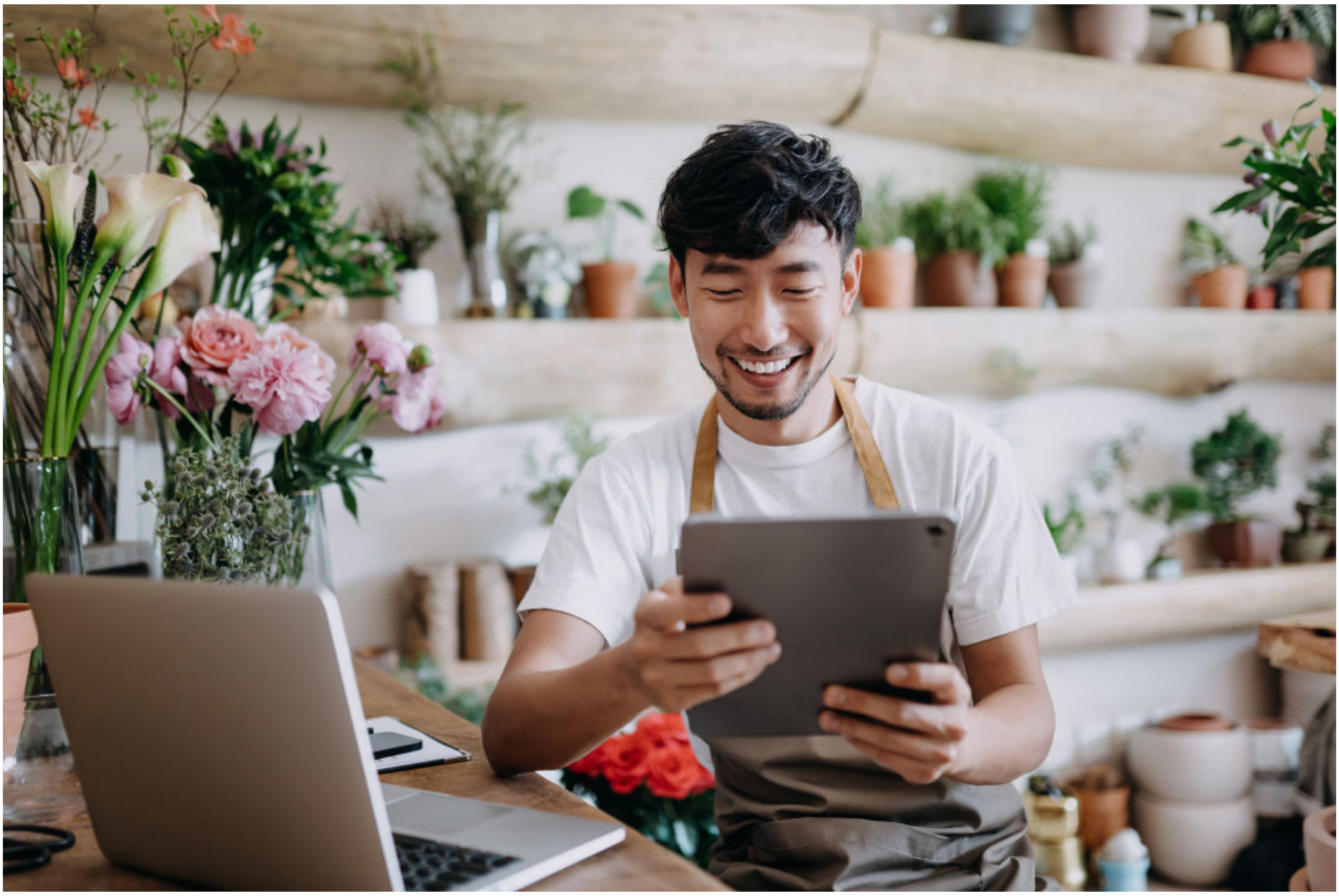
PKF FRANCIS CLARK

Shared Ambition

EIS and SEIS

Tax advantaged equity fundraising



For new businesses attracting investment is often a crucial factor in funding growth

The enterprise investment scheme (EIS) and seed enterprise investment scheme (SEIS) are generous government plans encouraging equity investment in new businesses by providing investors with significant income tax and capital gains tax (CGT) reliefs on their investments.

