Briefing

Tax

BURGES SALMON

Could you use EIS to attract investment?

What is the Enterprise Investment Scheme?

The Enterprise Investment Scheme (EIS) is intended to encourage investment into small and medium sized companies with a higher risk profile by offering significant tax relief to investors.

The EIS has evolved continually since its inception in 1994. Recent years have seen a significant increase in the applicable thresholds, creating a greater incentive for investors to make EIS eligible investments.

Why should I be interested in EIS?

Many small and medium companies in the FinTech sector will, in principle, qualify to receive EIS investments. The potentially generous tax reliefs available make investments eligible for EIS particularly attractive to investors.

Reliefs available include:

Income tax relief – income tax relief is available for the investor to the value of 30% of the amount of the qualifying EIS investment (subject to a cap).

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 after three years.

IHT – qualifying EIS investments generally 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.

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 some of the main requirements please see over the page.

What next?

Take advice to ensure that an investment will qualify for EIS relief. The rules surrounding eligibility for EIS relief are too complex to cover fully here and change frequently. There are several ways in which an investment can fail to meet the criteria. In some cases, a seemingly insignificant deviation from the conditions of EIS can lead to the full amount of relief being denied or withdrawn.

Key criteria

	Qualifying requirement
Company	■ Cap of £5 million per annum investment under EIS scheme and lifetime limit of £12 million generally or £20 million for knowledge-intensive companies (KICs). ■ Must be an unquoted company (AIM and PLUS quoted companies may qualify). ■ As a general rule, the EIS company cannot be more than seven years old or, for KICs, 10 years old (from date of first commercial sale). ■ EIS funds must be used to promote the growth and development of the company. ■ Must have a permanent establishment in the UK. ■ Must not be a subsidiary of another company. It may have its own subsidiaries provided it owns more than 50% in each of them (90% of any subsidiary which is involved in property management). Further conditions apply if EIS monies are to be used in the subsidiary. ■ Must have gross assets of not more than £15 million pre-investment and not more than £16 million immediately post-investment. ■ Must have 249 or fewer full time employees (or part time equivalent) pre-investment or, for KICs, 499 or fewer employees. ■ Must exist wholly for the purpose of carrying on a qualifying trade, i.e. activities cannot be substantially made up of 'excluded' activities (see below). ■ Must remain qualifying throughout a three year period. ■ Funds must be employed in the qualifying trade within two years.

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	Qualifying requirement
Shares	■ Must be "full risk" non-redeemable ordinary shares without preferential rights (other than certain dividend rights) or anti-dilution protection. ■ Must be new shares, fully paid up in cash at completion. ■ Must be held by the investor for at least three years, with no pre-arranged exit for the investor.
Investor	■ Must not be "connected" with the company during a period of two years before the investment and three years afterwards ie: the investor and his associates must not: ■ own or be entitled to acquire 30% or more of the company; ■ be able to control the company; ■ be an employee; ■ be a paid director before the investment (subject to certain exceptions). ■ Must be independent from the company and hold no other shares in the company at time of first investment (with exceptions for previous SEIS, EIS or VCT investments or "founder shares"). ■ Can invest up to £1 million in EIS qualifying investments per annum.
Excluded activities	Companies which carry out a substantial level of excluded activities do not qualify for EIS investment. If the company receiving the investment is the parent company of a group, the activities of the group as a whole are considered when determining whether the level of excluded activities is substantial. Certain financial services, including banking, insurance, money-lending, debt-factoring and hire-purchase finance are excluded. However, in most cases, developing and/or selling technology which has applications in the financial sector will not be excluded.

Contact:

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

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