

Product

**British Smaller Companies VCT &  
British Smaller Companies VCT 2**

Tax Status

**Venture Capital Trust**

Fund Group

**YFM Equity Partners LLP**

**Risk Warning**

This communication is provided for informational purposes only. This information does not constitute advice on investments within the meaning of Article 53 of the Financial Services and Markets Act (Regulated Activities) Order 2001. Should investment advice be required this should be sought from a FCA authorised person.

Tax Efficient Review is published by :

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10 October 2023 15:52

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## RISK WARNINGS AND DISCLAIMERS

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## GENERAL RISK WARNINGS

Your attention is drawn to the following risk warnings which identify some of the risks associated with the investments which are mentioned in the Review:

### Fluctuations in value of investments

The value of investments and the income from them can go down as well as up and you may not get back the amount invested.

### Suitability

The investments may not be suitable for all investors and you should only invest if you understand the nature of and risks inherent in such investments and, if in doubt, you should seek professional advice before effecting any such investment.

### Past performance

Past performance is not a guide to future performance.

### Legislation

Changes in legislation may adversely affect the value of the investments.

### Taxation

The levels and the bases of the reliefs from taxation

may change in the future. You should seek your own professional advice on the taxation consequences of any investment.

## ADDITIONAL RISK WARNINGS

### Venture capital trusts

1. An investment in a VCT carries a higher risk than many other forms of investment.
2. A VCT's shares, although listed, are likely to be difficult to realise.
3. You should regard an investment in a VCT as a long term investment, particularly as regards a VCT's investment objectives and policy and the five year period for which shareholders must hold their ordinary shares to retain their initial income tax reliefs.
4. The investments made by VCTs will normally be in companies whose securities are not publicly traded or freely marketable and may therefore be difficult to realise and investments in such companies are substantially riskier than those in larger companies.
5. If a VCT loses its Inland Revenue approval tax reliefs previously obtained may be lost.
6. No investment can be made by the VCT in a company whose first commercial sale was more than 7 years prior to date of investment, except where previous State Aid Risk Finance was received by the company within 7 years (10 years for a 'knowledge intensive' company) or where a turnover test is satisfied; and
7. No funds received from an investment by the VCT into a company can be used to acquire another existing business or trade.

## Factsheet

### British Smaller Companies VCT & VCT2

Type	Generalist VCT with track record
Size	£334m AUM across both VCTs and is seeking £65m with this launch in aggregate across the two VCTs with a £25m over-allotment facility
Manager	YFM Private Equity Limited ("YFM")
Sponsor	Howard Kennedy Corporate Services LLP
Registrars	The City Partnership
Receiving Agent	The City Partnership
Focus	To generate tax free capital gains and regular dividend income for its shareholders through a diversified portfolio of VCT qualifying investments across a broad range of sectors
Promoter	RAM Capital
Funds initially invested	Cash deposits, fixed income securities , money market funds and other securities
Minimum investment	£6,000 per tax year, including initial adviser charges
Initial Closing Date	28th March 2024 unless fully subscribed before
Issue costs	3% of amount subscribed, 3.5% for direct applicants
Annual costs	1% of surplus cash, 2% of other assets
Initial advisor charges	If charged, these will be facilitated by the VCT on subscription.

## Summary

**Table 1: Tax Efficient Review summary of offering Pros and Cons**

PROs	CONs
The performance of the BSC VCTs has been good over 3, 5 and 10 years and they have performed well against their generalist VCT peer group, and good level of dividends paid to shareholders, totalling 176.9p per share since launch for BSC and 84.75p per share since launch for BSC2	The BSC VCTs often use ordinary shares with a participating preference to take a priority return in the event of an investment company trade sale. This does not in any way guarantee a return or mitigate risk, but it does make their performance more static than when compared to VCT managers with normal equity
YFM are long term managers of the BSC VCTs, launched in 1996 and 2000 and offer a geographically diverse range of investments	There is a relatively high level of cash with in the two BSC VCTs with £74m and £49m respectively when their AUM are £201m and £133m
Reduced AMC is charged on cash holdings within the VCTs over £7.5m (BSC, £5m BSC2). Other VCT managers should take note!	There is a relative high concentration of the top 5 holdings across the portfolio, which total £103m of the £334m AUM

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## TER classification

TER classifies this VCT as a “Generalist VCT with track record” and YFM are experienced fund managers within the VCT market. The first British

Smaller Companies VCT was launched in the 1996/7 tax year.

## Review based upon

TER always meet/have an internet call with fund managers prior to a review. This review is based on those meetings, the prospectus for the offer, (British Smaller Cos VCT & VCT2 prospectus

(reference 20 September 2023) and data provided by YFM Private Equity Limited.

## ‘Sunset’ Clause

The ‘Sunset Clause’ was introduced by the Treasury for EIS and VCT reliefs to be reviewed and renewed by 6 April 2025. The clause provides that income tax relief will no longer be given to subscriptions made on or after 6 April 2025, unless the legislation is amended to make the scheme permanent, or the “sunset clause” is extended.

The government has the power to extend or remove the sunset clause through secondary legislation, which would allow the VCT and EIS to

operate in their current form beyond the current expiry date of the scheme.

The then Chancellor Kwasi Kwarteng announced during his mini-budget of 23 September 2022 that venture capital schemes will be safeguarded beyond 2025 and as at September 2023 the current chancellor has publicly stated he will extend the clause but no further details were given as to how this will be implemented.

