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EIS and SEIS - The Basics

EIS and SEIS regimes are designed to help smaller high-risk trading companies (broadly start-up companies) to raise finance by offering a range of tax relief to investors. There are several rules that must be adhered to by the investor for the scheme to be successful and to retain any relevant tax reliefs.

Enterprise Investment Scheme

The company must meet several conditions and cannot apply for EIS status until it has been trading for at least 4 months.

Company

- Generally, the company must be an unquoted trading company and must not be controlled by another company i.e. a subsidiary of a parent company cannot be within the scheme. However, a parent company can be within the scheme providing its subsidiary is a trading company and it holds more than 90% of its ordinary share capital.
- Gross assets of the company must be less than £15m prior to EIS investment and less than £16m following investment. The maximum amount of money a company can raise under the scheme in a 12 month period is £5m and it cannot raise more than £12m of investment during its lifetime.
- The company must have less than 250 full time equivalent employees.
- The money raised must be used for the trade within 2 years of the shares being issued.
- The company must be running a commercial trade and certain businesses are excluded, including:
  1. Dealing in land/shares
  2. Legal and accountancy services
  3. Financial activities e.g. insurance
  4. Farming or market gardening
  5. Property development
  6. Nursing homes

  The company can carry on these activities alongside another qualifying trade as long as the activity is minimal i.e. less than 20% of the overall business.
- A company can receive investment under EIS as long as it's made within 7 years of the company's first commercial sale. Investments made after this time are unlikely to qualify.
- Knowledge intensive companies can raise up to £10m in a year and £20m over its lifetime. These companies also benefit from a 10 year initial investing period and a higher employee limit of 499.

Income tax relief

EIS shares must be fully paid up ordinary shares with no preferential rights and should be held for at least 3 years for income and capital gains tax reliefs to apply.
Relief from income tax is available as follows:

- 30% of a maximum investment of £1m is available as income tax relief. The relief acts as a tax reducer i.e. 30% of the investment is deducted from individual's tax liability. If the income tax relief exceeds the individual's liability, no repayment of the tax relief can be made and the remaining EIS relief is potentially wasted.
- An individual can elect to carry back the income tax relief and use it in the previous tax year if this would be more beneficial e.g. they have a higher income tax liability.
- The investor cannot be an employee and must hold less than 30% of the shares in the company. If more than 30% is owned, the investor is 'connected' and EIS relief cannot apply. It may be possible for an investor to become a director of the company.
- If an investor already holds shares in a company in which they wish to invest under EIS, the existing shares must either be:
  1. Subscriber shares, or
  2. Shares that qualify for EIS/SEIS relief.

  If any individual holds any shares other than those mentioned above, future investment is unlikely to qualify for EIS status.
- Dividends paid by the company are taxable.
- All shares must be full risk and a 'risk to capital' condition must be met. The issuing company must intend to grow and develop its trade in the long term and there must be a significant risk of a capital loss exceeding the net investment return.

Capital gains tax relief

- Any gain on the disposal of EIS shares may be exempt providing the shares have been held for more than 3 years and income tax relief has not been withdrawn. If income tax relief was not claimed on investment, no capital gains tax exemption applies.
- If a loss is made on the disposal of EIS shares, this loss (less any income tax relief given) may be offset against general income.
- CGT deferral relief – If an individual disposes of any asset and invests into qualifying EIS shares, the gain on the asset may be deferred and will come back into charge when the EIS shares are sold. Every £1 of EIS investment will attract £1 of gain deferral e.g. if a £20,000 gain is made and £10,000 is invested into EIS shares, £10,000 of the gain will be chargeable on the disposal of the original asset with the remaining £10,000 deferred until the EIS shares are sold at which point the deferred gain comes back into charge.

Time limits apply to deferral relief.

Seed Enterprise Investment Scheme

The SEIS regime has very similar rules to the EIS regime but is designed to help very small businesses. Changes to the SEIS regime were announced in the last Budget and are due to come into effect from April 2023. The notable differences between the SEIS and EIS regimes are as follows:

Income tax relief

- Until 5 April 2023: 50% of a maximum investment of £100,000 per annum is available as income tax relief. The relief acts as a tax reducer as detailed above.
- From 6 April 2023: 50% of a maximum investment of £200,000 per annum is available as income tax relief. The relief acts as a tax reducer as detailed above.

Capital gains tax relief

- If an asset is sold and an individual makes an investment into SEIS shares, up to 50% of the investment may qualify for reinvestment relief, effectively removing some of the gain arising from the charge to capital gains tax altogether. Time limits apply to this relief.

No changes have been made to this relief.

Company

Rules until 5 April 2023

Gross assets of the company must be less than £200,000 prior to investment and the funds raised must be used for the purpose of the trade within 3 years of receipt.

- The company must have less than 25 full time equivalent employees.
- The maximum amount of money a company can raise under the scheme in a 12 month period is £150,000.
- The qualifying trade must have been carried on for less than 2 years prior to investment.
- Shares are unlikely to qualify for SEIS relief if the company has already received investment under EIS.

Rules from 6 April 2023

Gross assets of the company must be less than £350,000 prior to investment and the funds raised must be used for the purpose of the trade within 3 years of receipt.

- The company must have less than 25 full time equivalent employees.
- The maximum amount of money a company can raise under the scheme in a 12 month period is £250,000.
- The qualifying trade must have been carried on for less than 3 years prior to investment.
- Shares are unlikely to qualify for SEIS relief if the company has already received investment under EIS.

A company may utilise the SEIS and EIS regimes but care should be taken to ensure time limits and thresholds are adhered to.