Making VCT investments for income tax relief

John is a 48-year-old software engineer who earns £80,000 per year. He has a pension and some savings but he wants to reduce his tax bill and invest in private companies to improve his diversification. .

After assessing John's attitude to risk, investment goals and capacity for for risk, John's financial adviser suggest a VCT investment to manage his income tax liability

VCTs offer various tax benefits to John, such as:

- Income tax relief of 30% on the amount invested, up to £200,000 per tax year
- Tax-free dividends from the VCT
- No capital gains tax on the disposal of the VCT shares

The sale of portfolio companies provides capital back to VCTs, which can either be reinvested or distributed as dividends. Over a ten year period Northern VCTs average dividend is 6.8%, which is one of the best in the market.

John's finanical adviser reviews various strategies for the VCT investment, such as reinvesting dividends (DRIS), switching VCTs, and repeat investment.

John's financial adviser considers various VCT strategies, such as reinvesting dividends (DRIS) and repeat investments.

However, for simplicity recommends a single VCT investment of £71,666 funded from savings in Northern VCT before 30th November 2023. This strategy will remove John from paying any income tax in 2023/2024, he will then benefit from annual dividends of £4,873 per year.

Over the first five year and three month holding period John receives £26,802 in tax free dividends, based on a 6.8% 10 year average dividend. These dividends are not subject to income tax.

In February 2029, John sells the VCT at cost. This assumption is realistic, as the discount to NAV for buy backs is 5%, and NAV growth over the period of 5% is conservative, but subject to market fluctuations.

Due to the strong performance and simplicity, John chooses to reinvest the £71,666 into a different Northerns other VCTs, and benefit from another £21,500 income tax reliefs.

By switching VCTs every five years, John maximises his income tax relief and diversifies his portfolio across different sectors and companies.

After investing £71,666 originally, after ten years and six months and including two VCT switches, he will have received £43,000 in income tax reliefs, £53,603 in tax-free dividends and have a holding (assuming no capital growth) valued at the original cost (£71,66). Therefore, John has made a profit of £96,603 in the period, which is 120% of his annual salary (tax free) and still has his original capital.

John is pleased with the outcome of his investments and through reinvesting can build a valuable source of income over a number of years.

1st Northern VCT investment	2nd Northern VCT investment
£71,666 invested	£71,666 re-invested
£21,500 income tax relief	...after 10 years
...after 5 years	£43,000 income tax relief
£26,802 in annual dividends	£53,603 in total dividends
£71,666 shares sold at cost	£71,666 shares sold at cost
£119,968 returned	£168,289 returned
£48,302 profit	£96,603 profit

VCT Tax Planning with Mercia | how advisers can access attractive tax advantages for their clients

The Northern VCTs (Venture Capital Trusts) provide an opportunity to gain exposure to innovative UK businesses, with the benefit of up-front tax relief and tax-free dividend income.

The Northern VCTs invest across a range of innovative sectors from bioscience through to software and consumer goods providing investors access to unique opportunities. Whilst these do carry a degree of risk, as is the nature of all early-stage investment, they do also offer high rewards for those seeking a high-risk, high-reward profile.

Mercia acquired the contracts to manage Northern VCTs in 2019. The Northern VCTs comprises of three very similar funds, in the form of Northern Venture Trust (NVT), Northern 2 VCT (N2 VCT) and Northern 3 VCT (N3 VCT).

To simplify message, our collateral aggregates the three VCTs, as they invest alongside each other, but differences including their long term track records, are listed at mercia.co.uk/vct/northern-vcts.

Mercia also manages a market leading EIS fund, which invests at an earlier stage than Northern VCTs.

Tax incentives available

- Income Tax Relief - 30% income tax relief is available until the investor's income tax bill is reduced to zero.
- Tax-free dividends - if VCT shares are sold for more than was paid for them, any profits are free from capital gains

The Northern VCTs at a glance

Peter Dines, VCT Managing Director

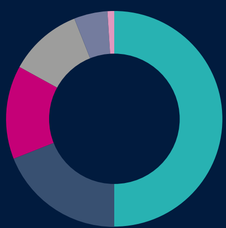
VCT Team's Expertise

Peter Dines spearheads the VCT investment team, bringing a successful entrepreneurial background, extensive investment expertise, and over two decades of experience in the Life Sciences domain. Supporting him is a VCT specialised investment team of 16, each possessing significant experience in the venture and VCT markets, collectively forming a formidable force in identifying and nurturing innovative ventures across the venture capital landscape

Where we invest

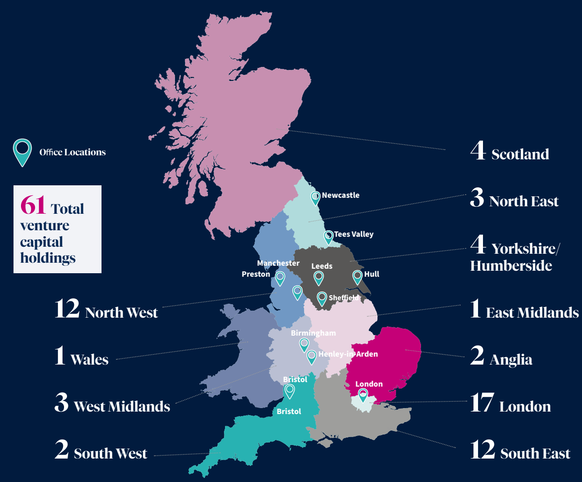
Northern VCTs are a national investor, with a focus on the UKs regions, where we discover compelling opportunities among businesses in diverse sectors, offering reasonable valuations and with modest capital needs. These favorable valuations often lead to enhanced investment returns.

The Northern VCTs cover both early and later stage UK companies, spanning diverse sectors like bioscience, software, and consumer goods.



Industry sector

Software/electronics	50%
Healthcare/biotechnology	19%
Consumer	14%
Services	11%
Industrial/manufacturing	5%
Other	1%



*Information and valuations as at 30 September 2021, adjusted for additions and disposals since this date. **Includes unquoted investments and investments quoted on AIM. ***Total capital and income returns over the investments lifetime for investments exited in each calendar year.

Risk warnings

VCT investment is restricted by the FCA rules to persons who qualify as high net worth or sophisticated, or who are acting upon advice from a suitably qualified financial adviser. Investing in early-stage businesses involves risks, including illiquidity, lack of dividends, loss of investment and dilution, and it should be done only as part of a diversified portfolio. Past performance is not a reliable indicator of future performance. You should not rely on any past performance as a guarantee of future investment performance. Tax relief depends on an individual's circumstances and may change in the future. In addition, the availability of tax relief depends on the company invested in maintaining its qualifying status. You may lose all the money that you invested; the investments are highly illiquid and have no ready market for disposal; there is a risk from future dilution of your shareholding.