Table 2: **Funds under management as at 30 June 2023**

Product Name	Net assets £m	Annual Management fee	Still to be invested £m
<b>VCT FUNDS</b>			
British Smaller Companies VCT plc	201	2.0%*	73
British Smaller Companies VCT2 plc	133	2.0%*	44
<b>NON VCT THAT CAN CO-INVEST WITH VCT FUNDS</b>			
YFM Equity Partners Growth Fund I**	10	£0	0
YFM Equity Partners Growth Fund II***	10	£0	0
YFM Equity Partners Growth Fund III	10	£0	3
<b>NON VCT FUNDS THAT CANNOT CO-INVEST WITH VCT FUNDS</b>			
YFM Equity Partners Buyout Fund I***	46	£0	5
YFM Equity Partners Buyout Fund II	80	£0	30
YFM Equity Partners Buyout Fund III	87	£0	87
<b>TOTAL UNDER MANAGEMENT</b>	<b>£577m</b>		<b>£242m</b>

\*2% per annum, which is reduced to the extent that cash exceeds £7.5m for BSC and £5m for BSC2, with a fee of only 1% charged on cash amounts above this level. The effective fee has been 1.7% in the last 12 months

\*\*Fully invested

\*\*\* no new investments, follow-on only

Source: YFM Equity Partners LLP

## The Offer

The British Smaller Companies (BSC) VCT was launched in 1996 and has £201m in assets under management; and the British Smaller Companies VCT2 (BSC2) was launched in 2000 and has £133m in assets under management.

The current offer is seeking to raise approximately £65m in aggregate with a potential £25m over-allotment, though the exact amounts raised by each VCT will depend on investors preferences, which have historically been around 60% for BSC and 40% for BSC2 in line with how the companies invest. Investors can allocate their investment between the two VCTs in whatever ratio they choose.

The investment strategy of each VCT is to create a portfolio of UK companies operating across a broad range of sectors that blends a mix of businesses operating in established and emerging industries that offer opportunities in the application and development of innovation in their products and services.

There has been an increasing level of homologation across the two VCTs. Each VCT will invest in UK businesses across a broad range of sectors including but not limited to Data , Tech-enabled Services, New Media, Business Services, Application Software, Retail & Brands, Cloud & DevOps and Advanced Manufacturing. Details of the values in each Sector at 30 June 2023 are given below.

These investments will primarily be in unquoted UK companies which meet the definition of a Qualifying Investment, in order to maintain each VCT's Venture Capital Trust status. It is anticipated that the majority of these businesses will be re-investing their profits for growth and the investments will, therefore, comprise mainly equity instruments.

The BSC VCTs seek to build a broad portfolio of investments in early stage companies focused on growth with the aim of spreading maturity profiles and maximizing return as well as ensuring compliance with the VCT guidelines in this regard. The offer builds on the existing diversified portfolio of unquoted investments covering a large number of sectors.

Between them the two BSC VCTs had liquid funds as at 30 June 2023 totaling £117m

(after the receipt of £72m from the 2022/23 fundraising in April 2023). Since 30 June 2023 the VCTs have invested £4.4m; paid gross dividends of £3.7m; utilised £0.7m for three months of management fees and other net operating costs; and paid the BSC incentive fee of £0.1m. The expectation is that at the end of the 2023/24 tax year the cash before any funds from this offer will be around £70m.

Although this seems a high level of cash across the two VCTs, YFM say that this is necessary for their favoured follow-on investment strategy and between the two VCTs around £25m per annum is normally utilised for the share buy-back scheme, net operating costs and dividends (net of amounts reinvested from the Dividend Re-investment Scheme). The two VCTs have made investments totaling £63.4 million in the 21 months to 20 September 2023, of which £22.9m has been invested in the first 9 months of 2023.

The two British Smaller Companies VCTs operate similar investment strategies. Therefore, they also have a similar split of investments across different sectors, which is broken down as follows:

Sector	BSC	BSC2	Total
Data	24%	28%	26%
Application Software	21%	20%	20%
Tech-enabled Services	17%	17%	17%
New Media	13%	12%	12%
Business Services	12%	10%	11%
Cloud & DevOps	8%	8%	8%
Retail & Brands	4%	4%	4%
Other	1%	1%	2%
<b>Total</b>	<b>100%</b>	<b>100%</b>	<b>100%</b>

The similarities between the VCTs continue when looking at the top 10 holdings for the VCTs, which can be seen in Table 5. The largest holding in both by a considerable margin is Matillion Limited, which is approximately 12% of the NAV in BSC and 16% in BSC2.

YFM ideally likes to see at least £1m of sales

in the last 12 months, increasing commercial traction and seeks to make investment of a size commensurate with each businesses addressable market.

### **Dividend and Share Buy-Back Policy**

Both VCTs aim to pay a consistent annual dividend but this is dependent on the level of investment income and realisations that can be achieved in any one period and cannot be guaranteed. As covered above we think investors should no longer expect a regular smooth “yield” although distributable reserves will still allow VCTs to smooth dividends for a time.

There is also a dividend reinvestment scheme available to shareholders. Cumulative dividends to date of 176.9p (including a 2p dividend paid on 28 July 2023) and 84.75p have been paid from BSC and BSC2 respectively. BSC2 has declared a dividend of 1.5p, to be paid on 3 November

## **Track record**

Our approach to comparing track records between providers is to use 3, 5 & 10 year measures of the annual increase in total return (calculated as closing net asset value less opening net asset value plus dividends paid during the period).

The results are in Table 3 and consist of results for each provider and their VCTs over a 3, 5 and 10 year period. As can be seen in this table, the 3, 5 and 10 year annual returns for the BSC VCTs are some of the best over each of the time periods under analysis.

In order to reduce the data down to one figure we score each VCTs’ position in the results from 1 (top position) to the total number of VCTs in the analysis, sum them and take an average over the three periods being measured. Thus lower numbers are better and are in Table 4 .

The analysis in Table 4 shows that YFM’s performance places it second out of the list of generalist VCT managers.

