holden
& partners

H&P Review

CLEAN ENERGY

Opportunities in a diverse market

Also in this issue:

Taking a look at the companies avoiding tax

Planning for the cost of your family's education

Understanding auto enrolment

Finding out the risks of retail bonds

ISSUE 8
AUGUST 2013

Holden & Partners is the trading name of Peter R T Holden & Partners LLP and is authorised and regulated by the Financial Conduct Authority

"The UK is ahead of the rest of the world in making our new infrastructure low carbon."

By **Steve Pyne**, Partner

The intervening months since our last edition of H&P review have seen the economy, energy production and ethical investment all make the headlines for differing reasons. These are themes which are relevant for many of our clients.

Positively, at the end of July, the Office for National Statistics reported that the UK economy expanded by 0.6% during the three months to the end of June. That's twice the growth rate witnessed during the first quarter of the year. The Organisation for Economic Co-operation and Development has suggested the UK recovery is rapidly gathering momentum. Britain has been on an upward trend since June last year and has been showing signs of growth since September. It has now joined a small group of "firming" economies, with the US and Japan. However, beyond the headline numbers, real wages have continued to fall, as inflation (despite extremely weak growth over the last three years) continues to erode purchasing power. Even allowing for population growth, British GDP per head is actually some 7% below its 2007 peak. Unemployment and underemployment both remain stubbornly high.

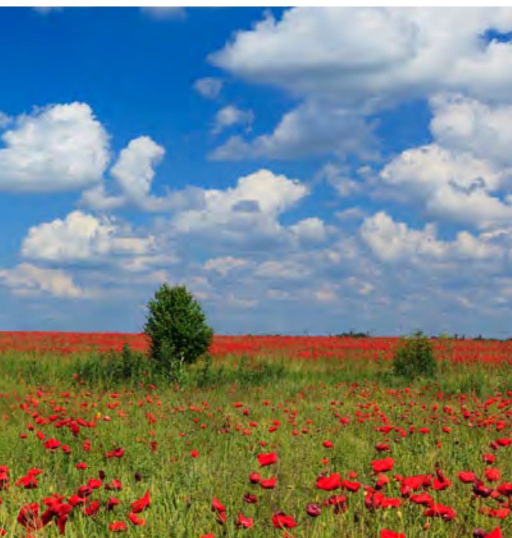
The question is whether we are witnessing a short term blip, or a return to long term prosperity for the majority of the population. The problems of youth unemployment, a potential new housing bubble, a possible Asian slowdown, weak growth in the US and ongoing problems in the Eurozone, all have to be factored in before any real definite conclusions can be drawn.

In the last month, we have seen the government, controversially, throw its weight behind the extraction of shale gas from the UK. Mankind remains a profligate user of energy and in the UK, vast numbers of the population use gas to heat their homes. Most sources of large scale energy production attract negative publicity and the truth is that everything from wind to nuclear power will have an impact on the environment in some way. Those living closest to the sites of energy production inevitably feel the impact more closely. Whilst we continue to use energy at current levels there will be pressure to find short term solutions to a long term problem. If we are interested in conserving the environment, we all have a responsibility to use less energy, however inconsequential our individual efforts may seem.

Findings from a recent poll conducted by You Gov seem to highlight the dilemma Britains feel on power generation and clean energy. Paradoxically, 78% of respondents said the government is right to spend money encouraging solar power projects, whilst 76% said the same for tidal, and 65% backed financial support for wind. On the other hand, 57% backed government support for clean coal, with 49% for nuclear power and 40% for shale gas extraction. However, in the same poll, 41% said that Britain should start extracting shale gas by fracking, while 33% said that it should

