Money Matters

NAVIGATING THE FINANCIAL LANDSCAPE

Winter 2017

Financial planning responds to seasonal changes

Pension transfers and the Annual Allowance in focus

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A warm welcome to the Winter edition of Money Matters.

Once again the Autumn and Winter period is one of Wren Sterling's busiest periods as clients return from their Summer holidays eager to make new plans for the remainder of the financial year. This is due in no small part to the raft of changes taking place in our market, which impact our clients and their plans.

In Money Matters we've looked at some of 2017's biggest issues; transfers out of final salary (or defined benefit) pension schemes as well as the rising importance of planning for long term care. April this year also saw changes to the Annual Allowance, which is causing advisers and clients to review plans to ensure they're aligned to new legislation and future goals.

As usual, we've gone beyond learning from our internal experts to some of our partners to help bring fresh perspective on related issues. Octopus Investments introduce Venture Capital Trusts (VCTs), 7IM's Justin Urquhart Stewart has some tips for limiting withdrawals from the bank of Mum and Dad and The Will Writing Company offers a concise piece on the importance of making a Will to ensure your legacy reaches the next generation.

I hope you enjoy reading Money Matters and please contact your adviser if you would like to discuss the content of any of these articles in more detail.

Yours sincerely,

Ian Halley
Chief Executive Officer
Wren Sterling

Managing the new Money Purchase Annual Allowance limit

As new pension drawdown options grow in popularity, earlier this year the Government implemented a change to the limit of how much you can pay into your Money Purchase Pension Scheme, reducing it from £10,000 to £4,000.

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There's a danger of unexpected tax bills as people may have little understanding of the limits, or the consequences of exceeding them.

What is the Annual allowance?

The Annual Allowance (AA) is the maximum that anyone can pay into a pension scheme in each tax year and obtain tax relief. This is currently set at £40,000. Think of this as the upper limit.

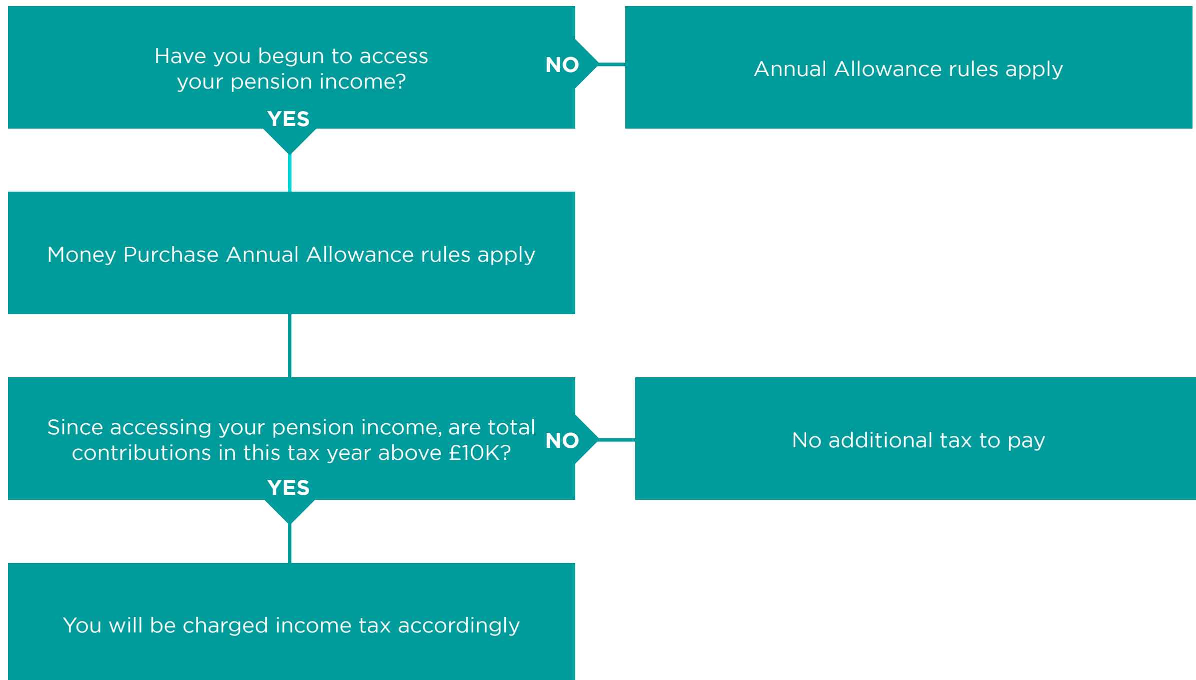
What is the Money Purchase Annual Allowance?

Generally, once a person accesses their pension benefits on a flexible basis, and takes an income from their pension pot, their AA changes to the lower Money Purchase Annual Allowance (MPAA). When it was introduced (at the same time as pension freedoms) in 2015 the MPAA was set at £10,000. This limit has been cut to £4,000 from April 2017, as announced in the Chancellor's 2016 Autumn Statement.

This affects the type of pension schemes that you can generally draw from age 55, not historic 'final salary' schemes. The MPAA is effectively the tax allowable amount you are permitted to pay in to your pension in each tax year.

If you have taken more than your tax free cash, even just £1, then your annual pension allowance will be restricted down by the MPAA for the rest of your life.