Whilst these results are impressive and show up well in comparison to their peer group, they don’t tell the full story of how different VCT managers value their underlying investment portfolio.

2023.

The VCTs operate a share buy- back policy at a 5% discount to net asset value. In the twelve months to 30 June 2023 BSC acquired 3.2m shares at a cost of £2.5m, and BSC2 2.1m shares at a cost of £1.1m.

The current share prices are trading at a discount of 5% and 4% respectively.

### **Non-Qualifying Investments**

The initial proceeds of the Offer may be invested in a portfolio of equities, fixed income and other securities, including UK Government bonds, highly rated corporate bonds and cash deposits.

**Tax Efficient Review Strategy rating: 29 out of 30**

Valuing unquoted venture capital backed companies can be a nightmare of interpretation and analysis. The way the BSC VCTs structure their investments is with a high degree of reliance upon preference shares (which confer some form of “liquidation preference”) within the structure of the investment. To be clear, this is not a debt structure, but as the name suggests, it does give the investor in the preference shares a preference (or priority) on returns in the event of a sale.

Preference shares can be Participating (known as “hard” preference) or non-Participating (known as “soft” preference). Participating refers to whether after recouping any funds in preference to other shares, the shares continue to share in any funds still available.

For example, a Venture Capital investor may invest £5m into a company as non-participating preference shares with a 1x liquidation preference which have a priority on the first £5m (driven by the 1x preference) in the event of the sale of that company to a trade purchaser. So (assuming no other share class has a priority position) if the company is sold for only £5m, the investor will get their investment back but the other equity holders will get nothing. But if the company were sold for, say £15m, then



Table 3: Generalist VCT provider 3,5 &amp; 10 year performance comparison

VCT manager (alphabetical order)	VCT name	Data as at	Annual return over last 3 years	Annual return over last 5 years	Annual return over last 10 years
ALBION	Albion VCT	31/03/2023	6.2%	4.5%	5.9%
	Albion Technology & General VCT	31/03/2023	9.4%	8.7%	5.3%
	Kings Arms Yard VCT	31/03/2023	13.4%	6.6%	8.2%
	Albion Development VCT	31/03/2023	13.1%	9.9%	8.4%
	Crown Place VCT	31/03/2023	10.3%	8.6%	8.1%
BARONSMEAD	Baronsmead Second Venture Trust	31/07/2023	2.6%	-0.3%	3.5%
	Baronsmead Venture Trust	31/07/2023	2.0%	-0.7%	3.6%
BERINGEA	ProVen Growth & Income New	31/05/2023	4.6%	-0.1%	2.5%
	ProVen VCT	31/05/2023	4.3%	-0.9%	4.0%
CALCULUS	Calculus VCT plc New Ord share	31/05/2023	3.7%	-1.0%	
DOWNING	Thames Ventures VCT 2 Healthcare shares	31/08/2022	1.3%	-3.0%	
FORESIGHT	Foresight VCT	31/03/2023	19.1%	8.3%	4.7%
	Foresight Enterprise VCT	31/03/2023	14.6%	5.4%	1.5%
MAVEN	Maven Income & Growth VCT	28/02/2023	2.9%	2.3%	3.8%
	Maven Income & Growth VCT 4	30/06/2023	6.1%	2.3%	3.0%
	Maven Income & Growth VCT 3	31/05/2023	6.0%	2.0%	4.1%
	Maven Income & Growth VCT 5	31/05/2023	6.3%	3.6%	7.2%
MERCIA	Northern Venture Trust VCT	30/06/2023	10.6%	4.9%	5.2%
	Northern 3 VCT	30/06/2023	11.7%	4.9%	5.7%
	Northern 2 VCT	30/06/2023	11.3%	4.9%	5.2%
MOBEUS	Mobeus Income & Growth 4 VCT	31/03/2023	21.9%	10.5%	7.2%
	Mobeus Income & Growth VCT	30/06/2023	16.0%	11.6%	8.1%
	Mobeus Income & Growth 2 VCT	30/06/2023	14.6%	9.0%	7.7%
	Income & Growth VCT	31/03/2023	20.4%	10.9%	7.1%
MOLTEN	Molten Ventures VCT	31/03/2023	11.6%	3.6%	6.2%
OCTOPUS	Octopus Titan VCT	30/06/2023	-0.1%	1.0%	4.5%
PEMBROKE	Pembroke VCT B share	31/03/2023	7.2%	5.9%	
PUMA	Puma VCT 13	31/07/2023	16.4%	10.8%	
SENECA	Seneca Growth Capital VCT B shares	30/06/2023	-4.1%		
TRIPLE POINT	Triple Point VCT 2011 plc Venture shares	07/07/2023	7.8%		
YFM	British Smaller Companies VCT 2	30/06/2023	17.8%	9.1%	6.2%
	British Smaller Companies VCT	30/06/2023	18.5%	10.6%	7.5%

Source: Tax Efficient Review calculation based on dividend and Net Asset Value data from public accounts

Calculation: (Closing period NAV less Opening period NAV plus dividends paid in the period) divided by number of years in the period

Figures do not include tax relief

Report produced 24/09/2023

Table 4: Provider results comparison

PROVIDER	AVERAGE SCORE BASED ON PLACE IN PEER GROUP (lower is better)
MOBEUS	5
YFM	6
ALBION	11
FORESIGHT	14
MERCIA	15
MOLTEN	15
MAVEN	21
OCTOPUS	24
BERINGEA	25
BARONSMEAD	26

Calculation as at 24/09/2023 and based on results in Table 3 for providers with ten year performance. In order to reduce the data down to one figure, each VCTs' position in the Table 3 results is scored from 1 (first in the year) to the total number of VCTs in the analysis for the period (lower numbers are better), added together and then averaged over the three periods being measured

the preference shareholder would receive their £5m preference first and then the remaining £10m would be split across the remaining shareholder(s) as a normal equity participation.