If you are planning to raise funds to aid business growth, ensuring your company qualifies as an EIS or SEIS investment may substantially increase your chances of attracting investors.

This guide will give you an overview of how these schemes operate, the conditions your business must meet, the process by which your investors obtain their reliefs and how PKF Francis Clark can help you every step of the way.

How the schemes work

Your business raises funds through the issue of shares to investors. Those investors can claim tax relief based on the amount they invest.

You must provide your investors with the forms they need to claim this tax relief. An application is made to HMRC to confirm that the conditions for relief under the appropriate scheme are met. HMRC will issue an EIS/SEIS2 certificate and EIS/SEIS3 form. The latter must be completed by the company and provided to the investor, who will then use it to claim their tax relief on that investment.

Investors must hold qualifying shares for a minimum of three years from the date of the share issue or commencement of the company's qualifying trade. Losing EIS or SEIS qualifying status during this period would adversely affect your investors' ability to claim relief and may result in provisional relief being clawed back.

The EIS and venture capital trust (VCT) tax relief will now be available beyond 2025 (when the original EIS/VCT sunset clause expires).

What is the difference between EIS and SEIS?

SEIS is designed to help early stage businesses attract seed funding. More mature companies can raise larger sums through EIS. Each scheme has different qualifying criteria and offer different levels of tax relief.

The tax reliefs available to investors under SEIS are more generous than those offered by EIS.

SEIS

- Income tax relief of up to 50% of the amount invested, up to an annual subscription limit of £100,000 up to an annual subscription limit of £200,000
- Exemption from CGT on gains from disposals of SEIS shares after three years
- Exemption from CGT on gains from the disposal of any asset of up to 50% of their subscriptions in SEIS shares during the same tax year
- Losses on disposals of SEIS are allowable for CGT purposes
- Business property relief (BPR) on SEIS investments after two years of ownership
- The company has an investment limit of £250,000

EIS

- Income tax relief of up to 30% on the amount invested
- Disposals of EIS shares after three years may be exempt from CGT
- CGT deferral relief allows investors disposing of any asset to defer gains against subscriptions in EIS shares
- Losses on EIS shares may be offset against taxable income
- EIS investments should qualify for BPR after two years of ownership

Both regimes are highly prescriptive and numerous stringent requirements must be met in order to ensure that tax relief is available to your investors. Conditions relate to the company, the issued shares, the funds raised and the individual investors themselves in order to ensure your investors qualify for tax relief under the appropriate scheme.

Qualifying criteria for businesses to qualify for EIS and SEIS

EIS

The issuing company (together with any qualifying subsidiaries) must have:

- Gross assets of no more than £15m immediately before, and no more than £16m immediately after, the shares are issued
- Fewer than 250 full-time employees (or 500 if a knowledge intensive company (KIC))
- The company must meet the permitted maximum age requirements. This means that EIS shares cannot usually be issued more than seven years from the first commercial sale by the company (10 years for a KIC). No more than £350,000 in gross assets

SEIS

- No more than £200,000 in gross assets (to increase to £350,000 from April 2023)
- Fewer than 25 employees
- Not previously carried out a different trade SEIS
- New qualifying trade of up to three years

Applying for EIS and SEIS approval

Changes have been made to each scheme since they were first introduced. The increasing number of qualifying conditions, which have to be met, need consideration when preparing an application for HMRC approval.

In particular, following changes to the law introduced with effect from 18 November 2015, applicants need to demonstrate how EIS and SEIS funds will be used and how this will lead to the growth and development of the business.