not. Despite concerns over its safety and environmental impact, 68% said that they believed it would be good for the economy, but only 25% said they would want fracking to begin in their local area. Interestingly, whilst the fracking debate has dominated the news, there have been some more positive signs for the low carbon economy. Green Alliance, the environmental and economic think tank, has found in a new analysis of the UK's low carbon infrastructure, that the UK is ahead of the rest of the world in making our new infrastructure low carbon. We are already a world leader in offshore wind and planned low carbon infrastructure projects make up over 70% of the government's infrastructure pipeline. This will create a cleaner, more productive economy, that will allow the UK to prosper while respecting environmental limits. The readiness of many of these projects also means they can have a significant short term growth impact, creating jobs and attracting investment at a time when the country desperately needs them. Green Alliance has found that an increase in spending on low carbon infrastructure projects should increase GDP by at least 0.7% by 2015. Conversely, if the government abandoned its low carbon investment programme, the overall impact on GDP could be a reduction of as much as 2.2% and such a drop could push the UK back into recession.

It is not often that ethical investment makes the headlines but the stinging comments made by the Archbishop of Canterbury, on the 'pay day lender' Wonga, which were then followed by revelations that the Church of England itself had a direct investment in the firm, ensured that ethical investment received widespread media coverage. The church has since announced a review of its investment screening process. The issue however does demonstrate how difficult the area of investment screening actually is. The mainstream media were quick, perhaps quite legitimately to ask questions such as "Can investments ever be ethical?" and debate whether "There is any such thing as an ethical investment." Interestingly, Simon Howard, chief executive of the UK Sustainable Investment and Finance Association (UKSIF) made the following comments in response "I don't think ethics are an absolute; everyone must develop their own views. I believe that investment can do good or ill, that some activities should not be funded because of their environmental (including climate) or social impact, and that anyone who tries to reflect this in their investments is doing the right thing. Increasingly too, fund managers and companies understand the risk to share prices from poor practice in terms of environmental and social behaviours. The need for sustainable as well as ethical investment is becoming better recognised across the investment chain."



In the latest edition of H&P Review, as investment returns begin to improve for clean energy funds, we look at whether the tide is finally turning for the fortunes of clean energy investors and whether responsible investment can crack down on corporate tax avoidance. We also consider how parents can plan to help meet the ever rising cost of school fees.

The implementation of auto enrolment now makes it compulsory for some employers to make pension contributions on behalf of their employees. We detail the basics and give details on what all employers need to know. Finally, we draw attention to the growing area of direct retail bonds and evaluate the pros and cons.

In this ISSUE

Welcome — 03
The latest issue of our Review

Schools Not Out — 04
Planning for the cost of your family's education.

Fairweather Visitors — 05
Can responsible investment help crack down on tax avoidance?

Clean Energy — 06
Finding the right opportunites.

Retiring Gracefully — 07
How auto enrolment works.

Caveat Emptor — 08
The risks and rewards of retail bonds.

You can also find these and other articles on our website:

www.holden-partners.co.uk

and on our social media sites:

Facebook.com/holdenandpartners
Twitter.com/holdenpartners
Linkedin.com/company/holden-&-partners

If you would like or prefer to receive a PDF version of our magazine in the future please email us at hpreview@holden-partners.co.uk

School's Not Out

The implications of your family's education

By **Mark Dodd**, Partner

Every parent wants the best for their children, and when it comes to education, this can lead to a consideration of private schooling and the potential cost. Parents are generally aware that school and university fees can represent the single greatest cost of being a parent, though they may not have quantified the likely cost or thought about how they might fund it.

According to a study by Lloyds TSB in 2012, average school fees have risen by 68% over the last decade, from £6,280 in 2002 to £11,457. That's 1.8 times faster than retail price inflation over the same period. There is a wide range in costs, with some of the best known schools in the UK costing three times the average.

So, on the assumption that you want to send your two 11-year-old children to a private secondary day school in the 2020s - if fees continue to rise at a similar rate over the next decade - seven years of education could set you back around £270,000! Educate them both privately from the age of five and you're looking at £500,000.

Finding a good local state school that offers the education you really want for your children can sometimes be easier said than done, so planning ahead is essential. It is clearly never too early to start planning, even if you are not sure whether you will actually choose private education for your children.