Clearly, there are many, many ways in which preference shares can be structured in terms of the rights and return profile they give the investor/shareholder, and it's part of the negotiation of an investor when they come to put money into a Venture Capital/Private Equity company.

But TER would like to point out that these preference share structures do not provide any form of safety net or guarantees. If a company with preference shares in its equity structure folds with a nil value, then there is no recourse to take any preference on any remaining value.

Why is this important for the performance of comparing BSC VCTs to other VCTs which might not use preference shares? Well the preference shares mean that the BSC VCTs performance would be more "static" compared to others which do not use preference shares.

Whilst preference shares typically help to give a priority recoupment on a sale of a company, they also can have a reduced upside in exchange for this priority return. Table 8 has a column indicating the type of shares held by the VCTs:

31 were in participating shares, 3 in non-participating and 5 in just "naked" equity.

Prior to 2015, the structuring of investments with the use of secured loan stock/and or preference shares enabled the VCTs to generate more revenue income than, say, other VCTs which use external gearing. In addition, however, dividends can also clearly come from realised capital profits, and like many other VCT managers YFM has regard to a "total return" of longer term performance when advising the Boards on setting their dividend policy.

The balance of investment from 2015 has seen a heavier weighting towards TMT (Technology, Media and Telecoms), with a strong emphasis on Data, Tech-enabled Services, New Media, Application Software and Cloud & DevOps, in total 28 investments have been made in these sectors of which 24 were still in the portfolio at 30 June 2023. The three other investments that have been made since 2015 are all in the retail sector. The only failures in the portfolio since the first lockdown in March 2020 were one of the retail investments which was realised through an administration with no return to the trusts together with a broker trading business that was realised for minimal value in September 2022.

As at 30 June 2023 there were 41 investments

Table 5: YFM Equity Partners LLP VCT unquoted analysis of sector (% of original cost) as at 30 June 2023

Sector	%
Data	16%
Application Software	13%
Tech-enabled services	11%
New Media	8%
Business Services	7%
Cloud & DevOps	5%
Retail & Brands	2%
Advanced manufacturing	1%
Other investments	1%
Other current assets	1%
Cash etc	35%
<b>TOTAL</b>	<b>100%</b>

Source: YFM Equity Partners LLP

Table 6: YFM Equity Partners LLP VCT unquoted portfolio analysis of investment stage (% of original cost) as at 30 June 2023

STAGES	%
Growth (revenue £1m-£5m):	34%
Scale up (revenue over £5m):	66%
<b>TOTAL</b>	<b>100%</b>

Source: YFM Equity Partners LLP

Table 7: Realisation analysis including write-offs - last three years to 30 June 2023

Company	Activity	Date of investment	Date of exit	Total invested £	Total Proceeds £	Multiple
Matillion Limited (partial)	Data & Analytics	25/11/2016	06/10/2021	£1,210,000	£13,017,075	10.76
Deep-Secure Ltd	Software, IT & Telecommunications	09/12/2009	13/07/2021	£1,928,751	£12,364,310	6.41
Springboard Research Holdings Limited	Data & Analytics	14/10/2022	22/09/2022	£3,964,000	£16,416,489	4.14
Intelligent Office UK (via IO Outsourcing Limited)	Business Services	14/05/2022	22/09/2022	£4,890,000	£12,590,013	2.57
Tissuemed Limited	Health Care Equipment & Services	01/08/2000	21/12/2022	£322,337	£624,496	1.94
Vuealta Group Limited (partial)	Tech-enabled services	22/09/2021	19/12/2022	£4,923,915	£7,668,326	1.56
Wakefield Acoustics (via Malvar Engineering Limited)	Advanced Manufacturing	01/12/2014	09/01/2023	£1,800,000	£2,624,311	1.46
Harris Hill Holdings Limited	Business Services	01/06/2009	05/07/2021	£600,000	£431,183	0.72
Ncam Technologies Limited	New Media	01/03/2108	09/04/2023	£4,404,520	£2,982,725	0.68
Bagel Nash Group Limited	Retail	15/07/2011	15/10/2020	£2,074,008	£1,306,103	0.63
Seven Technologies Holdings Limited	Advanced Manufacturing	03/04/2012	25/11/2022	£6,974,278	£2,746,526	0.39
Friska Limited	Retail	13/07/2017	05/07/2021	£3,500,000	£0	0.00
Arraco Global Markets Limited	Business Services	20/12/2022	22/09/2022	£4,449,702	£0	0.00
<b>TOTAL</b>				<b>£41,014,511</b>	<b>£72,771,557</b>	<b>1.77</b>

Source: YFM Equity Partners LLP

in the portfolio, with BSC holding 39 unquoted investments valued at £126m and BSC2 holding 40 unquoted investments valued at £89m.

Despite this level of diversification, there is still a heavy reliance on the top 5 holdings within the portfolio. This is not an accusation at BSC VCTs in isolation as many VCTs are concentrated on the top 10 holdings. It is natural for VCT managers to undertake follow on investment rounds in their better performing companies. But one holding in particular, Matillion Ltd is held at £46m which represents approximately 14% of the investment portfolio, even after a couple of top-slicing sales.

But within the BSC VCTs the current top 5 holdings total £103m of the total £334m of AUM. The top 10 holdings equate to £142m.

Table 7 shows the exits achieved over the past 3 years. Within the 14 exits achieved, 8 of them have been profitable and at considerable margins to comfortably outweigh the losses with an average return multiple of 1.8x. The two exits achieved in 2023 (from January up to the end of September) show an overall multiple of 0.9x, although there is currently an additional value still held in Ncam which if realized at that amount would give an overall return of 1.5x.

