Client planning scenario

For the use of professional advisers only and not to be relied upon by retail clients.

Landlords looking for a tax-efficient income stream

Investing in bricks and mortar became less favourable with major changes to buy-to-let rules in 2017. Given the new rules it's even more important for landlords to consider the tax implications of their property investments.

This example explains how landlords could use a Venture Capital Trust (VCT) to provide a tax-efficient income stream.

octopus investments

A brighter way

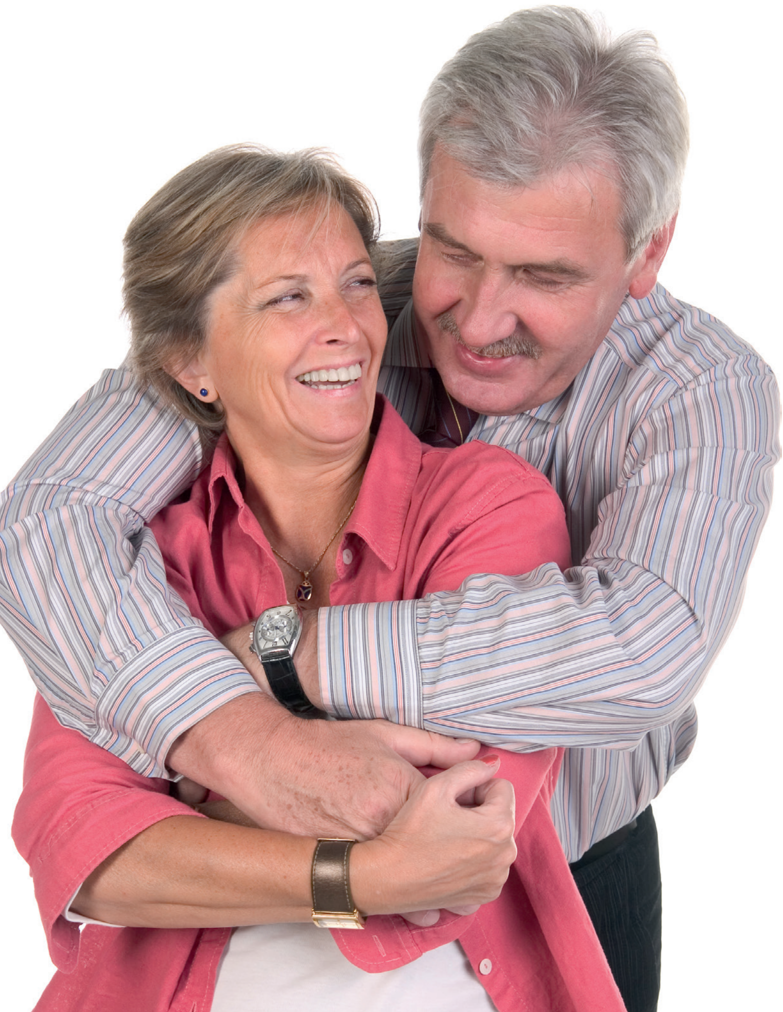
About this scenario

This tax-planning scenario is designed to help advisers develop appropriate planning strategies for their clients. Advisers should consider, among other things, the eligibility and timings of tax reclaims and tax liabilities depicted. They will also need to consider the impact of charges (including initial fees and ongoing fees, such as administration fees and annual management charges) relevant to the products represented and/or any specific product chosen. In addition to charges it's also worth bearing in mind that when clients choose to sell VCT shares, they are often sold at a small discount to the value of their underlying net asset value, so the impact of this should also be considered when assessing any specific products.

Nothing here should be viewed as advice. Any suitability decisions should be based on a comprehensive review of your client's objectives, needs and attitude towards risk. For more details, please see the relevant product literature.

Meet Daniel and Helen

Daniel and Helen have been married for 30 years, and both plan on retiring in ten years' time. Daniel pays higher rate tax and has adequate pension provision. Helen, on the other hand, invested in property to help fund her retirement. Helen earns £30,000 of rental income (after costs) from her properties and has other income up to her personal allowance. She expects to pay £6,000 income tax this year. Both Daniel and Helen are keen to enjoy a tax-efficient income during their retirement, but Helen in particular doesn't feel ready to sell her properties and be left with a large capital gains tax bill.



