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Enterprise Investment Scheme (EIS) & Seed Enterprise Investment Scheme (SEIS) tax breaks

EIS

EIS offers a number of tax breaks to investors who buy shares in small, private companies:

- You get **income tax relief** of 30 per cent. So if you invest £10,000 in a company that is eligible for EIS, you can knock £3,000 off your income tax bill in the year that you invest.
- You'll pay **no capital gains tax** on any profits you make from an EIS investment. So if you invest £10,000 and five years later sell your shares for £20,000, you'll get the full benefit of the £10,000 profit, saving you at least £1,800.
- If you make a loss on your investment, you can **offset that loss** against income tax. So let's say you lose your entire £10,000 investment. Because of income tax relief, your actual loss is only £7,000 (£10,000-£3,000). So you can, if you choose, reduce your taxable income for the year in which you disposed of the shares by £7,000, resulting in a saving of £2,800 (40 per cent of £7,000) for a higher-rate taxpayer. If you want to offset your loss against other capital gains in the normal way, you can do this instead.
- There's **no inheritance tax** to pay on shares bought through EIS.
- If you have capital gains that arose 1 year before you invested in the EIS company or 3 years after you invested, you can defer the capital gain. Thus if you had chargeable gains of say £40,000 and invested £25,000 into an EIS fund, you could defer £25K of the gains and be taxed on gains of just £15K. The deferred gain comes back though when you later sell the EIS investment.

To be eligible for these reliefs, you generally have to hold the shares for at least three years before selling them.

There's a few more catches. You still have to pay tax on any dividends – but most small private companies won't pay dividends anyway. There are certain restrictions as to what kind of business you can invest in (it can't be a bank, a farm or a nursing home, for example). And you can't be connected to the company or have a stake of more than 30 per cent of it.

You can invest a maximum of £1 million each year through EIS.

SEIS

SEIS is very similar to EIS but designed for investing in even smaller companies, and providing even more generous tax breaks.

While the maximum workforce and gross assets allowable under EIS are 250 staff and £15 million respectively, SEIS has lower limits of 50 staff and £200,000 gross assets. Businesses must also be less than two years old (there are no age restrictions under EIS).

The tax breaks are as follows:

- **Income tax relief** is 50 per cent, not 30 per cent. So you get £5,000 off your income tax bill for investing £10,000 under SEIS.
- As with EIS, there's **no capital gains tax** to pay on profits, **no inheritance tax**, and you can claim **loss relief** in the same way. See above for details.
- There is also **capital gains reinvestment relief** and this is more generous than for EIS. If you have chargeable gains on other investments, you get a full reduction of the gain equal to 50% of the amount invested into SEIS.

The maximum you can invest through SEIS in any tax year is £100,000.

How to access EIS and SEIS
If you invest through a business angel network or an equity crowdfunding website, the network or website should help you with the paperwork around getting your EIS or SEIS benefits.

You can also invest in a company you know, provided you are not considered to be connected to it by HMRC. Connection means being a partner, employee, director, or having a share of 30 per cent or more. If you do invest in a company you have come across privately, make sure you buy the shares *after* the company has been set up, otherwise EIS and SEIS won't apply.

You should always check that the company you're investing in is definitely eligible for EIS or SEIS – and make sure you're happy with it as an investment.

Never invest just for the tax breaks.

EIS funds
Although EIS was originally designed to encourage direct investments in companies by individuals, there are a number of EIS funds where professional managers will choose companies to invest in.

Sometimes, the EIS fund manager makes investments on your behalf, with your name ending up on the shares. In this case, you only get the tax reliefs as and when your money is invested in qualifying companies. Other EIS funds that have been specially approved by HMRC can give you the chance to claim all your tax relief when the fund closes for investment.

EIS funds can help you spread risk across a larger number of companies, and effectively outsource your investment decisions to a manager who should have the time and skills to assess companies properly. However, this doesn't change the fact that an EIS fund is still a very risky investment, with a high chance of losing large chunks of your money. Use with caution.

Practical Points

Suppose you invest £25K in EIS shares. You will get 30% x £25K = £7,500 off your total tax bill (to the extent that your total tax liability is at least this amount).

The date shares are issued to you (which will be after you've actually paid for the shares) will determine which tax year income tax relief is claimed for. Assuming the date the shares are issued to you is on or before 5 April 2018, you can claim income tax relief in 2017/18 or in the previous tax year 2016/17.

Similarly, if the date of issue of the shares (as will be shown on the EIS3 certificate you eventually receive) is dated on or after 6 April 2018, you can claim income tax relief in 2018/19 or 2017/18.

A practical problem is that it can take several months before you actually receive the EIS3 certificate and you are not allowed to make/submit any claim before this date of receipt of the certificate. This can often result in us as your accountants having to delay submitting your tax return until you get the EIS3 certificate. Moreover, if we decide to or have to (due to the impending filing deadline) submit the tax return before receipt of the certificate, you can still claim, but the claim has to be by using pages 3 & 4 of the certificate and submitting this by **paper**, rather than via your tax return.

Our cost for dealing with your tax return will increase by virtue of you making EIS investments. The amount by which our costs increase will depend on your specific circumstances, namely whether your investment goes bad and, if so, whether you get back any value at all or nothing and on whether you also claim capital gains tax relief (see further below).

If the investment goes bad (and I am sure you are aware that being smallish companies, there is a risk of this and it does happen), a further income tax loss relief claim can be made – the extra tax relief we then claim for you, mitigates a little the monetary loss on the investment.

To the extent that you claim income tax relief on the investment, you can also claim capital gains tax deferral relief (assuming of course you have capital gains against which the relief can be set). Thus, in this example, if you have a capital gain of £25K or more, the full £25K can **DEFER** the CGT on the gain. It is though a deferral, not an exemption. Unfortunately, the gain which you defer is re-instated in the tax year in which the investment goes bad or is sold. But you can choose to rollover/defer the gain another time by investing again in another EIS investment. You can also EXEMPT the reinstated gain by investing in a SEIS company. N.B. The EIS/SEIS investments must be made no more than 1 year before or no more than 3 years after the date the gain arose for CGT deferral or exemption to apply.

Our extra costs are for the extra time keeping tabs of all the relevant dates, which investments go bad, making additional claims if they do. I would add that where you wish to make a claim (whether income tax or CGT) for a tax year where the return has already been submitted, as mentioned, this involves us having to submit paper claims and so adds to our additional costs. Nonetheless the overall tax benefits are still significantly more than our additional costs.

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