Additionally, for shares issued on or after 15 March 2018, applicants must show that the investment carries a significant risk and that an investor could suffer a loss of capital of an amount exceeding the net investment return (including tax relief on the investment, distributions from the company and capital growth on the shares).

HMRC therefore expects applications to be supported by a business plan and financial forecast appropriate to the level of funds being sought. Those forecasts need to show how the raising of funds are part of the business plan and strategy to grow and develop the business over the long term.

The level of detail in a business plan will depend on the size and development stage of the company and the amount of investment that is being sought.

We can review and assist in the preparation of the supporting documents to ensure they are appropriately drafted.

Advance assurance

Full EIS and SEIS eligibility can only be granted by HMRC after the investment is made, so an advance assurance process was introduced to give businesses a provisional indication that they may be able to apply for tax relief for their investors.

Many investors will expect you to have obtained advance assurance from HMRC before agreeing to invest in your business, indeed some crowdfunding platforms now insist it is obtained before a funding campaign can commence.

We can assist in preparing the information required by HMRC in order to obtain advance assurance and manage the application process to ensure that it goes as smoothly as possible.

Share incentives for staff

For the directors and senior management of a business there is often a direct link between their actions and the value of the company. If the management team has a stake in the company they are directly aligned to growing the value of the whole company for the benefit of all shareholders.

Other than in limited circumstances directors and employees cannot benefit from SEIS or EIS tax reliefs when investing in their employer company. However, there are a number of ways in which employees can be incentivised through share based rewards either by acquiring shares outright, being given the right to acquire shares in the future, or cash bonus arrangements that track share price growth.

At PKF Francis Clark we have a dedicated team of specialists with experience of designing the right solution for your business.

Enhanced tax relief for expenditure on qualifying research and development

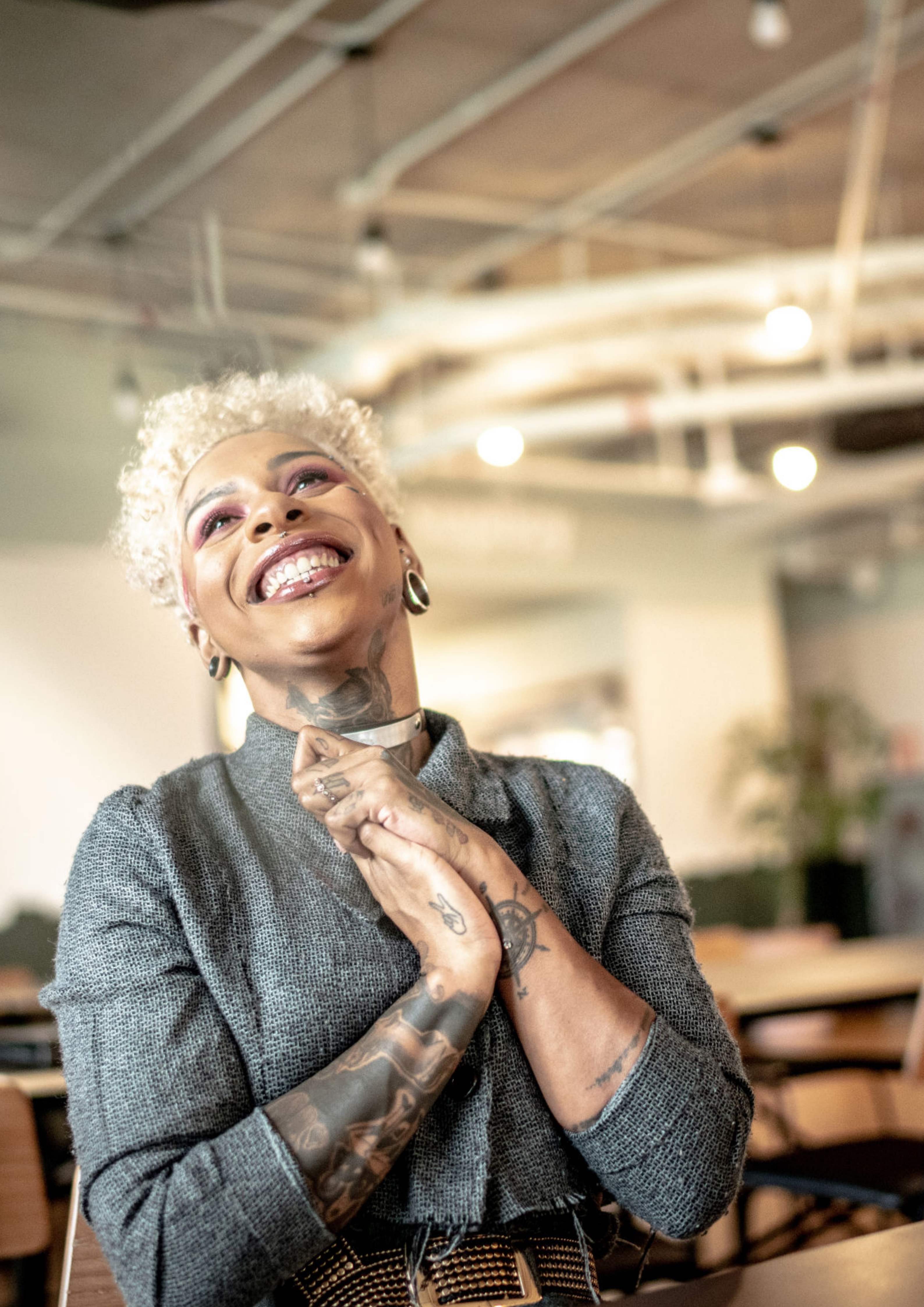
EIS and SEIS are attractive to investors and qualifying status can improve your business' prospects of attracting external investment. Innovative companies should also consider taking advantage of tax reliefs available for expenditure on qualifying research and development activities.

