Brieifing Note - EIS

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Letting the taxman attract investment in your business

The Enterprise Investment Scheme (EIS) is a Government incentive designed to encourage individuals to invest in Ordinary shares of unquoted trading companies. For the companies that qualify, it enables them to raise vital funds by issuing Ordinary shares to individual investors previously unconnected with them.

For the individual investor there are a number of attractive tax savings available. The Scheme's rules are complex and this guide is meant as a basic overview. If you feel the EIS could benefit your business do seek out detailed advice from your tax specialist or call us.

What can the funds be used for?

The funds raised from the EIS investment must be used on a commercial basis, for the purpose of a qualifying trade or for research and development expected to result in such a trade. A large number of business activities do qualify, however there are a list of about 15 or so trades that do not, so speak to us or talk to your tax adviser to double-check yours. The trade can be carried out anywhere in the world provided the business has a 'permanent establishment' in the UK.

Investment limits

An individual can invest up to a total of £1m in an EIS-qualifying company this current tax year (2014/15) in order to claim Income Tax Relief.

A husband and wife can each invest up to £1m each year (this has risen from £500k) provided they meet all the other qualifying conditions. Tax relief of up to £500,000 can also be claimed in the tax year 2013/14. The maximum that a company can raise under EIS is £5m in any one 12 month period.

What tax benefits are open to investors?

Six potential tax reliefs are available for investment in an EIS-qualifying company:

1. Income tax relief - 30% of investment
2. Capital gains tax relief on sale - up to 28%
3. Loss relief - up to 50%
4. Capital gains tax deferral relief - up to 28%
5. Inheritance tax business property relief - 40%
6. Business investment relief for non-domiciled individuals - up to 50%

Both the company and the investor must satisfy the relevant EIS conditions for 3 years from the time the shares in the company are issued, or from the time the company commences trading – whichever is later. The investor must **not** sell the shares or receive value from the company during that period.

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Rules for investors - an overview

- The investment must be in Ordinary shares and must be made in cash for new shares
- An investor (and associates) cannot hold more than 30% of the shares
- They must invest for a minimum of 3 years
- They must have sufficient UK income tax liability to benefit from the EIS
- They must not be a director/employee of the company before a share issue

Rules for companies - an overview

- To qualify for EIS the company cannot be a subsidiary or controlled by another company. It also cannot be listed
- It has to carry on some activity in the UK but does not need to be UK incorporated or have its main business in the UK
- There is a limit on the company's number of employees (250) and gross assets (£15m before share issue and £16m after)
- The investment raised from the EIS must be used in the business within 2 years

For small start-up companies there is a new Seed Enterprise Investment Scheme (SEIS) to help them secure investment which qualifies for 50% income tax relief. The maximum raise for a company is £150,000 and a single investor can invest up to £100,00 in a tax year.

A real-life example

We recently helped a company who manufactured medical products. For a number of reasons traditional funding was not an option for them and they were looking for private equity. We met with the company and a potential investor to discuss the options for investment under EIS.

As the company fitted the EIS criteria, the investment resulted in a number of tax advantages for the investor. Initially they were able to offset 30% of the investment cost against their income tax liability for the year.

Specific advice should be obtained before taking action, or refraining from taking action, on any of the subjects covered above.

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