BVCA Autumn Budget 2024 Representations: Driving UK economic growth and investment

Ahead of the Government's budget on 30 October, we are pleased to share with you the British Private Equity and Venture Capital Association (BVCA)'s recommendations. These proposals will support the Government in achieving its ambitions for driving economic growth built on stability, investment and reform, and forged through partnership with the private sector.

We welcomed the Government's ambitions thus far including the Pensions Review, the National Wealth Fund, and the drive to boost infrastructure and house building, all of which will facilitate further investment into businesses across the UK. We believe our proposals, outlined below, will complement the Government's plans to ensure that the UK maintains its position as a global hub for investment and remains one of the best places to scale and grow a business.

The private equity and venture capital (private capital) industry is an indispensable partner for UK economic growth, standing as it does at the unique intersection of deploying capital, investing for the long term and helping to shape the strategy of the British businesses it invests in. In 2023 alone, it directly supported 12,000 businesses, generating 2.2 million jobs and contributing 6% to GDP across all sectors.

In 2022, private capital firms in the UK raised a record £70.2bn, which brings the stock of available capital managed from the UK to £145bn. This is known in the industry as 'dry powder' and is expected to be invested over the next 3-5 years to help businesses innovate and grow.

Capital is mobile. To drive economic growth, we must bring that capital here, both by encouraging the global investors to put their capital in UK funds and by ensuring that investors have the confidence to invest in UK businesses.

The main themes of our submission are a stable and competitive tax framework, harnessing productive UK assets through investing pensions into private capital, and promoting opportunities for innovation and scale-ups, all of which will support the Government's Growth Mission.

Beyond this, to ensure the UK retains its place at the centre of the global financial ecosystem and can realise a sustainable and prosperous future for all UK nations and regions, we make recommendations to support the financial services sector and the Net Zero transition.

The BVCA is the industry body and public policy advocate for the private equity (PE) and venture capital (VC) industry in the UK. With a membership of over 600 firms, we represent the vast majority of all UK-based private capital firms, as well as their professional advisers and a large base of UK and global investors.

A stable and competitive tax framework for growth

BVCA welcomes the Government's recognition that private capital channels vital investment across the UK and will play an important role in boosting economic growth. We were pleased to respond to the Treasury's call for evidence on carried interest. Our response can be viewed here.

The current treatment of carried interest in the UK is – along with the wider regulatory and tax framework – at the heart of the internationally competitive investment environment which has made the UK an important hub for private capital. The treatment also reflects the long-term economics at the heart of the investment approach: institutional investors allocate risk capital to fund managers in the industry for a ten-year period (typically), in the expectation that the managers will deliver significant capital appreciation (and therefore returns) through active, long-term management, which is rewarded through a share in the realised capital return. The tax treatment reflects this economic reality and is consistent with other international jurisdictions.

The UK is currently the largest hub for private capital investment in Europe and is regarded as a world leading location for businesses to start up and grow, with clear and long-standing ambitions to attract global investment and grow UK businesses. It is critical to the Government's ambitions for increased private investment and growth that the UK remains an attractive and internationally competitive place for private capital firms to locate and invest.

To ensure a stable and competitive tax framework for growth, the BVCA calls for:

- **Any detailed changes to the carried interest regime to undergo a full and careful consultation.** A proper consultation process would help to ensure that the potentially complex impacts of any proposed detailed changes can be fully considered and assessed and avoid disruption and damage to the industry, investment and growth in the UK.
- **Safeguarding the international competitiveness of the UK private capital sector** to maintain the flow of domestic and international investment capital into UK businesses.
- **Any changes that may be introduced to be forward-looking**. Retrospective taxation would harm the UK's reputation when businesses are deciding where to establish themselves and invest. It is essential to respect the legal realities of existing funds being at differing stages of maturity over their minimum ten-year duration, and not having the ability to change their structure (and associated economics) at this stage.
- **Private capital funds must be able to retain flexibility in structuring that is possible under current rules,** including the ways in which carried interest and co-investment can be structured. We strongly advocate that the Government continues to engage with the industry to ensure that different variations and complexities are fully considered.
- **Any changes to the UK tax system should avoid complexity and being overly prescriptive.** While the underlying principles applying to carried interest are consistent across different types of fund, there are significant variations in implementation, so changes must be made carefully to ensure investment activity and the innovation and evolution of the industry is not limited.