The Government regards investment in research and development (R&D) as crucial to economic success. R&D tax relief is designed as an incentive for UK companies to invest in innovation. The relief can be extremely generous and enables the company to accelerate its R&D programme and invest a greater proportion of its profits into such things as hiring new staff.

Under the R&D tax relief scheme applicable to small and medium sized companies, profit making companies claim an enhanced deduction against their taxable profits, resulting in an additional reduction in corporation tax of the expenditure. For loss making companies, the loss can be 'surrendered' in return for a cash payment of the expenditure. In certain situations a claim may only or partially be made under the 'RDEC' regime, which is less beneficial.

Claims can be made up to two years after the end of the accounting period in which the qualifying expenditure was incurred.

Our specialist R&D tax relief team, comprised of tax specialists and a time served engineer, has a proven track record of successful claims across many sectors. We will ensure that the claim includes all applicable costs in order to maximise the value of relief.



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How PKF Francis Clark can help

If your business is seeking equity investment we can advise on eligibility, prepare applications for advance assurance and manage the process of obtaining EIS and SEIS compliance statements for your investors.

Ensuring that the company continues to meet the scheme conditions throughout the qualifying investment period is critical to ensuring that your investors receive the maximum available tax relief. Our teams of experienced professionals will work with you to ensure that that relief is not inadvertently lost.

Our teams also include specialists who are able to advise on share-based staff incentives and the availability of R&D tax relief.

Stuart Rogers
Partner & Head of Innovation Tax Group
E: stuart.rogers@pkf-francisclark.co.uk
T: 0177 403 9814

Nicola Manclark
Corporate Tax Partner
E: nicola.manclark@pkf-francisclark.co.uk
T: 0117 403 9807

Kate Culley
Tax Senior Manager
E: kate.culley@pkf-francisclark.co.uk
T: 01803 221818

Douglas Oakman
Tax Manager
E: douglas.oakman@pkf-francisclark.co.uk
T: 01823 697101

Thomas Oldham
Tax Consultant
E: thomas.oldham@pkf-francisclark.co.uk
T: 01392 351813