## Manager

In 2022 YFM celebrated its fortieth anniversary and has now realised over 145 investments. The investment manager has also developed relationships with CEOs and NEDs of these businesses as well as their advisors across the UK regions.

The investment team has grown over time and now comprises 33 investment/portfolio directors/associates. This is one of the largest VCT teams in the UK and gives a substantial presence in each region giving the manager a larger reach than most. YFM says that this gives access to investment opportunities that many others do not see and which are not the subject of private equity auctions.

YFM has five offices providing national coverage and local presence and through which deals can be sourced. Over the last few years most deals

Like many other VCT managers, there has been a relative dearth of profitable exits in 2023. with Wakefield Acoustic being the only profitable exit in 2023.

The exits, alongside the performance of the remaining portfolio, have helped to drive a healthy level of dividends across the two VCTs. The average dividends paid over the last 5 and 10 years to 30 June 2023, as well as the level of cumulative dividends to date are shown in the two tables below:

### British Smaller Companies VCT

- Average over last 5 years: 6.9p
- Average over last 10 years 9.1p
- Cumulative since launch: 174.9p\*

\* 176.9p after the 2p dividend paid on 28 July 2023.

### British Smaller Companies VCT 2

- Average over last 5 years: 5.6p
- Average over last 10 years 4.8p
- Cumulative since launch: 84.75p

**Tax Efficient Review Track Record rating: 34 out of 40**

have been sourced through the YFM network and from the network of Chairmen and CEO's that they work with on a regular basis. The local offices see proprietary deal flow from local banks and intermediaries.

Not only must an investment manager obtain deal flow but it must have a team resourced to invest at the correct rate to satisfy the VCT rules. The 30% and 80% investment rules require that by the end of the first accounting period after launch that 30% of the fundraised must be invested and by the end of the third accounting period, and in every accounting period thereafter, the VCT must have at least 80% of its funds invested in qualifying holdings. In this case both VCTs have a preferred investment level of around 85% or more.

As well as VCTs, YFM manages a number of

Limited Partnership Funds, details of which are included in Table 2.

The growth capital funds, that invest alongside the VCTS, are dedicated to providing the replacement capital element of the transactions which the VCTs are unable to provide. The funds invest on the same economic terms as the VCTs. The buyout funds provide funding where the VCTs are completely precluded; focusing on supporting entrepreneurs, owners and management teams of small businesses throughout the UK.

The VCT position as to funds needing investing by the team is as follows.

Prior to the raising of these monies, the liquid funds of the two VCTs at 31 March 2024 are forecast to total c£70m. The initial offer, assuming the full over allotment facility is utilised, will raise around £86m after costs making a total of £156m.

With a NAV post fundraise of £420m this equates to approximately 37% of the NAV in liquid funds at 31 March 2024. In considering the deployment of cash, it should be noted that buybacks have recently been at historical lows and it would not be unreasonable for future annual levels to increase by c£5m. In addition, with an enlarged portfolio there is likely to be increased demand for further investments into this portfolio, which may increase the annual investment deployment envisaged of circa £45m.

The VCTs will likely always retain a level of cash of 15-20% of NAV or around £63m-84m. This would leave cash to invest of £72m -£93m from 31 March 2024 onwards.

Between the two VCTs around £25m per annum is currently utilised for the share buy-back scheme, net operating costs and dividends (net of amounts reinvested from the Dividend Re-investment Scheme). This would leave a net £47m-£68m to invest. This compares to investments (new and follow-on) of £63.4m in the twenty one months to 20 September 2023, of which £22.9m has been invested in the first 9 months of 2023 (figure supplied by YFM).

The LP funds position as to funds needing investing by the team is as follows:

The LP funds work differently. YFM tell us that

generally they would seek to invest 75-80% of the fund total over a three year period.

Growth Funds I and II are closed for new investment and Growth Fund III has commenced its investment period and is anticipated to invest £2.5m over the next year. £6.7m has been invested to date. YFM tell us that the Growth Funds might undertake small follow-on investments alongside the VCTs.

For Buyout Fund II, of the total fund of £80.4m, the amount for new investment is £60-64m of which £50.1m has been invested to date, so YFM have £10-14m to invest over the six months to the end of the investment period. £25.3m was invested in the 12 months to 30 June 2023 and YFM inform us that they have two investments totaling £13.5m undergoing due diligence. Buyout Fund I is also reviewing two further investments totaling £4.0m into its portfolio. YFM expect that the initial investment phase of BFII and the further investments into Buyout Fund I will have been completed by 31 March 2024.

YFM has recently announced the first close of Buyout Fund III, raising an initial £86.5m, and anticipate a final close of c£95m, which it would look to invest over the next 2 - 3 years into 9-10 investments of £6-8m each, so c£72m at around £20-25m per annum.

Between funds, this suggests the need for an average investment rate of £56-£72m per annum (£36m-£47m VCTs assuming a deployment rate over 24 months of the calculated above figures of £72m-93m of VCT cash; £20-25m BFIII).

YFM tell us that they invested £52.1m in new investments and £16.7m in follow-on in the 12 months October 2022 to 20 September 2023, a total of £68.8m

In our view this indicates that the team are well resourced to invest the funds being sought.