Looking at all the possible options, and even combining them to help you reach your goal is important if you want to maximise your investments and minimise the impact school fees have on your lifestyle.

Many of our clients consider downsizing their home or asking grandparents to help, though if this isn't a practical solution and you are committed to educating your children privately, then you will need to consider alternative options.

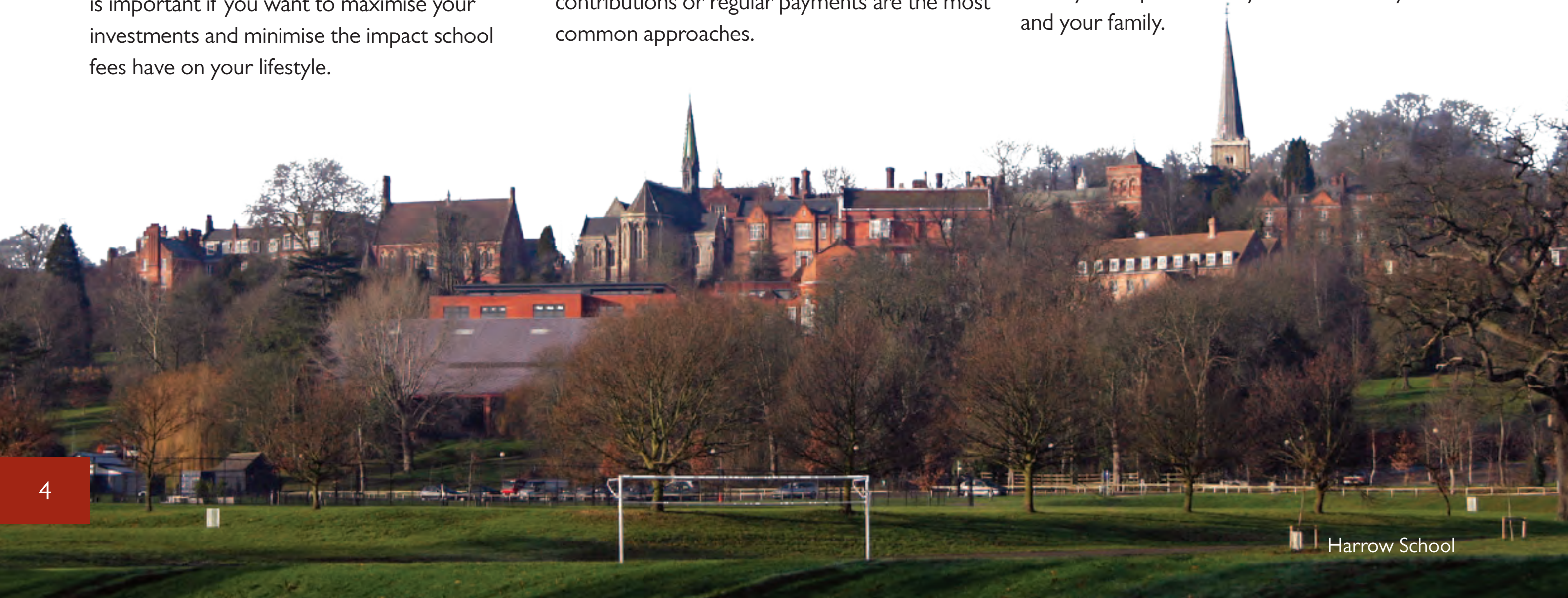
More recently, this has been compounded for families where one parent earns more than £50,000, which will now result in the loss of some or all of your child benefit entitlement. The secret of paying school fees is to plan early – meeting the costs as they arise from income, from a financial stand point is by far and away the most expensive approach. Money invested when your child is a baby can provide tax-free sums simply by maximizing your annual ISA allowance, which is currently £11,520, and then earmarking this for future education, or even using your child junior ISA or child trust fund allowance of £3,720.

There are no longer any specific tax efficient school fees plans, therefore you will need to consider all other opportunities if you want to avoid meeting these costs through income, so setting up investments through lump sum contributions or regular payments are the most common approaches.