Which type of allowance applies to me?



Will this apply to me?

By and large, if you are over 55 and have not taken anything from your pension, or only ever taken your Pension Commencement Lump Sum (PCLS), also known as 'tax-free cash', then you will not be affected. You will still be able to obtain tax relief on any pension contributions.

Remember: The MPAA is only triggered if you access your pension income. If you haven't done so, then the AA rules apply, and you can save up to 100% of your earned salary in your pension, capped at a maximum of £40,000 each tax year.

Why is it being reduced?

The chancellor, Philip Hammond, stated that this has come into force "to prevent inappropriate double tax relief". In other words, preventing people from diverting a significant proportion of their earned income into their pension then withdrawing up to the 25% allowed tax free and/or recycling tax free lump sums back into their pension.

What happens if I go above the MPAA?

The amount that you have gone over will be added to your income for that year and you will be charged income tax accordingly. You should note that the additional income you are being taxed on could push you into a higher income tax bracket.

Can you carry forward the MPAA from previous years?

MPAA is set at £4,000 a year and you are not allowed to carry forward any unused allowances from previous years.

How does the limit apply?

The MPAA includes both your own contributions and any other contribution made on your behalf from your employer into a pension. It should be noted that the limit is per person rather than per scheme. So, it applies across all contributions made in a year.

Important: Before making any income withdrawals or large contributions into your pension provision we strongly recommend seeking independent financial advice.

Accessing pension benefits early may impact on levels of retirement income and is not suitable for everyone. You should seek advice to understand your options at retirement.
Levels and bases of and reliefs from taxation are subject to change and their value depends on the individual circumstances of the investor. The Financial Conduct Authority does not regulate taxation advice.
www.gov.uk/government/publications/reducing-the-money-purchase-annual-allowance/reducing-the-money-purchase-annual-allowance

Care fees:

The impact of population growth on the care sector and how this affects your plans

In our recent webinar, Clive Barwell, an independent financial adviser at Wren Sterling and accredited by the Society of Later Life Advisers (SOLLA), talked through the issues in the sector, what people need to be aware of as they or a family member prepares to go into care and the value of a financial adviser in the process.

This article is a summary of the main points around the different types of care, and the preparation needed before a family member goes into care. After all, the UK population is getting older, quickly, and that's going to mean more pressure on already stretched care services.

There are over half a million people aged 90 and over in the UK. 70 per cent of these are women. Between 92,000 and 142,500 people in England each year have an unmet need for palliative care. Yet in real terms, spending on social care in England has fallen by £770 million since 2010.[1]

Why are we talking about care costs?

The short answer is that the UK is facing a huge strain on its care services in the coming years – if they're not already feeling it.

The UK population is growing and causing the care sector to grow at rapid rates. The number of adult social care jobs in England as at 2015 was estimated at 1.55 million – an increase of 12,500 jobs since 2014.[2] But is that enough to care for this rapidly growing section of the population?

Between 2005/06 and 2015/16 the total number of people aged 65 or over in England increased by close to 21 per cent, representing nearly 1.7 million extra people.[3]

Moreover, the greatest growth in percentage terms has been amongst those aged 85 and over, this age group increased by 31.3 per cent (or more than 300,000 people) over the period.[3]

We could be facing a crisis in the next few years, so preparation is key for those wanting to receive quality care.

The means test

The means test will look at the individual's regular income (pensions, benefits and earnings) and capital (savings, investments and property). For example, in England if you have more than £23,250 then your capital is deemed to create sufficient income – on top of your pension and other income – to cover **all** of your social care costs. The chart below shows the regional variations in the means test for 2017/18.

	England	Scotland	Wales	NI
Upper capital threshold	£23,250	£26,500	£30,000	£23,250
Lower capital threshold	£14,250	£16,500	£30,000	£14,250
Tariff income	£1 pwp £250	£1 pwp £250	NIL	£1 pwp £250
Additional benefits	NIL	£171 + £78 pw*	NIL	NIL

* The £78 benefit is only payable for those who require Nursing Care.[4]

** The above rates are the DWP rates applicable 2017/18, and have been taken from each of Age UK's regional websites

Other than in Wales where the upper and lower limit are the same. In England, Scotland and Northern Ireland, we have to take the lower capital threshold into account. In these areas, £1 per week per £250 over the lower threshold is added to other income to assess affordability. The reality is that even when you reach £23,250 the capital erodes pretty quickly down to that lower threshold. Once this reaches that lower threshold then the capital is no longer taken into account.

Who pays for your care?

The NHS pays for all aspects of **medical care**, and this is free at the point of delivery. For those unsure about who pays, it's important to know that there are three types of care; social, registered nursing, NHS continuing healthcare.

Social care

This type of care includes daily living assistance – getting up, going to the bathroom, showering, dressing, feeding, etc. These are all daily living activities, and any care of this kind will need to be paid by the individual. If they do not have sufficient income, then the local authority will pay this, assuming the individual is assessed as having "Eligible Care Needs".

Their medication and the occasional visit from a nurse will be paid by the NHS. The local authority will only pay £400-600 a week for a care home – and you have to consider do you want to be able to choose the home your loved ones will be placed in?