The principal members of the investment team are:

- David Hall (Executive Chair, 34 years' experience, ex Enterprise plc and PwC)
- Eamon Nolan (Managing Director, 24 years' experience)

- David Bell (Director – Head of Portfolio, 24 years' experience, ex-3i)
- Marcus Karia (Director – CFO, 15 years' experience)
- Ian Waterfield (Head of Investment-North, 21 years' experience)
- Jamie Roberts (Head of Investment-South, 11 years' experience)
- Steve Harrison (Head of Portfolio- North, 17 years' experience)
- Charlie Winward (Head of Portfolio- South 18 years' experience)

Table 10 shows the key team members. The VCT directors of the VCTs are:

**BSC VCT**

- Rupert Cook – Chairman
- Adam Bastin
- Jonathan Cartwright
- Purvi Sapre

**BSC VCT 2**

- Peter Waller – Chairman
- Barbara Anderson
- Roger McDowell

**Tax Efficient Review Team rating: 18 out of 20**

**Costs**

The costs for the British Smaller Companies VCT are as follows:

- **Initial costs:** The Initial Application Fee is 3.0 per cent of the Application Amount and is paid by the relevant Company to the Manager. In consideration, the Manager has agreed to meet the costs associated with the Offers, save for commissions payable to execution only brokers, on behalf of the Companies and the Manager will, therefore, be responsible for all of these costs. For investors who apply direct i.e. not via a broker or advisor the initial cost is 3.5%. Applicants who subscribe for the first £20m in the fundraising will receive additional shares equivalent to 0.25% of their application amount, and applicants who subscribe for the next £10m in the fundraising will receive additional shares equivalent to 0.125% of their application amount, the costs of which will be met by the Manager. In addition, to the extent possible, Applicants will receive additional New Shares equivalent to receiving a 3.70 per cent per annum rate of return on funds awaiting allotment, calculated by reference to the number of days between receipt of cleared funds and the date of allotment – a first for the industry.
- **Annual management fee:** 1% of surplus cash 2% of other assets. The annual fee for the twelve months to 31 March 2022 was £2,782,000, equal to 1.7 per cent of the average NAV.

The annual fee payable to the Manager is

calculated as 1.0 per cent on all surplus cash, defined as all cash above £7.5 million. The annual fee on all other assets is 2.0 per cent per annum. This is calculated half yearly at 31 March and 30 September.

In the year ended 31 March 2023 annual operating expenses (including the management fee but excluding any payment of the performance incentive) were 2.12% (they are capped at 2.9% of Net Asset Value). At this level the costs are at the lower end of charges for generalist funds.

- **Performance Fee:** 20% above the hurdle BSC has two hurdles, target levels of both Total Return (the “BSC Total Return Hurdle”) and dividend (“BSC Dividend Hurdle”). Subject to meeting the BSC Total Return Hurdle, the Manager will receive an amount equivalent to 20% of the amount by which dividends paid per BSC share exceeds the BSC Dividend Hurdle, multiplied by the number of shares in issue at the year end. The incentive fee in any financial year will be subject to a cap if the excess of dividends paid over the BSC Dividend Hurdle is greater than the sum of the excess of the Total Return over the BSC Total Return Hurdle divided by 1.2.

The Total Return Hurdle is increased annually by an RPI-adjusted 4.0 pence per BSC share. For the year ended 31 March 2024 the annual increase in the BSC Total Return Hurdle and the BSC Dividend Hurdle is 7.0 pence per BSC share.

A fee of £125,000 was paid in respect of the year ended 31 March 2023. As the Hurdles for the year ended 31 March 2024 have not been met to date, no accrual for a 2024 performance fee has been made at 30 June 2023.

The costs for the British Smaller Companies VCT 2 are as follows:

- Initial costs:** The Initial Application Fee is 3.0 per cent of the Application Amount and is paid by the relevant Company to the Manager. In consideration, the Manager has agreed to meet the costs associated with the Offers, save for commissions payable to execution only brokers, on behalf of the Companies and the Manager will, therefore, be responsible for all of these costs. For investors who apply direct i.e. not via a broker or advisor the initial cost is 3.5%. Applicants who subscribe for the first £20m in the fundraising will receive additional shares equivalent to 0.25% of their application amount, and applicants who subscribe for the next £10m in the fundraising will receive additional shares equivalent to 0.125% of their application amount, the costs of which will be met by the Manager. In addition, to the extent possible, Applicants will receive additional New Shares equivalent to receiving a 3.70 per cent per annum rate of return on funds awaiting allotment, calculated by reference to the number of days between receipt of cleared funds and the date of allotment – a first for the industry.
- Annual management fee:** 1% of surplus cash 2% of other assets, The annual fee for the twelve months ending 31 December 2022 was £1,786,000, equal to 1.7 per cent of the average NAV.

The annual fee payable to the Manager is calculated as 1.0 per cent on all surplus cash, defined as all cash above £5 million, as the hurdle has been met triggering a performance incentive payment. The annual fee on all other assets is 2.0 per cent per annum. This is calculated half yearly at 30 June and 31 December.

In the year ended 31 December 2022 annual operating expenses (including management fee but excluding any payment of the performance incentive) were 2.08% (they are capped at 2.9% of Net Asset Value). At this level the costs are at the lower end of charges for generalist funds

- Performance Fee:** 20% above the hurdle BSC2 also has a hurdle but different to that of BSCVCT. It's the aggregate of cumulative dividends paid as at the last Business Day in December each year and the average of the middle market price per BSC2 Share on the five Business Days prior to that day must exceed 120 pence per BSC2 Share (the "BSC2 Hurdle"). The fee is 20% of the excess over this amount multiplied by the number of BSC2 Shares in issue and the BSC2 Shares under option (if any). Once the BSC2 Hurdle has been exceeded it is reset at that value going forward, which becomes the new BSC2 Hurdle; the 2022 hurdle was 135.5 pence per BSC2 Share.