The options available include:

- Maximise use of your annual tax-free investment allowances.
- Save in your children's name to utilise their annual income and capital gains tax allowances.
- Consider topping up your pensions using your tax free cash or purchase annuities to provide a secure stream of income.
- Trust planning.
- Assign life policies and investment bonds to your children.
- Consider the use of an offset mortgage to allow you to release funds when required to meet school fees. Where any cash reserve is offset against an outstanding mortgage, this will maximise the tax efficiency of your savings and reduce your mortgage costs.
- Utilise the annual withdrawals facility available through onshore or offshore investments bonds.

If you already have children or are planning on starting a family soon then seek advice early to allow you to plan in a way that best suits you and your family.



Harrow School

Fairweather Visitors

Can responsible investment help crack down on tax avoidance?

By **Mark Pate**, Partner

Two corporate giants, Amazon and HSBC, recently held their AGMs where shareholders are raising the same concern: that aggressive tax avoidance strategies may be hurting the long-term value of the company.

Earlier this year Parliament's powerful spending watchdog formally castigated the internet giant Google for a "brazen" and "unconvincing" attempt to avoid paying its fair share of UK tax.

In a damming report, the Public Accounts Committee (PAC) called on HM Revenue & Customs to "fully investigate" the company, after concluding it had used "highly contrived" tax arrangements with the sole purpose of avoiding corporation tax on its multibillion-pound UK revenues.

Amazon were also criticised for paying only £2.4m in UK corporation tax, despite making £4.2 billion in sales. Meanwhile, research by MSCI has shown that HSBC has a higher proportion of its subsidiaries in tax havens than any other UK bank.

The reaction in the UK has generally been one of moral outrage. In March, a survey by Christian Aid found that two in three people think such tax avoidance is "morally wrong". Margaret Hodge, the chair of parliament's public accounts committee, commented last week that such behaviour on tax is "devious, calculated and, in my view, unethical".

With tax avoidance being painted in such ethical terms, the way the UK's responsible investment community has reacted to the issue tells us a lot about how the sector has evolved in recent years.

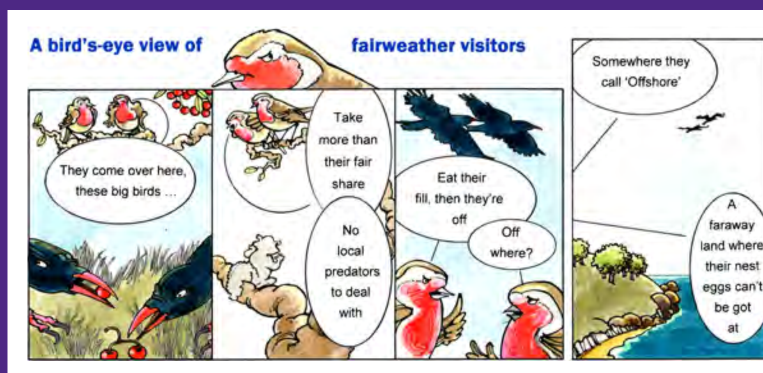
A decade ago, the loudest calls on such an issue would have been for ethical funds to screen these companies out. However, as far as we are aware, there are no funds offering an ethical screen to 'avoid tax avoiders'.

This is a very complicated issue because most individuals and companies seek to minimise their tax payments according to the rules in place. Whilst minimising your tax position within the rules is considered good corporate governance because it drives up returns to shareholders, it is difficult to impose an ethical screen asking companies to pay more tax as this doesn't make financial sense to its shareholders.

So instead of embargo, there is engagement. Responsible investors are choosing an active ownership approach, where they try to use their influence as shareholders to change the companies' behaviour.

Responsible investors, particularly in the institutional investment community, are exploring the business case for acting on the issue. They argue that the negative issues that arise from tax avoidance – like reputational damage, or fees, fines and retrospective charges from watchdogs – influence their risk management.

