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Briefing document

EIS and Seed EIS

Introduction
The Enterprise Investment Scheme (EIS) and Seed EIS (SEIS) are both intended to help small, higher-risk unquoted trading companies raise capital. The schemes do this by providing a range of tax reliefs for individuals who subscribe for shares and who meet various conditions. The conditions must continue to be met over a prescribed period or any tax relief that is given may be clawed back.

SEIS offers more generous tax reliefs than EIS, but is available on much smaller companies that have a shorter maximum trading history compared to EIS eligible companies. An overview of both schemes is set out below.

Tax reliefs and exemptions

EIS
The following forms of tax relief and exemption are available on the making of an EIS investment:

- Income tax relief of 30% on the amount invested into an EIS company. Income tax relief can be claimed on a maximum investment of £1million per annum into most trading companies, though it is possible to claim relief on up to £2million of investment per annum if the additional £1million is invested into 'knowledge-intensive' companies. Relief can be carried back to the previous tax year, subject to the aforementioned maximum amounts on which relief can be claimed.
- Capital Gains Tax (CGT) exemption on disposal of EIS shares on which income tax relief has been claimed.
- CGT on gains made on other assets can be deferred. Deferred gains come back into charge once the EIS investment is sold, or if the relevant conditions for EIS to apply otherwise cease to be met. CGT deferral relief must be claimed.

SEIS
The following forms of tax relief and exemptions are available on the making of a SEIS investment:

- Income tax relief of 50% of the amount invested can be claimed, up to a maximum investment of £100,000 per annum. As with EIS, SEIS relief can be carried back to the previous tax year, subject to the £100,000 maximum.
- CGT exemption on disposal of SEIS shares on which income tax relief has been claimed.
- In contrast to EIS, where gains have been made on disposal of other assets, 50% of the gains may be made exempt from CGT, rather than merely deferred. These gains are not subject to CGT at a later date, provided the conditions for SEIS to apply continue to be met for the requisite period. If these conditions are not so met, the gain that would otherwise be exempt will be charged to CGT. This relief must be claimed.

Withdrawal of reliefs and exemptions
The EIS and SEIS reliefs and exemptions outlined above may be wholly or partially withdrawn if various conditions are not met for the requisite period. This, broadly, means for three years following the making of an investment, though the time period may differ if the company has not commenced trading at the date the investment is made. Both the investor and the company must meet conditions, which means that tax reliefs and exemptions may be lost through no fault of the investor.

International aspects

Income tax relief for both EIS and SEIS is available to both UK and non-UK resident individuals. The CGT exemption is also available to both UK residents and to non-UK residents, though is typically only of relevance to UK residents, since non-UK residents are normally not within the scope of CGT on disposal of shares.

Non-UK residents who make a qualifying SEIS investment are eligible for the 50% exemption on gains realised on disposal of other assets. This may be relevant if a non-UK resident has realised a gain which is subject to CGT, such as a gain on disposal of UK land.

EIS CGT deferral relief is only available to UK residents, and a deferred gain may be subject to CGT if an individual who has claimed EIS deferral relief ceases UK residence.

Inheritance tax

EIS and SEIS shares may also be eligible for relief from inheritance tax after they have been owned for at least two years. This is not part of the EIS or SEIS: relief may be available due to overlap with the conditions that must be met for business property relief from inheritance tax to be available.

Conditions to be met

A number of conditions must be met for both EIS and SEIS. There is a high degree of overlap between the conditions that must be met for the two schemes, though there are some points of difference. Some of the key points to note are as follows:

- With the exception of EIS CGT deferral relief and inheritance tax business property relief, the reliefs outlined above are only available if the investor is not 'connected' to the company. Among other factors, individuals are connected if they have an interest of more than 30% in a company. Interests of 'associates', such as some relatives, are taken into account when determining an individual's percentage interest in a company. The investor cannot be an employee of the company, and can only be a director if certain conditions are met.
- EIS and SEIS are only available on investments into trading companies. Certain trades are non-qualifying, and EIS and SEIS are unavailable on investments into companies that undertake these activities to a substantial extent. This includes, but is not limited to, dealing in land and property development. In addition, the company must have objectives to grow and develop its trade in the long-term.
- For both EIS and SEIS, relief is only available if, by making the investment, the investor puts his or her capital at risk and so could make an overall loss on the investment, taking into account the net investment return, loss of capital and any tax relief obtained.
- The reliefs are only available on subscriptions for new ordinary shares. Broadly, the ordinary shares must not contain any conditions that seek to limit the investors' risk. The company must be unquoted. Companies listed on the Alternative Investment Market (AIM) are considered to be unquoted for these purposes.
- For SEIS purposes, the company must have gross assets of at most £200,000 when the SEIS investment is made. EIS reliefs are available into much larger companies, with up to £15millon of gross assets pre-investment and £16million afterwards.
- In order to be eligible for SEIS companies can only have been trading for a maximum of two years before an SEIS investment is made. EIS is usually available on investments into companies that have been trading for up to seven years, though relief may be available for later investments into older companies some cases.
- In order to qualify as 'knowledge-intensive', such that investors may be eligible for the higher annual EIS investment limit, the EIS company must meet certain conditions which, broadly, relate to its research and development expenditure, creation of intellectual property and/or the number of skilled employees.

Commercial issues

Whilst they are attractive, the tax benefits of EIS and SEIS investments are only one of a number of aspects of which a potential investor should be aware.

EIS and SEIS investments carry a significant investment risk so it is essential that appropriate investment advice is taken from an FCA authorised advisor.

Investors also need to be aware that it can be difficult to sell the shares, as the reliefs outlined above are only available on subscriptions for new shares. This means that there are unlikely to be many potential purchasers of second-hand EIS and SEIS shares. Investments of this nature should therefore only be considered as a part of an overall investment strategy and subject to obtaining suitable advice.

Claims
Income tax reliefs on investment and CGT deferral/exemption of gains realised on disposal of other assets must be claimed. Claims typically need to be made within five years and ten months of the end of a tax year in which an investment is made. Claims can only be made once the relevant EIS / SEIS 3 certificate has been issued by the company.

If relief is to be carried back and claimed in respect of the tax year before the investment is made, the deadline for making the claim is four years and ten months from the tax year in which the investment is made.

Find out more…
This note reflects the law in force as at 9 April 2020. This note sets out available reliefs and exemptions, and conditions that must be met, for shares issued from the aforementioned date. Different provisions may be relevant to shares issued beforehand. Please be aware that this note does not cover all aspects of this subject.

To find out more about any aspect of the above, please discuss with your usual Deloitte contact. If you do not have a usual contact, please contact Michelle Robinson (michellerobinson@deloitte.co.uk).

For further information visit our website at www.deloitte.co.uk.