As at 31 December 2022 the total of cumulative cash dividends paid and mid-market price was 137.25 pence per ordinary share. Consequently the Hurdle (135.5 pence) was exceeded and a performance related incentive of £635,000 was paid. The Hurdle for the year ending 31 December 2023 is reset at 137.25 pence per ordinary share. The Net Asset Value and Total Return as at 30 June 2023 is stated after an incentive fee accrual of £1,180,000 in relation to the year ending 31 December 2023. The accrual is based on the total of the share price per Share and cumulative dividends paid as at 30 June 2023

In addition to the fees described above, which are paid by the VCTs, the Manager receives advisory fees in connection with new investments which are paid by the relevant investee company. In respect of each of the VCTs there is an aggregate annual cap applied to these fees for new investments of 3 per cent and for further investments of 2 per cent, with any fees above this cap being payable to the VCTs. Where expenses have been incurred and the investment does not proceed, the Manager pays any abort fees. The Manager also receives monitoring or non-executive director fees from unquoted portfolio companies. In respect of each of the VCTs these fees are capped at a maximum of £40,000 per annum for an unquoted company.

The aggregate of these fees received by the Manager in the twelve months to 31 March 2023 was £2,260,000, of which £333,000 was borne by the two BSC VCTs.

**Tax Efficient Review Cost rating: 8 out of 10**

## Conclusion

The British Smaller Cos VCTs are two VCTs, launched in 1996 and 2000, which now have over £334m split across the AUM of the two VCTs. Since launch they have generated a good level of annual dividends to shareholders, totalling 176.9p per share for BSC VCT and 84.75p per share for BSC VCT 2.

Under the stewardship of long term manager David Hall, these VCTs have been consistent fund raisers in the VCT market, but it's a symptom of the current market conditions that this fund raising has been launched in September, which is earlier than TER can recall them having launched in the past except for tax year 2021/22. After two historically good years for VCT fund raising, the declining AIM and UK small cap markets mean that the 2023 VCT market could mean VCT managers are coming out earlier this year to give themselves time to raise the funds they are seeking.

So what do advisers considering these VCTs get? They get two large investment portfolios with a geographically diverse range of investments. Compared to other generalist VCTs they are more concentrated in the number of investments which make up the £334m of AUM, particularly at the top end of the investment portfolio, with the top 5 holdings across the portfolio totalling £103m of the £334m.

This could make their performance particularly sensitive to movements in these top 5 companies, but the way that the BSC VCTs invest into their portfolio companies, with a reliance on ordinary shares with a participating preference, mean their performance is relatively more static than many of their peers. Whilst ordinary shares with a participating preference typically give a priority recoupment on a sale of a company, they also can have a reduced upside in exchange for this priority return. But to be clear, they do not form any type of guarantee or "debt style" investment, as if an investment returns zero, the ordinary shares with a participating preference return zero.

But the overriding reason why advisers should consider the BSC VCTs is the track record which they have managed to maintain over the past 10 years. Within the generalist peer group the BSC VCTs have been some of the best performers and this performance has been generated from a diverse number of exits over recent years. Whilst the UK private equity markets have been subdued over the past 18 months, the manager David Hall reports seeing an increase in their deal flow and an increase in the amounts of funding that entrepreneurs are now seeking over the long term, which could bode well for the future.

**Tax Efficient Review rating: 89 for a generalist VCT with a track record.**



Table 8: YFM Equity Partners LLP Unquoted portfolio analysis for Tax Efficient Review as at 30 June 2023