Such investors are bringing pressure to bear on specialist index providers such as FTSE4Good, to consider tax avoidance strategies as one of the criteria on which they judge the sustainability performance of companies.



That approach is another indicator of modern responsible investment – looking at the materiality of the issue, not the morality of it.

In truth, the jury is out on whether this modern responsible investment approach will actually change the behaviour of tax avoiding companies. Perhaps it is up to governments to work out a fair way of collecting tax. The rise of internet businesses means governments have not yet worked out how to change the tax system to catch these businesses which can be based anywhere in the world.

Responsible investment can help but those determined to take a stand on tax avoidance may also need to contact their MP as well as their financial adviser.

Illustration by Chris Radley.

Clean Energy

The opportunities: where and why

By **Mark Hoskin**, Partner

This is an extraordinary time to be discussing clean energy because for the first time in maybe 6 years clean energy funds are showing positive performance. Guinness Alternative Energy fund is up 63% over a year (to the 30th July), which together with the Premier Energy &Water Trust PLC (up 47%) are the two best performing funds on www.worldwiseinvestor.com which looks at clean energy, agriculture, water and timber funds as well as those with an ethical or sustainable stance.

For those choosing a clean energy fund, investors need to get a feel for what type of risk and return dynamic they are looking for. Clean energy funds are very different in composition and therefore the risk versus return profiles are very different. This difference in approach can be seen by comparing the sector weightings of the Guinness Alternative Energy fund with Pictet's Clean Energy fund. The former has a high exposure to wind and solar manufacturers, with 47% in wind and 25% in solar companies, while Pictet's Clean Energy fund has 60% exposure to energy efficiency companies, 30% to Natural Gas Infrastructure and only 10% to renewable energy companies and this to hydro, rather than solar and wind. So the stock composition of the two 'clean energy' funds could not be more different.

Pictet's clean energy fund is only up 22% in the last year (to the 30th July), while the Guinness Alternative Fund is up 45%. Luciano Diana, fund manager at the Pictet Clean Energy fund, sees this as a combination of a return in risk appetite in investment markets and the result of a bounce in solar and wind stocks from a very low base. Vestas, he points out is up 130% over the last year.

"You need to look at performance over three to five years," says Luciano, "many of these companies have been on the verge of bankruptcy and still face structural problems going forward." Q Cells and Suntech Power are two recent examples of solar companies which have gone bankrupt. "The name of the game in renewables manufacturing is driving down costs and few companies have the capacity at the current levels of technology to do this".

At Pictet, Luciano sees politicians unable to square the energy circle. They want security of supply, affordable electricity and to de-carbonise. But how? Something has to give and contradictory energy policies and uncertainty has been the result. He points to Spain as an example where once again they expect a reduction in the Feed-in Tariff on solar investments which have already been built, pushing many investments into the arms of the banks as covenants on debt financing are broken. The Pictet fund leans towards energy efficiency and Natural Gas which Luciano feels has more investment certainties. Conveniently (some might say) Pictet therefore does "not focus exclusively on CO2. CO2 is a problem but it is not the only problem". Natural Gas penetration is global and it is cleaner than oil or gas. Sulphur and Nitrogen emissions from Natural Gas are 50% lower and there is a particular fall off in particulates which the Chinese are so concerned about due to air quality. He also sees this type of energy source as crucial until storage technology has been developed for cleaner renewables. Renewable energy needs Natural Gas, "the two go hand in hand."

Equally, while renewables may ultimately provide the answer he does not see today's solar or wind technology as optimal. Solar panels at "15% efficiency cannot be the answer. This is not the end point. We are going through an energy transition which will take a great deal of time and does not happen overnight."

So while we may all understand the type of stocks Guinness Alternative Energy might invest in, such as Vestas. Pictet give examples of some of the stocks they like, such as Spirax Sarco in the UK which helps deliver energy efficiency into industrial processes; Telecity which provides data centres for companies which can provide significant energy savings; and Linde which provides among other things pure Hydrogen, Oxygen and Nitrogen which helps companies drive energy efficiencies into their industrial processes. The Pictet fund thus has a much lower risk profile than it has had in the past and indeed yields between 2% and 2.5%.