Registered nursing

When an individual needs more help than can be provided by a GP and a visiting nurse, the social care aspects continue to be means tested if they have the income. The NHS will then pay for the nursing provision. In England that's currently £155.05 per week.

So, if the cost of the care home or nursing home is £655.05 a week, then the NHS pays the £155.05, and the individual pays the £500 – or if they've run out of money, the local authority will top-up their income to cover that.

NHS continuing healthcare

When the balance between social care and medical needs changes to where the medical needs outweigh the social care needs the NHS picks-up the entire bill.

There are a number of situations where arguments can break out about where the line occurs between social care and NHS continuing healthcare. Sometimes this will take place after death using their medical records.

When should you start planning for your care?

There is no golden rule for when you should start planning for your own care, but I do talk to clients about this at the point of their retirement so that when we're looking at deployment of assets we can discuss this. But remember, the local authority is never going to criticise you for having enjoyed your retirement if you end up needing payment for care - but you should consider if you want to have a say in your care.

The value of a financial adviser

I sit down with clients and talk through various scenarios long before they need care. As a qualified independent financial adviser – who holds the required regulatory qualification for advising on long term care – I am able to provide an holistic review of an individual's financial situation. This also means that my clients can include the whole family into any decision. And of course there are regulated investment products which only specialist financial advisers can advise on.

Next steps

Our care fees webinar with Clive is just over 30 minutes long, and covers other topics like Power of Attorney, Asset Protection Trusts and leaving an inheritance as well as going into more detail about the means test. Find out about more about care fees by searching for Wren Sterling's YouTube channel and watching the webinar.

Alternatively, if you have questions about your retirement and provision for care fees, please contact your Wren Sterling adviser to arrange a consultation about your care requirements. If you do not currently have a Wren Sterling adviser and require advice on your specific situation, please contact marketing@wrensterling.com to arrange a free initial consultation.

[1] https://www.mariecurie.org.uk/globalassets/media/documents/commissioning-our-services/publications/understanding-cost-end-life-care-different-settingspdf
[2] http://www.skillsforcare.org.uk/NMDS-SC-intelligence/NMDS-SC/Workforce-data-and-publications/Size-and-structure-of-the-adult-social-care-sector.aspx
[3] http://www.ageuk.org.uk/Documents/EN-GB/For-professionals/Research/The_Health_and_Care_of_Older_People_in_England_2017.pdf?dtrk=true
[4] http://www.adviceoncare.co.uk/scotland-care.html

Ensuring that your legacy reaches the next generation

As the onus for paying for care fees moves back from the state to the individual, how can you make sure you're protecting the legacy you plan to leave?

Lindsey Atterbury, Solicitor and Head of Legal at The Will Writing Company Limited

Whether we agree with it or not, most of us understand the concept of paying for our later life care. Most people are careful and do not want to pay more than necessary, although paying for your own care brings with it the choice of where and how you are cared for.

Many people I have met would prefer (and indeed expect) their estate to pass to the next generation and this will not happen if their share has been used to pay for the care of the surviving partner. You may be content with that position, but if you would prefer that your assets provide a legacy for your loved ones (rather than going towards care fees) there are ways to avoid this extra burden on your finances - by arranging your assets and your Will in different ways.

Paying for a partner's care

Paying for a partner's care is the default position and naturally occurs as most couples leave their estate to each other on the first death. If this is the case the survivor owns the whole estate which can then be used to pay for care. There are ways to arrange your assets and your Will so that you can avoid this situation.

Revisit your Will

To protect your legacy, first you should examine how you hold your assets. Are they in joint names? Do they pass by survivorship, outside a Will? Should the ownership be changed? You will also need to consider the terms of your Will. If your Will leaves everything to your spouse or partner on the first death, then you will achieve nothing more than the default position – so you could consider a second step.

Protect your property

Including a trust within your Will is one way you can protect your home for your spouse and your descendants. It is possible to set up a trust so that if you were to die, the surviving partner would be given the right to reside in the property for as long as necessary. On the eventual sale of the property the proceeds will be divided between the beneficiaries named in the Will. This way, your share of the property would not be available to pay for your partner's care.

This isn't the only type of trust your advisor would consider when discussing your needs. It's just one example which addresses the concerns of many of our clients when they talk to us about what they want to happen to their home.

Further protect your legacy

You may decide to include a trust within your Will regarding your cash assets. Depending on the type of trust, this will give your partner right to receive income from your estate – and then only income could be used towards your partner's care. The underlying investments would not be owned by your partner and could not be used towards their care fees.

Getting help from a specialist

Deciding how you want your legacy to be distributed, arranging your financial affairs to minimise your outgoings in respect of tax, care fees and other matters are all basic rights and can be done without falling foul of the law. Many people choose not to do this alone and take advice from Independent Financial Advisers, Lawyers and Estate Planning Professionals on how to legitimately minimise their care fees.

Through our partnership with The Will Writing Company, your adviser can introduce you to a specialist who will work closely with you to ensure your Will is set up as you want it and it ties in with your financial planning arrangements. So, no matter how complicated your Will may be, you can be confident that your wishes will be carried out – including any provisions you've made to minimise tax liabilities after your death.

To arrange an appointment to discuss your Will please contact your Wren Sterling adviser.

