

INVESTMENT

AN INVESTOR AND COMPANY GUIDE TO

THE ENTERPRISE INVESTMENT SCHEME (EIS)



Interface 

Independent Financial Advisers - Financial Life Planners

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Introduction

The Enterprise Investment Scheme (EIS) offers one of the best tax schemes currently available to investors.

It also provides a valuable way for companies, particularly smaller companies, to raise money.

It is a rare example of a generous and relatively simple tax incentive in an otherwise complex tax environment.

The government has enhanced the benefits and the value of the EIS over the past few years as part of a broader approach to encourage investors to back smaller unquoted companies.

In return they offer investors a series of tax incentives. The combined value of these incentives can be exceptional in the right circumstances.

Crucially the EIS is enshrined by legislation which means, unlike many other tax schemes, it is robust and protected from future uncertainties or whether the tax benefits will 'stick'.

Our guide aims to help you understand the basics of how the scheme works, how the Seed Enterprise Investment Scheme (SEIS) works, how investors and business owners can benefit from them and what you need to do to take this further in either case.

Please note this guide is issued to provide an overview of the EIS and SEIS for investors and for companies. It is a general description of how the scheme works and the benefits to investors/ companies. It is not a technical guide and will not cover every technical point. It should be noted that references to conditions and reliefs are based on existing law and our understanding of current HM Revenue and Customs practices (as of tax year 2019/2020) and are therefore subject to change. Readers should seek further advice or help before proceeding to invest or raise funds under the EIS.

The EIS for investors looking to invest

If you are looking to invest into a company, then you may be able to do so under the Enterprise Investment Scheme; you can take a shareholding in a qualifying company and obtain valuable tax benefits. Or you may like to invest into a portfolio of qualifying companies through an EIS discretionary portfolio, where your investment is spread across several different EIS qualifying companies.

The EIS offers investors more than one possible tax angle; there are advantages for investors, in many ways, of investing a sum into an EIS qualifying investment. Essentially there are five main tax benefits:

- Income Tax relief
- Capital Gains Tax Deferral Relief
- Capital Gains Tax Exemption
- Loss Relief
- Inheritance Tax Exemption

There are many qualifying criteria around EIS qualifying investments (see section five), if you invest into a company or scheme that qualifies, here in brief are the main features of these various tax advantageous elements:

Income tax relief

An individual can reduce their income tax liability by an amount equal to 30% of the amount invested; the shares must be held for a minimum period of 3 years.

The relief is given by way of a reduction of tax liability, providing there is enough tax liability against which to set it.

There is no minimum investment amount; the maximum per investor is £1,000,000 per tax year.

There is an additional £1,000,000 per year limit for investments in knowledge-intensive companies

Individuals who have not used their EIS entitlement in the previous tax year can treat all or part of the cost of the investments as subscribed in that year, up to the maximum annual investment limit for the applicable year.

Capital Gains Tax (CGT) Deferral Relief

Tax on gains realised on a different asset can be deferred. The EIS shares you subscribe for must be issued to you in the period beginning 12 months before, and ending 36 months after, the date of the disposal of the asset against which you wish to claim CGT relief. There is no minimum period for which the EIS shares must be held.

The deferred capital gain is brought back into charge whenever the shares are disposed of (or are deemed to have been disposed of under EIS legislation).

This relief is not limited to investments of £1,000,000 per annum.

Capital Gains Tax (CGT) Exemption

No Capital Gains Tax is payable on any sale of the EIS shares after three years. This is, however, provided the EIS initial income tax relief was given and not withdrawn on those shares.

Loss Relief

If EIS shares are sold in the future at a loss, the loss can be offset against the investor's income in the year of disposal or the previous year. (The loss is calculated less any income tax relief previously given). Alternatively, the losses can be offset against Capital Gains Tax.

Inheritance Tax Exemption

EIS qualifying investments are exempt from Inheritance Tax after two years of holding the investment.

