Guidance note

Burges Salmon

Enterprise Investment Scheme

This guidance note provides an overview of the benefits and qualifying requirements of the Enterprise Investment Scheme.

What is the Enterprise Investment Scheme?

The Enterprise Investment Scheme (EIS) has been in existence since 1994. It is intended to promote investment in small and medium sized companies with a higher risk profile.

The EIS has evolved continually since its inception. Recent years have seen a significant increase in the thresholds to qualify for EIS.

Why should I be interested in EIS?

The tax reliefs available under the scheme are very generous.

- **Income tax relief** – income tax relief is available at 30% of the amount of the qualifying EIS investment provided the shares are held for three years.
- **CGT deferral** – capital gains realised on the disposal of other assets can be deferred by reinvesting the proceeds of the disposal in qualifying EIS investments.
- **CGT exemption** – gains on qualifying EIS investments are exempt from capital gains tax providing the shares are held for three years.
- **IHT** – qualifying EIS investments may also qualify for 100% business property relief once held for two years.
- **Loss relief** – losses on qualifying EIS investments (less any EIS income tax relief already received) can be set-off against income to reduce income tax, or gains to reduce capital gains tax.

Does the investment qualify for EIS relief?

There are a number of requirements relating to the company, the investor and the shares which must be met. **For a summary of certain of these requirements please see overleaf.**

What next

Take advice to ensure that the investment will qualify for EIS relief. The rules surrounding eligibility for EIS relief are complex and require tailored advice. There are several ways in which an investment can fail to meet the criteria or relief can be withdrawn following investment.

Burges Salmon has expertise in corporate, tax and funds EIS advice. We are able to advise across the EIS approval process, as well as on more specific investor or issuing company issues and concerns.

Further information

If you would like any further information on EIS please speak to your usual contact at Burges Salmon or:

Who to contact

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Key criteria

	Qualifying requirement
Company	• Can raise up to £5 million per annum or, for shares issued on or after April 2018, £10 million per annum if the company is classified as a Knowledge-Intensive Company ("**KIC**") under the EIS scheme (capped at a lifetime limit of £12 million generally or £20 million for KICs). • Must be an unquoted company (AIM and PLUS quoted companies may qualify but not PLUS-listed companies). • Shares must be issued within seven years of the company's relevant first commercial sale. For KICs, the period is 10 years from the relevant first commercial sale or from the date when annual turnover exceeds £200,000. • Must be a genuine entrepreneurial company intending to grow and develop with a significant risk of loss of capital. • Must have a permanent establishment in the UK. As long as the issuing company has a permanent establishment in the UK, the funding can be used for a qualifying trade that is not in the UK. • Must have gross assets of not more than £15 million pre-investment and £16 million immediately post-investment. • Must have 249 or fewer full time employees (or part time equivalent) pre-investment (499 or fewer for KICs). • Must exist wholly for the purpose of carrying on a **qualifying trade**: activities cannot be substantially made up of **'excluded' activities** (see below). HMRC apply a 20% limit to the amount of activity of the issuing company that may be non-qualifying or an exempt activity, which applies for three years from the date of share issue. • Funds must be employed in the qualifying business activity within two years. For shares issued on or after 18 November 2015, acquiring an existing company or trade will not satisfy this requirement. • The issuing company must not be a 51% or more subsidiary of another company or under the control of another company for the period of three years from the date of share issue. The Company may have its own subsidiaries provided it owns more than 50% in each of them (this rises to 90% for property management subsidiaries). If funds raised are to be used by the subsidiary, the subsidiary must be at least 90% owned by the issuing company throughout the three-year period from the share issue.
Shares	• Must be new and fully paid up in cash at the time of issue. They must be non-redeemable ordinary shares without preferential rights (other than certain dividend rights) or anti-dilution protection. • Must be held by the investor for at least three years, with no pre-arranged exit for the investor. • Must be issued to raise money for a **qualifying business activity**, for commercial reasons and not for the purposes of tax avoidance. • Shares with a right to conversion into shares of another class in the company can qualify for relief.
Investor	• The investor (and any "associates") cannot hold (or be entitled to hold) more than 30% of the issued share capital or voting rights or otherwise control the company or any subsidiary. • Must not be "connected" with the company during a period of two years before the investment and three years afterwards i.e.: the investor and their associates must not: – subscribe for shares under reciprocal arrangements. – be an employee of the issuing company, any subsidiary or any partner of them. – be a paid director of the issuing company, any subsidiary or any partner of them before the investment (subject to certain exceptions). • Can invest up to £1 million in EIS qualifying investments per annum. From 6 April 2018, the limit is £2 million, provided anything above £1 million is invested in KICs. • For shares issued on or after 18 November 2015, investors that already hold shares in the company (or subsidiary) will only qualify if those shares were risk finance shares (i.e. shares for which an EIS/SEIS compliance certificate was issued or founder shares).
Excluded activities	• There are a number of excluded activities: – all energy generating activities and creating fuel. – dealing in land, commodities, futures, shares, securities or other financial instruments. – dealing in goods otherwise than in the course of an ordinary trade of wholesale or retail distribution. – banking, insurance, money-lending, debt-factoring, hire-purchase financing or other financial activities. – leasing. – receiving royalties or licence fees (this exclusion is waived in certain circumstances). – providing legal or accountancy services. – property development. – farming or market gardening; holding/managing or occupying woodland, forestry activities or timber production. – shipbuilding; producing coal or steel. – operating or managing hotels or nursing/residential homes. – providing services or facilities to a connected business which carries on an excluded activity.

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