The above is not intended as a substitute for legal advice tailored to your individual circumstances. If you'd like to know more and how our partnership can help you, get in touch with your adviser.
The Financial Conduct Authority does not regulate taxation & trust advice and will writing. Levels and bases of and reliefs from taxation are subject to change and their value depends on the individual circumstances of the investor.
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Pension transfers: Why are some people cashing in final salary pension schemes?

Robert Blumberger is an independent financial adviser and pension transfer specialist at Wren Sterling

To younger people entering the workplace, final salary pension schemes (otherwise known as defined benefit pension schemes, or DB schemes) are seen as luxuries from a bygone era. They're traditionally much more lucrative than a defined contribution (DC) scheme because they guarantee the retiree a proportion of the level of income they earned during their career rather than relying on them to save themselves. In recent years they've been phased out by employers because people are living for longer and the uncrystallised liabilities are wreaking havoc with corporate balance sheets.

However, a new trend has emerged for those with final salary pensions to consider cashing them in and moving them to a defined contribution scheme. Robert Blumberger explains why this is happening and sounds a cautionary note for those attracted to the idea of transferring.

Money Matters: Hi Rob, what is a defined benefit pension transfer?

Robert Blumberger: A defined benefit pension is provided by your employer's pension scheme and is determined by your final salary and your years of service. A defined benefit pension transfer allows you to swap your future secure pension income for a cash sum transfer value which can be transferred to an alternative pension arrangement. The individual is then in charge of their own money, and takes on the management of their funds and inherent risk in return for an unknown future income but more flexibility.

Transferring a final salary pension may be attractive, but in my experience it's not the right option for many people.

MM: Why are DB pension transfers suddenly gaining popularity?

RB: There's certainly coverage in the media as final salary transfer values are at historic highs and consequently people are sharing stories with their friends and colleagues. This is prompting more and more people to ask if a DB pension transfer could be the right option for them.

Another reason why DB pension transfers are becoming more popular is the recent pension freedoms. Once you transfer a pension to a DC scheme, which is more flexible, you can take a tax-free lump sum and defer the income until you need it at a later date. The death benefits under a flexible arrangement are also very attractive to many. Under a final salary scheme the income typically stops on death of both the member and spouse and there is nothing to pass on to the next generation. Under a DC scheme there are flexible death benefits which means the remaining pot of money can pass on to family. There's a lot more flexibility with the new arrangements, which is appealing for some people.

Transferring a final salary pension may be attractive, but in my experience it's not the right option for many people.

Another factor influencing transfer values is gilt yields. Currently these gilt yields are low, increasing the cost of the DB scheme and the size of the transfer value people can receive.

In my opinion, values are artificially high at the moment, which is driving interest and more acceptances than I've been used to.

MM: How are transfer values calculated?

RB: The cash equivalent transfer values (CETVs) are calculated by the scheme actuary and will vary between schemes but the main factors that the CETV is based on are:

- How far away you are from retirement
- Your salary
- Your service with the company
- Any rules about how your pension will increase, and any other benefits from the scheme
- Assumption on future annuity/ interest rates
- The value of gilt yields

MM: So why would someone want to transfer their DB pension?

RB: There are several reasons for taking this route. I think primarily it's because DB schemes are inflexible and benefits are lost on death and whilst transfer values are high people see an opportunity to move these schemes to a more flexible arrangement. This drive can be stronger than the secure income a final salary scheme will provide.

MM: When would a transfer be appropriate?

RB: I'm advising one lady on a transfer for over £900,000 at the moment. She'd been told she might have a high transfer value by a colleague, which is what prompted her to contact me. While it looks like a lot of money, she wants to make sure she's doing the right thing as these funds could quickly evaporate due to poor future investment returns, charges and the lifestyle she wants to maintain.

One factor that we also look at is the Critical Yield. This is essentially a calculation of the investment return required to match the benefits being given up in the old scheme. Whilst this is not the only factor we consider it is an important one as we would be reluctant to advise on a strategy we know would significantly financially disadvantage the client in retirement.

In this case, her family owns many other assets and she isn't relying on this income. The investment returns required are not too onerous so she could transfer it without it affecting her future and the new strategy will allow her additional flexibility and the opportunity to leave a legacy for her family which is important to her.

If you need security of income, an annuity or final salary is likely to be the best way to go, rather than a flexible drawdown arrangement.

MM: When would a transfer be inappropriate?

RB: The point of a pension is to provide you with an income in retirement, not to provide a legacy – yet this is one of the main reasons individuals look into a pensions transfer.

The main reason I would advise against a transfer would be because I don't think they could afford the risk and I think it will impact on their retirement.

Recently, I had a gentleman who wanted me to look into a transfer for him so that he could provide a legacy - as DB schemes cannot be passed on to the next generation.

He and his wife had a total transfer value of just over £300,000 between them, and he thought he could easily achieve a better return. He didn't have many other assets set aside though and was very reliant on the income from the scheme in retirement, so I recommended that his pension was not transferred. He wasn't happy because it wasn't what he thought he wanted but it would have been the wrong thing for him and his family in the circumstances.

MM: Why is a financial adviser so important to the process?