The EIS for companies looking to raise funds

There are two 'sides' to the EIS: on the one side private investors seeking to invest into smaller companies, making profits and getting tax benefits. On the other side are companies that use the EIS to raise funds.

Companies can raise funds through issuing new shares in their company; either through the Seed EIS (see next section) or through the EIS. It is possible for a start-up or new company to raise money in its formative stages through the SEIS and then later down the line through the EIS.

A company looking to raise funds via an EIS need to consider:

The tax benefits of EIS are only available when new shares are bought. If the existing shares of an EIS-eligible company are bought on the secondary market, then none of the tax breaks are available via EIS.

In addition, the company must:

- Have gross assets of less than £15 million before the share issue (with a cap of £16 million post investment)
- Have fewer than 250 full time employees
- Be trading in the UK
- Be carrying on a "qualifying trade"

The SEIS

The Seed Enterprise Investment Scheme is the baby brother of the main EIS. It is a variation on the same theme, except it is aimed at newer and smaller companies.

For Investors:

The biggest difference with the SEIS for investors to consider is that the income tax relief is 50% not 30%. This extra amount is a trade off against the greater risk of investing into a newer business which may not have the same survival prospect rate of a larger company.

Income Tax relief is available to individuals who subscribe for qualifying shares in a company which meets the SEIS requirements, and who have UK tax liability against which to set the relief.

Investors don't need to be UK resident.

The maximum annual investment for investors to obtain relief, is £100,000.

A claim to relief can be made up to 5 years after the 31 January following the tax year in which the investment was made.

All other tax benefits as are per the EIS.

For Companies:

For its investors to be able to claim and keep the SEIS tax reliefs, the company must meet several requirements.

Some of these apply only at the time the relevant shares are issued. Others must be met continuously, either for the whole of the period from date of incorporation to the third anniversary of the date of issue of the shares, or in some cases, from date of issue of the shares to the third anniversary of their issue.

If the company ceases to meet one or more of those conditions, investors may have their tax relief withdrawn.

Finally, there are requirements as to how the company must use the monies it has raised via the issue of relevant shares.



Main points for companies to consider:

The company must be unquoted at the time of issue of the shares.

It must have fewer than 25 employees.

It must have no more than £200,000 in gross assets.

The company must not have had any investment from a Venture Capital Trust or issued any shares in respect of which it has submitted an Enterprise Investment Scheme (EIS) compliance statement.

The company may not receive more than £150,000 in total under the scheme.

Any trade being carried on by the company at the date of issue of the relevant shares, must be less than 2 years old at that date. That condition applies whether the trade was first begun by the company, or whether it was first begun by another person who then transferred it to the company. (The company need not have started trading when it issues the shares).

The company must not have carried on any other trade before it started to carry on the new trade.

The company must not be controlled by another company or another company and any person connected with it, and there must be no arrangements in place for it to be controlled by another company.

The company must be UK resident, or have a permanent establishment in the UK.

If a single company, it must exist wholly for the purpose of carrying on a qualifying trade.

Within 3 years of the date of the relevant share issue, all the monies raised by that issue must be spent for the purposes of a qualifying business activity.

A qualifying trade is one which is conducted on a commercial basis with a view to the realisation of profit.

There is a significant list of excluded qualifying trades (dealing in property for example), in these cases SEIS is not available.

In both cases where a company is looking to raise funds under the SEIS or the EIS it is imperative that professional advice is sought and proper clearance checks have been undertaken before any shares are issued on this basis.

Some common considerations around the EIS

The SEIS/EIS offers great attractions to both companies and to investors, here are some of the common considerations applying for both parties:

For Investors:

- Don't let the tail wag the dog! There are tremendous tax benefits involved but these would be outweighed if a bad investment is made. Investing into unquoted companies is risky and if the investment goes wrong the advantages of the tax breaks will be mitigated and more. In this respect risk cannot be taken out of this type of investment - but take care that the risks are understood and weighed up.
- It is possible to invest into an EIS discretionary portfolio, which may allow for the investment sum to be spread around several companies. This diversification provides an element of risk reduction.
- EIS reliefs are particularly valuable for those who have a potential Inheritance Tax (IHT) Liability because the sum invested can be used to reduce an Estate Value and the qualifying period for this is 2 years, whereas many other IHT reduction schemes can take years to lock in and/or involve passing an asset outside of an Estate.
- Advice from a qualified source is crucial before any steps are made to invest via the EIS.

