authority. Information and opinions contained in this interview have been arrived at by Octopus Investments. Octopus Investments and Asset.tv Ltd. accept no liability for any loss arising from the use hereof nor make any representation as to their accuracy or completeness. Any underlying research or analysis have been procured by Octopus Investments for its own purposes and may have been acted on by Octopus Investments or an associate for its or their own purposes. Octopus Investments is authorised and regulated by the Financial Conduct Authority. Information and opinions contained in this interview have been arrived at by Charles Stanley Direct. Charles Stanley Direct and Asset.tv Ltd. accept no liability for any loss arising from the use hereof nor make any representation as to their accuracy or completeness. Any underlying research or analysis have been procured by Charles Stanley Direct for its own purposes and may have been acted on by Charles Stanley Direct or an associate for its or their own purposes. Charles Stanley Direct is authorised and regulated by the Financial Conduct Authority.