RB: If your CETV is worth £30,000 or more and you're considering a transfer, you are required to seek regulated financial advice. Not every financial adviser is able to advise on DB pension transfers as additional qualifications are required. Also the firm needs the appropriate FCA permissions to carry out this business, which Wren Sterling has.

When considering a pensions transfer, a financial adviser will take a holistic view of your finances, not only considering an individual's appetite to risk, but also discussing the provision in place for their spouse. Even if a pension transfer isn't the right option, financial advisers can look at other products which could achieve a person's financial goals. For example if a legacy is important to a client we can look at alternative ways of providing this such as whole of life cover or funding an alternative pension if appropriate.

MM: What does the process look like?

RB: At Wren Sterling we go through a series of stages to decide whether a DB pension transfer would be right for you. First, we conduct a 'fact find' to learn about your finances and how you want to manage them and assess your financial objectives. Then we'll get a transfer value analysis report and make an assessment on which of your options would be most suitable to you. If the transfer is appropriate we are then able to recommend a suitable vehicle to accept the transfer and an appropriate investment strategy to achieve your goals.

Next steps

If you have a preserved DB pension, have you had it valued?

If you'd like to discuss your pension provision, or find out your DB pension's transfer value, we would recommend speaking with a financial adviser. At Wren Sterling we have a dedicated retirement service, and would be happy to talk you through your options and help you make your choices with confidence.

The value of your investment and income from it can go down as well as up and you may not get back the full amount invested. Accessing pension benefits early may impact on levels of retirement income and is not suitable for everyone. You should seek advice to understand your options at retirement.

https://www.moneyadviceservice.org.uk/en/articles/transferring-out-of-a-defined-benefit-pension-scheme

Some advantages to transferring	Reasons not to transfer
Reliance: If a person is not reliant on the money for retirement income (i.e. they have other pensions and investments to give them a retirement income)	**Investment performance**: This may be worse in a new scheme and leave the clients in a worse position than before. This is absolutely fundamental.
Legacy: final salary schemes cannot be passed on to the next generation on death of both the owner and spouse	**Reliance**: The holder's spouse is reliant on the income
Investment control: transferring to a DC scheme gives more flexibility	**Insufficient assets**: If clients are relying on a DB scheme for retirement income because there are not many other savings and investments available, a transfer might not make sense
Value: transfer values are artificially high at the moment due to low gilt yields	**More appropriate products**: If a client wants to create a legacy for example, it might make more sense to review protection policies to see if life insurance policy will have the same effect without compromising the security of a DB scheme
Ill health: if the DB pension scheme member is unwell and likely to die in the near future, cashing in will ensure a legacy can be left for future generations	

Please note, this table is not exhaustive and there may be other reasons, on both sides, for approving or rejecting a pension transfer request.

Is your children's lifeline of credit leaving you in need of a lifebelt?

Justin Urquhart Stewart, Co-founder and Head of Corporate Development, Seven Investment Management

When you think about banks, most people's minds meander down the High Street, thinking of names – some of which have actually been assigned to the annals of history – as well as the likes of Lloyds, HSBC and my old shop, Barclays. No one's mind, I venture, would just stay at home.

But numbers now show that the Bank of Mum and Dad is now our ninth largest mortgage provider, up a place in the rankings from the year before. And the parental (and grand parental) generosity doesn't stop there.

In a survey we ran among 2,025 representative UK citizens in the summer, some 15% of parents were helping their adult children with property payments. But 42% are offsetting their offspring's day to day living expenses and a fifth (21%) of parents are rallying round for car costs. Parents are also sharing the hefty financial burden of university costs (17%) and paying off other debt (13%).

The truly sad thing here is not that many families are pooling their funds – it's the potential impact on the parents' long term financial wellbeing that concerns me. And that's mainly due to the longevity of some of these monetary lifelines. It's almost expected that you'd help out your 18-21 year olds and 42% are. However, 30% are helping 22-29 year olds, a quarter (25%) are assisting 30-39 year olds and 18% are giving contributions to children into their 40s.

So what can you do, so that when you get off the career treadmill, your finances are fighting fit for your retirement? Here are three pieces of advice that have held me in good stead... touch wood!

1. The sooner you save...

Little and often is an excellent approach when it comes to investing for children or indeed anything. Saving £100 a month for 18 years in an investment fund generating 5% annual growth could give you around £35,000 – a good financial head start in life. Yes, of course, investments can go down as well as up and there are risks involved. But the sooner parents start putting money aside, the less drastic any sudden support will be later on down the line. And it'll help your kids – no one needs the burden of almost bankrupting someone you love.

2. Prioritise the pension

It seems a little counterintuitive to be putting money in your pension when you've always invested in your children. But your considerable efforts to help them get to university now seem to leave them in a financial hole. The situation today means that kids can finish their studies with £50,000 in debt and incur a whopping 6.1% in interest rates from the day that they get their money – not at the end of their course as some seem to think is the case.

Putting aside my view about this stupid system, you should actually think through what they'll pay back rather than what's on the balance sheet, especially since it doesn't actually count as debt. Yes, it will be included in calculations as to what they can afford, but only once they're over the £21,000 a year earning threshold and then they only pay 9% on any marginal income. If they never earn that over the 30.5 years after they leave university they won't need to pay back a penny. And from 2021, that starting threshold may also begin to rise again, if it doesn't become politically expedient to do so earlier.

