

What is EIS? Why is it of interest to both investors AND companies?

"EIS is a Government-sponsored financial incentive to invest in private company shares. It benefits investors and therefore companies seeking investment."

Summary of the main tax benefits

Investments made under the enterprise investment scheme ("EIS") qualify for certain tax advantages, the main ones being:

- income tax relief for the sum invested
- exemption from tax on capital gains on subsequent disposal
- deferral of the tax liability on other capital gains reinvested in EIS qualifying shares.

Income tax relief

An investor in shares issued by a qualifying company may claim to reduce his income tax liability for the year in which he makes the investment by an amount equal to 20% of the qualifying investment.

Exemption from tax on capital gains

Provided that the qualifying shares are held for more than three years, any capital gain arising on their disposal is exempt from capital gains tax. On the other hand, subject to certain restrictions, any loss arising on the sale of qualifying shares qualifies as an allowable capital loss to off-set against other capital gains or, in certain circumstances, may be relieved against taxable income.

Deferral of other capital gains

The capital gains tax liability arising on the disposal of any assets may be deferred to the extent that the proceeds are invested in a qualifying EIS company.

Claims

All claims for EIS relief must be made within five years after the normal self-assessment filing date for the tax year in question. The claim must be supported by a form EIS 3 issued by the company issuing the shares confirming entitlement to the relief. A company can only issue this certificate of entitlement on the specific authority of HMRC.

Summary of the main conditions for investment to qualify for EIS relief

Conditions concerning the issuing company

Independent company

The issuing company must be unquoted and not be under the control of any other company.

50 employees

The scheme is limited to companies or groups with no more than 50 full-time employees.

20% tax relief

"Income tax relief for 20% of amounts invested by outsiders in small companies and no capital gains tax on sale"

HMRC approval

"Each individual investment must be **certified by HMRC** as qualifying. If the investment meets the conditions, it will be approved"

Gross assets

The scheme is limited to companies or groups that have total gross assets not exceeding £7 million before the shares are issued and £8 million immediately afterwards.

Qualifying business activity

At the time of the share issue, either the issuing company or its 90% subsidiary must be either carrying on or preparing to carry on a qualifying trade mainly in the UK. A number of trades are specifically excluded but broadly qualifying activities are all business activities other than financial, property, agricultural and other land-based activities and those involving the provision of accommodation.

Conditions concerning the investor

Investor must not be connected with the company

In order to benefit from the income tax relief and capital gains exemption, the Investor must not be connected with the company as follows:

- Employee
- Partner of the issuing company
- Director who is remunerated for services except a "business angel".
- Person who possesses or is entitled to acquire 30% of the capital of the company.

This restriction does not apply to the deferral of other capital gains by reinvesting in EIS shares.

£500/£500,000 limits per individual

The current minimum qualifying investment by the investor in each company is £500 annually and the maximum total investment by the investor each year in respect of all qualifying investments is £500,000.

Further advice

The legislation is complex and includes many pitfalls for the unwary. The benefits are significant and worth the effort. If your company is considering issuing shares that may qualify for EIS relief or, having issued such shares, it is considering a change of business or share structure or you are considering investing in such shares, we should be pleased to provide the detailed, specific advice that you require. Alternatively, we would be pleased to send you a more detailed technical note on the scheme. Please speak to either your usual contact at Winter Rule or

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The rules covering EIS tax relief are detailed and complex. Whilst we have taken due care in the preparation of this statement of the benefits and requirements for qualification, it is of necessity abbreviated and does not address some of the conditions in sufficient detail to provide assurance that any particular issue of shares will qualify for the several reliefs or that, if granted, will not be withdrawn. Any company or other interested party should take specialist advice in relation to its own circumstances before proceeding. Winter Rule LLP, its partners and employees accept no responsibility for any loss arising to anyone acting or failing to act in reliance of the statements in this note.