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- **More broadly, tax incentives to encourage long-term investment and entrepreneurship must be retained.** The UK has long been the hub of the world's financial markets, with a reputation as a safe and secure home for investment and an incubator of entrepreneurial talent. It is vital that we do not lose this reputation. Any changes to the capital gains tax system that would markedly reduce incentives for entrepreneurs to start and build business, and for investors to make the necessary long-term commitments to enable innovation and growth in businesses across the UK, could have a negative effect on investment and growth in the UK.
- **Finally, we welcome the commitment to publish a tax roadmap** offering stability and certainty for businesses and investment.

Investing pensions for growth to harness productive UK assets and bolster returns for pensions savers

We are encouraged by the speed at which the Government brought forward its pensions review and announced the Pensions Schemes Bill. It is more important than ever that we find ways to boost the UK's economic growth and the retirement prospects of pension savers. To do this, we need policies that help UK pension schemes access longer-term investments in private capital, which can then be invested into UK businesses, boosting economic growth whilst delivering higher returns for savers.

Despite the UK having one of the largest pension sectors in the world, UK pension schemes, relative to global peers, currently invest very little in private capital. Sixteen times more capital from pensions around the world goes into UK private capital than from UK pension funds. Moreover, the PLSA estimates that only 35% of households saving into a DC pension will meet the 'moderate' level of retirement income, as set out in the Retirement Living Standards. This means UK workers are missing out, whilst overseas pension savers benefit from the diversification and strong returns generated by the growth of UK private companies.

We encourage the Government ambitiously to explore a wide range of options in its review and build on the work of the Pensions and Private Capital Expert Panel. The Panel will publish its recommendations on September 11 for a series of structural, technical and wider policy options designed to contribute towards better outcomes for UK savers in DC pension schemes and greater investment in high growth businesses in the UK.

To begin investing pensions for growth, the BVCA calls for:

- **A new pensions investment roadmap to be set out by Spring 2025**, following the Pensions Review, outlining the steps expected from both the pensions and private capital sectors to enable increased UK investment and higher returns for savers.
- **Implement the Pensions and Private Capital Expert Panel's recommendations for how Government can help pensions invest into private capital.**
    - The pensions industry should be empowered by Government to move away from short-term cost considerations, towards a more holistic focus on long term adequacy. The emerging Value for Money framework will be key to this.

    - As the Government considers the creation of a new investment vehicle or scheme that enables further opportunities to invest in innovative and emerging sectors, it should draw lessons from overseas initiatives, such as the French 'Tibi' scheme.
- **Government-backed action to encourage consolidation in the pensions industry** into fewer, larger schemes to increase pension schemes' ability to deploy capital into growing UK businesses through UK private capital funds.
    - The Government should ensure that the emerging Value for Money framework sets out a clear plan for those schemes found to be consistently not offering value to savers.
    - Implementing regulatory changes designed to encourage the direct consolidation of the small pots which make up a large part of the 28,000 UK DC pension pots.
    - Exploring how the assets of the LGPS should be effectively pooled.
- **Across all pension schemes, the Government should give consideration to how easily schemes can invest in regional and smaller projects,** and avoid scenarios whereby pensions are effectively only able to invest in projects or funds of a certain size. This is particularly relevant in LGPS, where there is significant institutional knowledge of regions, and a long history of supporting innovation private capital projects.
- **Increase pensions investment opportunities through expanded Government support for the British Business Bank**, with new vehicles and more funding for programmes that support emerging managers, growth deals and growth funds.

We welcome the announcement of a call for evidence on pensions investment and will provide further suggestions as part of that exercise, ahead of the Budget.

Promoting innovation and scale-up opportunities for growth

While the UK has a strong funding ecosystem at the early stage, the 'scale-up' stage of VC investing often prompts UK companies to seek investments from the US and elsewhere. We welcome confirmation from the Government that the EIS/VCT sunset clause will be extended to 2035. This provides much needed certainty and will support early stage companies to raise the financing they need to grow and succeed.

Innovative UK businesses need this capital to create large-scale, independent, businesses, but relying on foreign investment to scale-up UK companies exposes the UK to geopolitical risk and fluctuations in global capital allocations.

The UK has a strong track record in science and technology research but loses out on opportunities when companies move overseas, taking intellectual property, quality jobs, and innovation with them. Other issues related to lack of infrastructure further inhibit the UK from being a global scale-up destination for the largest tech companies.

The UK should be the best place to both start and scale a business. That means protecting our world class universities, having investor support for spin-outs and encouraging a greater appetite for risk taking at later stages to ensure companies can scale in the UK.