You could even use the system to your advantage and think whether the first few retirement years could be spent in full time education. If your pension is below the threshold, you could fill your days and your mind at the state's expense.

3. Be at least a little selfish

With children moving out of home later in life and everything seemingly terribly expensive these days, it's only natural that you want to help out. But are you in danger of moving from back stop to their first port of call for everything? When I went to university I compounded my lack of understanding of credit cards with feckless finances and developed debts that took me several years to pay off. My parents quite rightly refused to bail me out. And while it was a hard lesson at the time, I never repeated the experience.

So there is a time when you will need to draw a line in the sand and say enough is enough. A few weeks ago I was on stage in front of an audience drawn from Financial Times readers talking about rich-kid-itis – a lingering malaise that affects children that are far too spoiled. But any child to be honest is in danger of contracting a deep dependency disease as far as finances go. The good news is that almost anything can be treated if nipped in the bud.

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Risk and reward in Venture Capital Trusts

Stuart Lewis is Head of Tax-Efficient Investments at Octopus Investments

Venture Capital Trusts (VCTs) offer investors a number of tax benefits in return for taking the risk of investing in UK smaller companies. VCTs were once considered 'niche' investments, but recent events have put them on the radar of a much greater number of UK investors, explains Stuart Lewis of Octopus Investments.

There is a healthy appetite among UK investors for VCTs. In the last tax year, VCTs raised an impressive £542 million from investors, which is an increase of 18% from the previous year and the second-highest VCT fundraising year on record. This means there's a total of £3.9 billion currently invested in the VCT market.[1]

Serving a valuable purpose

VCTs were introduced in 1995, as part of a package of government measures aimed at encouraging investment in the UK's small but growing businesses. The main aim of the legislation was to drive economic growth and job creation. VCTs support newer, entrepreneurial types of companies, which have traditionally been under-served by more conventional methods of company funding.

An attractive investment proposition

The tax benefits of a VCT can be quite attractive. You are able to claim up to 30% upfront income tax relief on the amount invested, provided you are willing to keep holding the VCT shares for at least five years.

Another valuable benefit is that VCTs are able to pay tax-free dividends, although dividend payments are not guaranteed. Finally, should you decide to sell your VCT shares and you make a profit, the proceeds won't be liable for capital gains tax.

Explaining the risks

It is always worth remembering that these tax benefits are there, in part, to offset the higher risk associated with investing in a VCT. And as with any investment, the value and any income from it can fall as well as rise. You may not get back the full amount you invest. VCTs shares could fall or rise in value more than other shares listed on the main market of the London Stock Exchange. Your tax treatment will depend on your individual circumstances and tax incentives may change in the future. The tax reliefs also depend on the VCT maintaining its VCT-qualifying status.

In pursuit of complementary retirement planning strategies

One of the reasons why VCTs have gained in popularity is that many high earners, particularly those getting closer to retirement age, are now feeling far more constrained in how much they can put into their pension. Changes to the lifetime allowance have meant that a large number of investors have started looking at VCTs in a new light, as a means of complementing existing retirement planning strategies.

Tax relief for investors

HM Revenue and Customs (HMRC) offers tax relief to encourage individuals to invest in companies through a number of venture capital schemes. You can get tax relief when you invest in small UK companies and social enterprises that qualify for venture capital schemes.
The amount and type of tax relief you can claim depends on what venture capital scheme you use to invest in a company and you meet certain conditions. You can get tax relief through the following venture capital schemes:[2]

Scheme	Annual investment limit you can claim relief on	Income Tax relief	Minimum qualifying period for share relief	Tax payable on dividends
Enterprise Investment Scheme (EIS)	£1 million	30%	3 years	Yes
Seed Enterprise Investment Scheme (SEIS)	£100,000	50%	3 years	Yes
Social Investment Tax Relief (SITR)	£1 million	30%	3 years	Yes
Venture Capital Trusts (VCT)	£200,000	30%	5 years	No

[1]The Association of Investment Companies, April 2017
[2]https://www.gov.uk/guidance/venture-capital-schemes-tax-relief-for-investors [Accessed 29 September 2017]

Back in 2010, the lifetime allowance – the maximum amount that could be invested into a pension without triggering additional tax charges – was £1.8 million. But this amount has now almost halved to the current figure of £1 million. In a similar vein, the annual allowance – or how much a saver can contribute to a defined contribution pension scheme each year while still receiving tax relief – stood at £255,000 in 2010, but is now down to £40,000, and is reduced to as little as £10,000 for high earners. Advisers have been telling us about clients who have accumulated significant pension pots over their lifetime, who have suddenly realised that they risk hitting the lifetime allowance even if they make only modest future pension contributions. As a result, they are interested in exploring how a VCT can complement their existing pension arrangements.

More generally, the pension freedoms that were announced in April 2015 – which scrapped the requirement for retirees to buy an annuity – have opened investor's eyes to a world of opportunity and choice when it comes to planning for retirement. It's important to stress of course that a VCT is a high-risk investment, and therefore shouldn't be considered as a replacement for pension investments.