For Companies:

- Becoming EIS (or SEIS) qualifying makes the company more attractive for investors. For any company seeking to raise funds it is worth exploring the EIS route to see if the qualifying conditions can be met.
- Any fund-raising requirement should be assessed based on the company's major business needs; it may be that issuing shares is less attractive than raising funds as a loan; there may be other, possibly better, ways of raising funds (e.g. through Peer to Peer loans or via a grant). The issuance of shares via the EIS should be measured against alternatives.
- Advice from a qualified source is crucial before any steps are taken to raise funds via the EIS.

Taking this further

At Interface Financial Planning we can help you whether you are an investor looking to invest and benefit from the EIS tax reliefs or a company looking to raise money under the EIS.

As stressed throughout this guide, advice and guidance is crucial.

These are areas with great potential, but they involve tight rules and qualifying criteria which you need to make sure are being met – and will continue to be met.

The continuing qualification is important because reliefs can be withdrawn if the various criterion are not met for certain periods of time.

If you want to explore the EIS or SEIS further, then we are here to help you; please see our contact details below. Please get in touch with us for further help.

THE COMBINED VALUE
OF TAX INCENTIVES FOR
INVESTORS TO BACK
UNQUOTED COMPANIES
CAN BE EXCEPTIONAL IN
THE RIGHT CIRCUMSTANCES...

ALWAYS SEEK INDEPENDENT PROFESSIONAL ADVICE FIRST

History, structure, and expertise

Interface Financial Planning started providing independent financial advice in 1992. From the beginning it had the aim of providing professional advice and quality service to people with modest income and wealth.

Its key value was putting people before profit, and contribution before reward. This mission statement has been our torch to light the path ahead and has been the reason that we have endured for over 24 years.

Alan has lead the company with his personal values of: Integrity, Compassion, Respect, & Loyalty, and he is proud that over the years he has worked with clients who share similar values. Like him they want to help others and make the world a little better.

Client care and service is important and he is proud that his first two clients from January 1990 remain his clients today.

We believe that every client should have access to highly qualified advice and expertise.

Technology is used to the full to maximise efficiency and engage expertise from throughout the UK. The business has been paperless for 10 years and for over 5 years has been 'cloud' based. This structure reduces costs and allows support staff to operate anywhere - from Colchester to Honiton to Leicester and elsewhere.

Clients are encouraged to access their online account where they can exchange messages and documents securely. They can view their investments and reports, and they have immediate access to their paper file. Clients love the transparency and openness of being able to view and print paperwork going back for years and many clients use it as a source of reference.



ALAN MORAN
Owner, Director
Interface Financial Planning

Alan Moran is one of the most highly qualified advisers in the UK. He became a Certified Financial Planner in 1995 and he was one of the first Chartered Financial Planners in 2005.

He is a Chartered FCSI, a holder of the IMC certificate and member of CFA UK. His expertise has been called upon by The CII, The IFP, The Kinder Institute, and others, where he has trained and examined other financial advisers.

Alan Moran B.Sc. M.Soc.Sc. Cert.Ed. FPFS FSWW IMC CFP^{CM} RLP[®]

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Compliance

Readers should not rely on, or take any action or steps, based on anything written in this guide without first taking appropriate advice. Interface Financial Planning Ltd cannot be held responsible for any decisions based on the wording in this guide where such advice has not been sought or taken.

The information contained in this guide is based on legislation as of the date of preparation and this may be subject to change.

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www.interfacefinancialplanning.co.uk