To drive innovation and scale-up opportunities for growth, the BVCA calls for:

- **Supporting the appetite to grow truly global businesses**, by:
  - Increasing funding for programmes such as British Patient Capital and Future Fund: Breakthrough, which have already been successful in scaling later stage funding rounds for UK tech companies.
  - Lifting the EIS Knowledge Intensive Company upper limit from £20m to £30m so R&D intensive IP rich companies in sectors such as biotech and deeptech can continue to raise capital after hitting the current ceiling.
  - Raising limits placed on EIS and VCT funds to access the schemes because regional funds take longer to reach the stage when they are able to receive institutional investments from VCs. Regional EIS and VCT funds in particular are often constrained by restrictions such as the 7-year rule.
  - Unlocking domestic institutional capital (from DC pension schemes and insurance companies) for investment into UK funds and later investment rounds and addressing issues around investment culture.
- **A comprehensive, long-term, properly funded Government R&D strategy with expanded R&D tax relief to incentivise genuine innovation and pioneering investment in the UK**.
  - R&D tax credits allow research-driven companies backed by private capital to reinvest in their future growth, but the UK's regime isn't as attractive as those of international competitors, and the process for obtaining these credits is too slow. The UK must strengthen and solidify its offer by including long-term public funding commitments and R&D intensity targets.
- **Expansion and simplification of Government programmes and incentives which deliver predictability and support to groundbreaking ventures and innovative companies,** by:
  - Increasing the scope of the Enterprise Capital Fund Programme (ECF). The ECF has been successful in backing first time and emerging VCs; however, it has been limited to backing one to two funds a year. The government corporate venturing model, which has successfully been deployed by the National Security Strategic Investment Fund (NSSIF), should be expanded to other strategic sectors such as healthcare. This will help increase collaboration between Government, VCs and innovative companies, to improve procurement processes and access to the latest technologies.
  - Clarifying the future of grant and match-funding schemes like the BBB's Future Fund: Breakthrough and Regional Angels Programme, considering further extension and expansion.
  - Introducing new Government-backed vehicles for investment pooling or co-investment in strategically important sectors. These should support minority and majority stake

investment in growing businesses across the business life cycle and have a conscious goal of building fund scale and expertise in the UK.
    - Providing clarity on the scope and remit of the National Wealth Fund (NWF) and ensuring that the development of any vehicle considers the funding provided by existing Public Finance Initiatives (PFI). The NWF could provide a much needed source of domestic capital for growth stage companies, to ensure that the most innovative UK businesses, including companies developing solutions to the energy transition, can continue to remain and grow in the UK.
- **Maintain Business Asset Disposal Relief (BADR)** for entrepreneurs and founders who start and build breakthrough businesses in the UK. While a better targeted regime could carve out low risk-bearing assets, it is essential that those who risk capital to invest in pioneering ventures continue to be incentivised to do so.
- **Industry to be a partner in identifying and addressing skills gaps while promoting education in STEM, data science, technology and entrepreneurship.** The UK is a leader in tech, life sciences and financial services innovation, but all of these industries need a strong talent pool with STEM skills to capitalise on global investment.
- **Full implementation of the findings of the Independent Review of the UK's University Spin-out Companies** by:
    - Ensuring the rapid adoption of best practices outlined by the TenU initiative by all university stakeholders, in particular university tech transfer offices.
    - Expanding the £20 million translational fund as UKRI funding often falls short in advancing technology to the commercialisation stage. Further funds and expertise should be provided for UKRI, Innovate UK and early stage university funds in the nations & regions, to help build a national pipeline of high growth companies ready to scale.

Financial Services Sector for Growth to make sure the UK remains the international destination for investment

It is vital that the UK retains its place at the centre of the global financial ecosystem so that private capital continues to choose to invest in the UK and help UK businesses thrive. This requires regulation which takes a common-sense approach, is applied consistently, and equally balances incentivising growth with upholding world-class standards. Regulatory frameworks must be flexible, proportionate, and clear enough to allow capital to flow efficiently and predictably through UK structures.

To support a financial services sector for growth, the BVCA calls for:

- **A cross-cutting Government review of regulation of innovative technologies,** focused on areas where regulatory capacity is holding back innovation and growth, and where legislation has not kept up with technological possibility.
- **Improvements to the functioning of the National Security and Investment (NSI) Regime to strike the right balance between protecting national security and encouraging investment in the UK, including:**