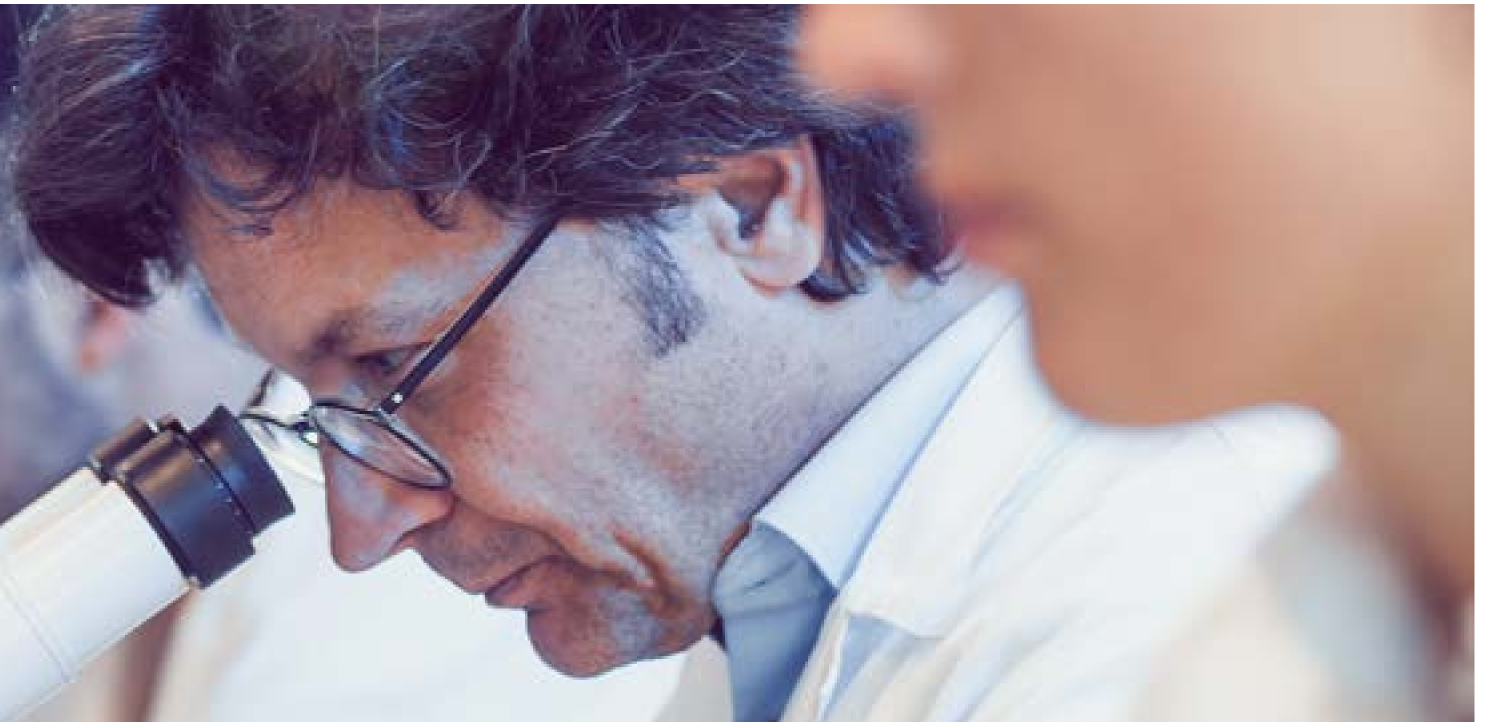
Landlords are also feeling the pinch

Historically, many people have opted to invest in property as a way to complement or even replace pension planning. However, a series of measures – including a 3% stamp duty surcharge on the purchase of buy-to-let properties and second homes and, more recently, the phased reduction in tax relief on mortgage interest – has made this less tax-efficient. One of the unfortunate outcomes is that many property owners who were paying income tax at the basic rate will likely be pushed into the higher-rate tax bracket, despite their effective income from the property staying the same.

VCTs with 'the right stuff'

When it comes to finding the right VCT to invest in, there are a number of important factors that could help to narrow your search. You and your adviser should consider the following:

- Track record: how long has the VCT been in existence? How experienced is the VCT manager? A well-established VCT should be able to demonstrate a performance track record. However, newer VCTs can take longer to reach the size and scale required to start delivering meaningful returns for investors. They may also be invested in younger companies that could still be a few years away from potential profitability.
- Diversification: one of the best ways to manage the risks of investing in higher-risk smaller companies is to diversify and spread the risk. By the same token, even a VCT with good performance – if it's small and not diversified – will have a higher concentration risk. It may be worth looking at more mature VCTs featuring diverse portfolios of companies that are already hitting their stride.
- Discount to Net Asset Value (NAV): VCT shares tend to have a limited secondary market, as second-hand shares don't qualify for the 30% upfront income tax relief. Therefore it's important that investors are able to find buyers for their shares when it comes time to sell them. There isn't an active market for VCT shares in the way there is for shares in larger, listed companies. This means that should you decide to sell your VCT shares, it may take time to find a buyer, or you may have to accept a price lower than the NAV of the investment. Most VCTs will offer a share buyback facility, where the VCT itself offers to buy the shares back from the investor at a discount to NAV. A 5% discount is considered reasonable, but some VCTs will only buy back shares at a higher discount so it's worth looking for established VCTs with a strong track record of buying back shares from investors at a small discount.