Clean Energy is undoubtedly an area which will continue to attract much attention in the future from society, companies and investors, but investors need to be aware that the clean energy funds are not from the same mould. Renewable energy companies, with close to 100% invested in the sector, have had such a bad time over the last 5 years that it might be that this is the start of the recovery. As an investor, funds like the Guinness Alternative Energy fund will provide genuine exposure to that theme. Pictet's approach is more circumspect and fits more comfortably into a mainstream global equity portfolio, but also may not provide the investment ride you were expecting.

Retiring Gracefully

Auto enrolment: the basics

By **Andrew Johnson**, Partner

The Government have introduced auto enrolment to ensure that people have enough money saved for their retirement.

There will be more pensioners in the future and those pensioners will live longer. This will put a massive strain on the State pension system. To alleviate this burden, the Pension Acts 2007 & 2008 make changes to the Basic State & Second State Pension and introduce new employer duties for pensions under auto enrolment. Here, we set out a brief summary of some of the key points.

Auto enrolment is a complex on-going process with multiple implications and it applies to all employees. Once you start to delve into the complexities, a number of actions will need to be considered. Auto Enrolment is part of a series of workplace pensions reforms aimed at encouraging employees to save more of their earnings for their retirement. It requires employers to contribute to pension schemes for their employees. All employers, regardless of size, will be affected by this legislation.

Starting from October 2012, up to 11 million workers will be enrolled into a workplace pension. Larger employers will go first (they have already started), with small and medium sized employers following over the next 6 years. Employers of different sizes have different 'staging dates' by which they must start automatically enrolling their employees. The current trigger dates are:

Employees	Staging Date
3,000-3,999	1 July 2013
1,250-2,999	Aug/September 2013
800-1,249	1 October 2013
500-799	1 November 2013
250-499	1 January 2014
50-249	1 April 2014 to 1 April 2015
Less than 50	1 April to 1 June 2017
New Company	Up to February 2018

Who will be enrolled into a workplace pension?

Employers will automatically enrol employees into a suitable workplace pension who:

- are not already in a qualifying scheme
- are aged 22 or over
- are under State Pension age
- earn more than £9,440 a year (this figure is reviewed annually) and work or usually work in the UK

Employees who have been automatically enrolled may opt out. If opting out occurs within one month from the day they officially become a member of the pension scheme, it will be as if they were never a member of the pension scheme and any payments made by them to the pension will be refunded.

Employees who do not 'qualify' for auto enrolment, may also opt into a pension and depending on their earnings and age, the employer will need to contribute. Based on current experience, employers are experiencing a high level of opt-in.

How much will pension contributions cost worker and employers?

The government has set a minimum contribution which is based on earnings (known as Qualifying Earnings) of more than £5,668 and £41,450 or less. The figures for 2013/2014 are expected to change each year. Minimum contribution levels start low and will increase gradually over a number of years. The table below sets out the minimum contribution limits:

Contribution rates required to meet the contribution requirement as a % of qualifying earnings

Date	Total required	Employer contribution
Oct 2012 - Sep 2017	2% +	1%
Oct 2017 - Sep 2018	5% +	2%
Oct 2018 onwards	8% +	3%

An agreement must be in place for the enrolled employee to make up at least the difference between the total and the employer amount. This can include tax relief on any employee contribution.

It is important to be aware that Qualifying earnings include salary, bonus, commissions overtime and statutory pay (sick & maternity). This may differ from what an employer includes in the definition of salary and wages within their employment contracts.

Additional Employer duties

Employers are required by law to provide the right information in writing to the right individual at the right time so that people know how automatic enrolment will affect them.