- Not increasing the scope of certain aspects of the regime, as suggested in the previous government's Call for Evidence in 2023, but instead looking to narrow and focus it. Mandatory sectors should be refined and types of transactions (such as internal restructuring) should be removed from scope.
    - Offering more official guidance and communication from the ISU to reduce uncertainty and delay in transactions.
    - Aiming to speed up the timing of ISU reviews, which are often prolonged. This delay can significantly impact Venture Capital firms in particular which need to invest nimbly into fast growing companies.
    - Removing the clause in legislation related to Automatic Invalidity for failure to file under the mandatory regime. Under the mandatory regime, if a notification is not made where it should have been, there is automatic invalidity. We believe that this is legally flawed for agreements governed by laws in jurisdictions other than the UK, it is disproportionate and should therefore be reviewed.
- **Better calibration of UK legislation and regulation to support the competitiveness of UK private capital.**
    - There are several areas of UK legislation and regulation that unnecessarily "gold-plates" the original EU Directive approach, imposing more complex regulation and putting UK firms at a competitive disadvantage, often with little or no benefit for investors. Our response to the FCA's 2023 discussion paper on updating and improving the UK regime for asset management includes a number of recommendations to improve competitiveness and is available here.
    - We look forward to working with HM Treasury and the FCA to enhance proportionality and improve the competitiveness of the UK regulatory regime for alternative asset managers as part of the Smarter Regulatory Framework (SRF).
- **Increased resources for regulators that face particular challenges keeping up with technological change.**
    - For regulators financed at least in-part by the Government, the Treasury should permanently uplift funding to restore their 2021 budgets in real terms to recoup core, 'business as usual' capacity, and also commit to annual, inflation-linked budget increases to accelerate new efforts.
    - Expand the Regulatory Pioneers Fund to £50m initially, in time rising to £100m+, to provide dedicated surge capacity for regulatory innovation projects on top of core funding increases.

Unlock private capital and support SMEs for sustainable growth

Nine out of 10 businesses supported by BVCA members are SMEs, making private capital well placed to both drive the transition towards Net Zero and encourage regional economic development in areas of the economy that public markets cannot reach.

To unlock this capital, it is essential that clear and consistent commitments and actions on public spending and policy for Net Zero are well communicated and understood which cover the full spectrum of private capital and associated policy or capital needs.

The UK needs proportionate and interoperable sustainability regulation that supports private capital investment and its portfolio companies, retaining our position as a world leader on green finance and the Net Zero transition. Similarly, SMEs, whose primary focus is to grow their business, must not be overburdened. Resources and incentives that enable SMEs to understand and execute decarbonisation will be crucial to this process.

To unlock private capital and support SMEs for sustainable growth, the BVCA calls for:

- **More private capital for the energy transition and social agenda.**
  - Develop a Net Zero Blueprint, setting out clear commitments and actions on public investment and policy including for sectors with clear planning and fiscal arrangements in key areas. This is vital to ensure that the right policy levers are used to encourage more capital to be deployed, depending on the type of private capital needed. Investors need to have confidence in the long-term financial viability of investments and clarity on policy direction will also help to coalesce funding around the technology best able to drive the green transition.
  - Build out blended finance frameworks and options with specific case studies, ensuring the government's approach caters to companies at every stage of their investment journey, providing clear and easy-to-follow guidelines for scaling options from start-up to more mature companies.
  - Enable the supportive environment to incentivise and help scale private capital to invest in sustainable solutions and services which increase public well-being and improve the quality and capacity of public services.
  - Ensuring that Public Finance Institutions, such as the National Wealth Fund (NWF) are focusing on the green sectors where the UK can have a competitive advantage and the potential to be a global leader. It is important that these mechanisms not only channel capital to the founders developing the solutions of tomorrow but also to those businesses which need to grow. We need a supportive environment which enables them prosper in the UK. It is also critical that their strategies and objectives focus on streamlining procurement and expediting talent acquisition and that government departments are aligned to reduce ineffectiveness.
- **Incentives and support for SMEs to work towards Net Zero targets while allowing them to grow.**

- Define what Net Zero means for SMEs and what ‘good’ looks like and establishing a ‘one stop shop’ for the resources, skills, guidance, and approaches needed.
- Incentivise decarbonisation progress through mechanisms such as tax breaks for those that make meaningful progress to the global race to Net Zero.
- Shorten time-horizons and implement voluntary targets set for SMEs to enable businesses to decarbonise step-by-step.
- Set out definitions as to what constitutes transition finance for different sectors and industries. Transition finance should focus decarbonisation efforts within hard-to-abate sectors whilst also considering how transition finance may help in scaling up green technology companies which, once scaled, may significantly contribute to the decarbonisation effort.

In closing, we welcome the Government’s commitment to secure the highest sustained growth in the G7. Private capital stands ready to help the UK economy grow. But we need the right policy environment to do. We believe the measures contained above will ensure a stable economy, world-class regulatory standards, support for an investment ecosystem and predictable policy frameworks, all four of which are essential to ensure stable foundations for growth.