For more information on Venture Capital Trusts and your potential suitability for them, please contact your Wren Sterling adviser, who will consider their appropriateness in line with your overall financial planning goals.

VCTs can be considered high risk investments and they will not be appropriate for every investor. Wren Sterling strongly recommends speaking to your adviser before taking any action directly.

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Important information

The contents of this article are correct as at 02.10.2017. The tax treatment of Venture Capital Trusts may be subject to change in the future.

The value of an investment, and any income from it, can fall as well as rise. Investors may not get back the full amount they invest. Tax treatment depends on individual circumstances and may change in the future. Tax reliefs depend on the VCT maintaining its VCT-qualifying status. VCT shares could fall or rise in value more than other shares listed on the main market of the London Stock Exchange. They may also be harder to sell. Personal opinions may change and should not be seen as advice or a recommendation. We do not offer investment or tax advice. We recommend investors seek professional advice before deciding to invest.

This information is based on our understanding of tax rules at September 2017.

About Wren Sterling

Wren Sterling is a nationwide independent financial planning business that specialises in all aspects of investments, protection and retirement planning. We pride ourselves on navigating clients through their financial journey by providing uncompromised and objective advice. Our advisers are committed to developing long standing client relationships that span generations to achieve our clients' lifetime financial goals.

Where we are

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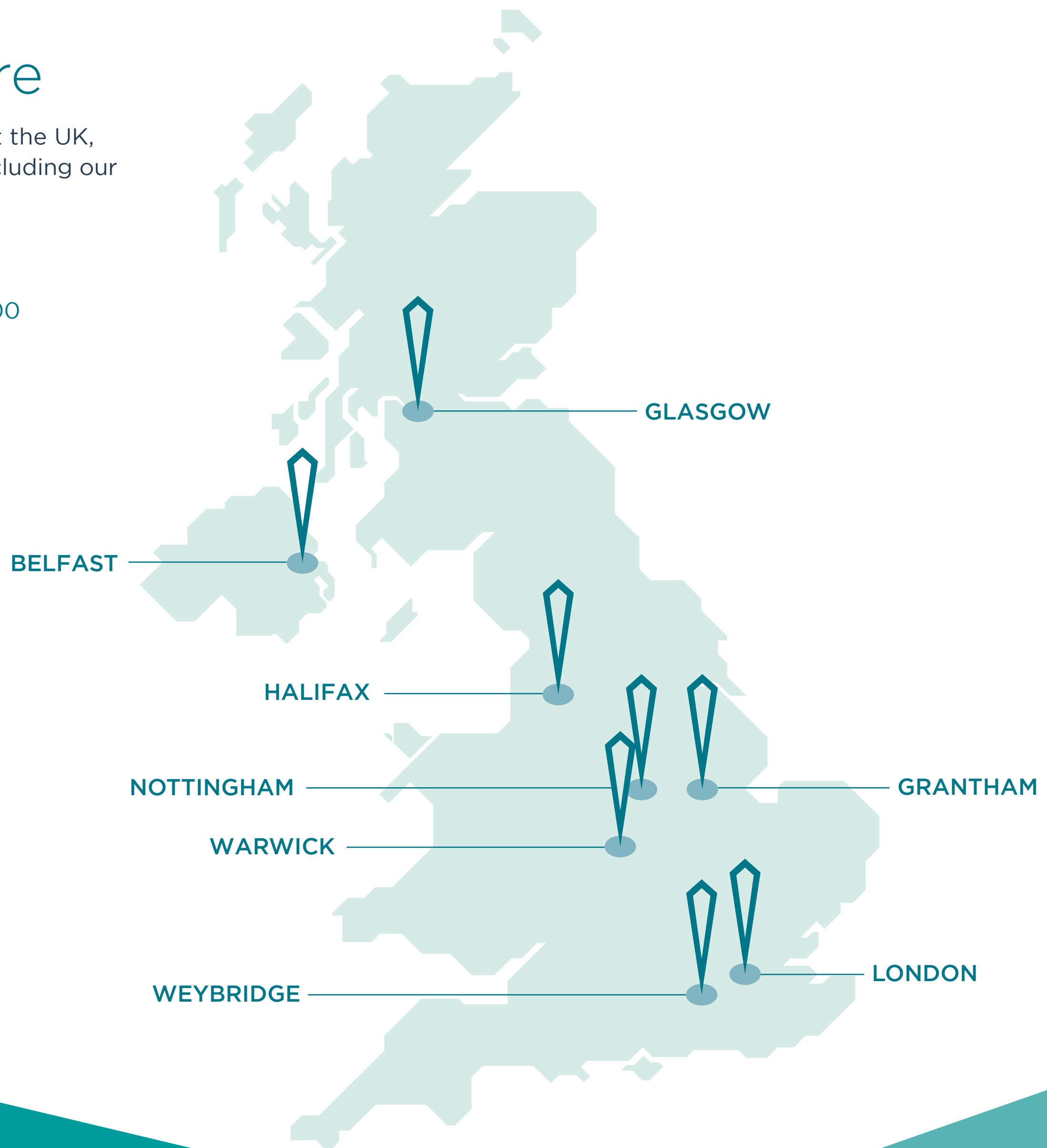

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