Investee Company	Residual Cost	Value	Date invested	Y/N	YFM is Lead investor-Y/N	Structure of investment (ordinary shares, soft non-participating, hard participating)	Industry Sector	Financing stage	Valuation method	Multiple on cost
	£000	£000		Syndicated						
KeTech Enterprises Ltd	£20	£4,220	11/2015	Y	Y	Soft non-participating	Tech-enabled Services	Scale-up	Note 1	211.0
DisplayPlan Holdings Ltd	£200	£13,583	01/2012	Y	Y	Soft non-participating	Business Services	Scale-up	Note 1	67.9
Vuealta Holdings Ltd	£152	£3,659	12/2022	Y	Y	Hard participating	Tech-enabled Services	Scale-up	Note 2	24.1
ACC Aviation Group Ltd	£365	£6,836	11/2014	Y	Y	Ordinary	Business Services	Scale-up	Note 1	18.7
Matillion Ltd	£3,234	£45,908	11/2016	Y	Y	Soft non-participating	Data	Scale-up	Note 2	14.2
Macro Art Holdings Ltd	£802	£1,817	06/2014	Y	Y	Hard participating	Business Services	Scale-up	Note 1	2.3
Unbiased EC1 Ltd	£9,327	£17,519	12/2019	Y	Y	Hard participating	Tech-enabled Services	Scale-up	Note 2	1.9
Outpost VFX Ltd	£7,500	£14,466	02/2021	Y	Y	Hard participating	New Media	Scale-up	Note 2	1.9
Elucidat Ltd	£6,600	£10,377	05/2019	N	Y	Hard participating	Application Software	Scale-up	Note 2	1.6
e2E Engineering Ltd	£1,500	£2,376	09/2017	Y	Y	Hard participating	Business Services	Scale-up	Note 1	1.6
Wooshii Ltd	£7,740	£11,635	05/2019	N	Y	Hard participating	New Media	Growth	Note 2	1.5
Force24 Ltd	£5,250	£7,930	11/2020	Y	Y	Hard participating	Application Software	Growth	Note 2	1.5
Traveltek Group Holdings Ltd	£2,879	£4,282	10/2016	Y	Y	Hard participating	Application Software	Growth	Note 2	1.5
Vypr Validation Technologies Ltd	£5,500	£6,931	01/2021	Y	Y	Hard participating	Tech-enabled Services	Growth	Note 2	1.3
EL Support Services Ltd	£1,000	£1,338	04/2015	N	Y	Hard participating	Other	Growth	Note 3	1.3
Tonkotsu Ltd	£3,980	£4,578	06/2019	Y	Y	Hard participating	Retail & Brands	Scale-up	Note 1	1.2
Automate Pro Ltd	£3,708	£4,443	12/2022	Y	Y	Hard participating	Cloud and DevOps	Growth	Note 2	1.2
Sharpcloud Software Ltd	£5,678	£6,419	10/2019	Y	Y	Hard participating	Data	Growth	Note 2	1.1
Xapien (via Digital Insight Technologies Ltd)	£2,900	£3,100	03/2022	y	y	Hard participating	Application Software	Growth	Note 2	1.1
OC Engineering Services Ltd	£1,000	£1,072	04/2015	N	Y	Hard participating	Other	Growth	Note 3	1.1
Quality Clouds Ltd	£6,526	£6,720	04/2022	Y	Y	Hard participating	Cloud and DevOps	Growth	Note 2	1.0
DrDoctor (trading as ICNH Ltd)	£5,942	£5,942	02/2022	Y	Y	Hard participating	Application Software	Scale-up	Price of recent investment	1.0
Workbuzz Analytics Ltd	£4,295	£4,295	06/2023	Y	Y	Hard participating	Application Software	Growth	Price of recent investment	1.0
Plandek Ltd	£3,450	£3,450	10/2022	Y	Y	Soft non-participating	Cloud and DevOps	Growth	Note 2	1.0
Summize Ltd	£3,000	£3,143	10/2022	Y	Y	Soft non-participating	Application Software	Growth	Note 2	1.0
Frescobol Carioca Ltd	£3,000	£3,110	03/2019	N	Y	Soft non-participating	Retail & Brands	Scale-up	Note 2	1.0
Biorelate Ltd	£2,600	£2,584	11/2002	Y	Y	Hard participating	Application Software	Growth	Note 2	1.0
Paninsight Ltd	£2,500	£2,500	11/2019	Y	Y	Hard participating	Data	Growth	Note 2	1.0
NB Technology Services Ltd	£1,000	£894	04/2015	N	Y	Hard participating	Other	Scale-up	Write-down up to 15%	0.9
TeraView Ltd	£754	£676	12/2011	Y	N	Hard participating	Advanced Manufacturing	Growth	Write-down up to 15%	0.9
SH Healthcare Services Ltd	£1,000	£830	04/2015	N	Y	Hard participating	Other	Scale-up	Write-down 26% to 50%	0.8
Relative Insight Ltd	£6,340	£4,490	03/2022	Y	Y	Hard participating	Tech-enabled Services	Growth	Write-down 26% to 50%	0.7
Sipsynergy (via Hosted Network Services Ltd)	£4,699	£2,843	06/2016	Y	Y	Hard participating	Cloud and DevOps	Growth	Write-down 26% to 50%	0.6
Eikon Holdco Ltd	£1,250	£592	03/2018	N	Y	Soft non-participating	New Media	Scale-up	Write-down 26% to 50%	0.5
Arcus Global Ltd	£5,125	£450	05/2018	Y	Y	Hard participating	Application Software	Growth	Write-down 76% to 100%	0.1
SP Manufacturing Services Ltd	£1,000	£16	04/2015	N	Y	Hard participating	Other	Scale-up	Write-down 76% to 100%	0.0
Biz2Mobile Ltd	£3,163	£0	10/2016	Y	Y	Hard participating	Application Software	Growth	Write-down 76% to 100%	0.0
Intamac Systems Ltd	£1,208	£0	06/2014	Y	Joint lead	Hard participating	Lifesciences	Early stage	Write-down 76% to 100%	0.0
Immunobiology Ltd	£2,699	£0	06/2003	Y	N	Hard participating	Business Services	Early stage	Write-down 76% to 100%	0.0
<b>TOTAL GROWTH PORTFOLIO</b>	<b>£128,886</b>	<b>£215,024</b>								<b>1.7</b>

Note 1: Earnings: Uplift in value, manager valuation based on earnings multiple

Note 2: Revenue: Uplift in value, manager valuation based on revenue multiple

Note 3: Net assets: Uplift in value, manager valuation based on net assets

Source: YFM Equity Partners LLP

Table 9: Matrix of individual responsibilities YFM Equity Partners LLP where Deal Origination & New Deal doing exceed 30% of an individual's time and with at least three years VCT involvement 30 June 2023

NAMES	David Gee	Jamie Roberts	Ian Waterfield	David Wrench	Andy Thomas	Mike Clarke	Dan Freed	Roshan Puri	Helen Villiers	Adam Hart	Laura Sisson	Matt Gordon- Smith
<b>VCT RELATED WORK</b>												
Deal origination	10%	20%	20%	30%	30%	30%	30%	30%	30%	30%	30%	30%
General enquiries												
New deal doing	40%	40%	40%	40%	40%	40%	40%	40%	40%	40%	40%	40%
Investee board observer seat												
Investee board director seats No.												
Sitting on Boards/Monitoring		5%	5%	5%	5%	5%	5%	5%	5%	5%	5%	5%
Fund raising												
Internal issues	15%	10%	10%									
Exits												
<b>NON VCT WORK</b>												
Non VCT work	35%	25%	25%	25%	25%	25%	25%	25%	25%	25%	25%	25%
<b>TOTAL</b>	<b>100%</b>			<b>100%</b>	<b>100%</b>	<b>100%</b>	<b>100%</b>					
Years in venture capital	35	11	21	3	10	7	10	7	5	7	3	13
Years involved with VCT Funds	35	11	21	3	10	7	10	7	5	7	3	13
Years with current team	35	11	15	3	6	5	5	3	5	5	3	1

Source: YFM Equity Partners LLP