A tax-planning solution from Octopus

Helen talks to her financial adviser, who makes an assessment based on her risk profile, investment time horizon (five years plus) and attitude towards smaller company investing. Based on the results, Helen's adviser suggests investing £20,000 of her annual rental income in a VCT and putting the remaining £10,000 in an Individual Savings Account (ISA). The upfront income tax relief Helen makes from her VCT investment (£6,000) would eliminate the annual income tax she's required to pay on her rental income.

In order to keep upfront income tax relief claimed, VCT shares must be held for at least five years (should Helen sell the shares before then, she'd have to repay the tax relief to HMRC). However, after five years, Helen could sell her first VCT investment, then reinvest the proceeds in another VCT and use the additional income tax relief to reduce her year six income tax bill. Similarly, Helen's year two VCT investment could be sold and reinvested in another VCT in year seven, giving her additional income tax relief, and so on.

An important reminder about key risks

VCTs are high risk and should be considered as long-term investments. The value of an investment, and any income from it, can fall or rise. Investors may not get back the full amount they invest.

Tax treatment depends on individual circumstances and can change in the future. Tax reliefs also depend on the VCT maintaining its qualifying status. Tax relief is available on investments of up to £200,000 per year.

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.

These products are not suitable for everyone.

Invest £20,000 and get £6,000 income tax relief

This diagram shows how Helen can claim income tax relief from each VCT investment made across several consecutive tax years. We've used six years as an example but in practice she could use this method to keep claiming income tax relief indefinitely. This is, of course, subject to certain conditions, including the requirement to hold VCT shares for at least five years in order to retain the 30% upfront tax relief. VCTs are high risk and are not suitable for everyone. If an investor needs guaranteed income, cannot tolerate loss or is uncomfortable losing immediate access to their money, then VCTs are not suitable. It is also worth noting that after selling shares in a VCT, it is not possible to claim tax relief on new shares bought in the same VCT within six months of the initial sale.

1 Helen invests **£20,000** in year one, which allows her to claim **£6,000** in tax relief.

2 She continues to invest an additional **£20,000** in a VCT in years two, three, four and five, claiming income tax relief of **£6,000** in each tax year.

Year 1	Year 2	Year 3	Year 4	Year 5	Year 6
Invest **£20,000** in a VCT	Invest **£20,000** in a VCT	Invest **£20,000** in a VCT	Invest **£20,000** in a VCT	Invest **£20,000** in a VCT	Re-invest original **£20,000** in another VCT
£6,000 income tax relief	**£6,000** income tax relief	**£6,000** income tax relief	**£6,000** income tax relief	**£6,000** income tax relief	**£6,000** income tax relief

3 In year six, Helen can choose to sell her first year's VCT investment, tax-free. By investing the proceeds of the sale into another VCT, she is able to use her first year's investment to claim further income tax relief. After six years, Helen could have claimed **£36,000** in income tax relief from a £100,000 investment. By reinvesting in subsequent years, Helen could continue to use this cyclical approach to claim up to **£6,000** tax relief each year, without having to invest more than her initial **£100,000** stake of **£20,000** per year over the first five years.

Note: This example is for illustration purposes only. It assumes no loss or gain on the investment, or any dividends, although fluctuations will apply in practice. It also doesn't take into account the initial and ongoing fees and charges investors would pay, both at outset and when reinvesting. When clients choose to sell their VCT shares, they are often sold at a small discount to the value of their underlying net asset value, the impact of this should also be considered when assessing any specific products.

Octopus: an investment company with a difference

When we launched Octopus in 2000, our ambition was to create a different type of financial services company. We wanted to be known for putting our customers first.

Today, Octopus is an investment company with more than 500 employees and more than £7.2 billion in funds under management (source: Octopus, June 2017). We work with tens of thousands of clients, and we've built market-leading positions in tax-efficient investment, smaller company financing, renewable energy and healthcare. But no matter how big we get, our aim is to keep doing the simple things well and to look after each of our customers, day in, day out.

Our products are not suitable for everyone. Any recommendation should be based on a holistic review of your client's financial situation, objectives and needs. We do not offer investment or tax advice, but we recommend investors seek professional advice. Before investing in a VCT, investors should read the product prospectus and Key Information Document (KID).

Why not look through some of our other tax-planning scenarios?

- Clients looking to extract profits from a business tax-efficiently
- Clients with Power of Attorney over someone's affairs
- Clients looking to set up a trust
- Clients who are additional rate tax payers
- Clients who want to reduce their income tax bill

For copies, or to find out more about Octopus and what we do:

Call our Business Development Managers on **0800 316 2067**
or visit **octopusinvestments.com/clientscenarios**

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