To ensure compliance one year before the staging date, The Pension Regulator will write to each business informing them of their obligations. At the staging date, if the business is not compliant, the Regulator will send enforcement notice giving a final deadline to comply. If the deadline is exceeded, they will issue a fixed fine of £400, which can escalate to a range of uncapped daily fines.

The key message is that if you have not already done so it is time to put your auto enrolment plan in place now, as you need a minimum of six months to plan and implement.

Caveat Emptor

What's the risk with Retail Bonds?

By **Mark Hoskin**, Partner

Retail Bonds are loans offered by trading companies direct to the public, in effect replacing the role the banks once took. They are under the radar of the Financial Conduct Authority ("FCA" previously known as the FSA) because they are deemed a 'bilateral loan'. This is a loan between two consenting parties, which is neither, listed, tradable or secured on a specific asset. They can be likened to loans between two companies or indeed friends.

Who has issued Retail Bonds in the past?
King of Shaves £5m (2009), Hotel Chocolat £3.7m (2010); John Lewis £50m (2011); Ecotricity £20m at 6% to 7.5% (2010 and 2011); Nuffield Health Bond £15m at 6% (June 2013); Energy Bond PLC £7.5m at 7.5% (July 2013).

What are the benefits?
An investor can gain access to returns far higher than deposit rates available at the bank and subject to the offer can provide an attractive risk versus return dynamic.

What to watch out for?
1). Financial Structure of the Company
By virtue of the fact that these are not secured on any specific assets, an investor must consider not just what other loans are in place today but also what other loans could be secured on assets in the future. They must also consider how strong the revenue of the company is for the future and whether existing loans can be refinanced.

2). Corporate Governance
An investor needs to consider who will be looking after their interests in the future? What representation do the lenders have in the event of a default, or in the management decisions up to this event? An unsecured loan ranks very poorly in the list of creditors who need to be repaid in the event of bankruptcy and so corporate governance is an important aspect in helping to mitigate this risk. This is particularly important when you appreciate that the average investment by a lender in a retail bond may be as low as £1,000 and so the individual investors are unlikely to want to spend money on legal fees in protecting their rights in the event of a corporate restructuring.

3). Liquidity
An investor needs to be prepared for a long period of investment, perhaps much longer than the initial stated length of the retail bond. A company will often rely on refinancing from other parties to buy out existing loans, which may not be available at the time.

Our View
Retail bonds as part of a portfolio can be an attractive alternative to listed liquid investments such as corporate bonds, property, shares, unit trusts or OEICs. There is no doubt that they can be very popular. Ecotricity were oversubscribed for both of their retail bond issues, while the Nuffield Health Bond recently raised £18.6m having set a target of £15m. 1,300 individuals invested in the Nuffield Health Bond, with the average investment amount being approximately £14,000 per person.

Investors though need to consider the risks carefully. While all retail bonds have the same legal position, the risk and return profile of these bonds can vary wildly depending on the actual financial position and structure of the individual offer. At the same return, some offers will have good security and future protection, while others may be taking on much higher risk than an investor may have realised, or should expect for the return on offer. Investors should also note that retail bonds are not covered by the Financial Services Compensation scheme (FSCS). Retails Bonds are therefore truly a case of buyer beware, or 'Caveat Emptor'!

Content of the articles featured in this publication is for your general information and use only and is not intended to address your particular requirements. They should not be relied upon in their entirety and shall not be deemed to be, or constitute, advice. Although endeavours have been made to provide accurate and timely information, there can be no guarantee that such information is accurate as of the date it is received or that it will continue to be accurate in the future. No individual or company should act upon such information without receiving appropriate professional advice after a thorough examination of their particular situation. We cannot accept responsibility for any loss as a result of acts or omissions taken in respect of any articles. Thresholds, percentage rates and tax legislation may change in subsequent finance acts.

For more information, please contact us:

+ 44 (0) 20 7812 1460
hpreview@holden-partners.co.uk

www.holden-partners.co.uk

Holden & Partners
The Piano Works
117 Farringdon Road
London EC1R 3BX
+44 (0) 20 7812 1460